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COMMISSIONERS

JEFF HATCH-MILLER, Chairman
WILLIAM A. MUNDELL
MARC SPITZER
MIKE GLEASON
KRISTIN K. MAYES

ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, AZ 85007

**Re: Response to requests for additional information from Renewable Energy
Standard and Tariff hearing on May 23, 2006;
Docket No. RE-00000C-05-0030**

Dear Commissioners:

As part of the Renewable Energy Standard and Tariff (RES) rule development process, a public hearing was held on May 23, 2006. During that hearing, Arizona Public Service (APS) was asked to provide additional written information before the next public hearing on June 5, 2006. This letter provides the requested information.

Historical EPS Expenditures and CPP Funding

Commissioner Mundell requested information regarding historical funding for the APS' Environmental Portfolio Standard (EPS) and the Credit Purchase Program (CPP). The requested information is provided as Exhibit 1.

Estimated Cost for Compliance

During the hearing, APS stated that the estimated total cost of compliance with the RES was expected to average between \$60 and \$75 million through 2010. APS estimates that the cost of complying with the entire RES over the next three years (2007-2009) will average between \$50 and \$60 million annually. APS believes it is more appropriate to focus on RES compliance cost estimates in the near term. Compliance costs are anticipated to increase more rapidly in later years as the RES requirement begins to increase and become a larger fraction of APS' total retail energy sales.

APS estimated compliance cost for the non-distributed fraction of the RES based on experience gained from existing or recently signed power purchase agreements. APS estimates the cost for complying with the non-distributed portion of the RES to average about \$15 to \$20 million per year through 2009.

The majority of the cost for compliance with the Renewable Energy Standard is expected to go towards meeting the distributed energy requirement. For the next three years the cost for compliance with the distributed energy requirement is expected to average between approximately \$35 and \$40 million per year. At this point no one can accurately forecast all costs for complying with the distributed requirement because of uncertainties surrounding the incentive programs, the availability of new technologies, customer adoption rates for new and existing technologies, and the size and ultimate distribution of those resources. APS' compliance cost estimates include only the costs associated with technology incentives; they do not include any integration costs described below for non-distributed resources. In the near-term, APS does not believe that integration costs associated with distributed resources represent a significant cost of complying with the distributed energy requirement.

Distributed energy incentive structures and incentive levels for distributed generation technologies are being developed as part of the Uniform Credit Purchase Program (UCPP) working group. The UCPP working group only recently began to work on incentives levels and incentive structures and has not yet begun to address issues of incentive allocation.

Absent known incentives, APS estimated compliance costs for distributed generation based on the existing incentives for photovoltaic (PV) systems, which have accounted for about 80 percent of all energy obtained from distributed installations from 2002-2005. These cost estimates may change if, after the UCPP working group has completed its recommendations, the market and incentive for other technologies present lower cost means of achieving the distributed energy requirement. The working group's efforts are scheduled for completion in July 2006.

System Integration Costs

During the May 23rd hearing, Chairman Hatch-Miller asked whether all costs had been considered as part of the estimate for RES compliance. APS' estimated cost for non-distributed RES compliance is intended to include all costs for such renewable resources over and above the cost of the conventional resource alternative. The two primary costs that must be considered in the economic analysis of renewable resources are spinning reserves (for intermittent resources) and transmission costs. In determining the cost of any intermittent renewable project, APS includes a cost for spinning reserve in order to balance the volatility of the intermittent resource. In addition, APS includes the cost for transmitting the electricity to its load centers in its economic evaluations, both for

conventional and renewable resources. In estimating the compliance cost for RES, the transmission cost for generic conventional and renewable resources was unknown so no distinction was made and no cost differential was included.

Tariff Alternatives

Chairman Hatch-Miller requested that APS estimate the rates within the tariff rate schedule required to achieve the necessary cost recovery. APS has provided the estimated rates necessary to collect the revenue to comply with the RES for the next three years as Exhibit 2. That exhibit details the kWh rate and monthly cap for each of the three customer categories for recovery of \$50 million and \$60 million, reflecting the range of costs estimated by APS. Estimated annual percentage increases also are included based on average use as indicated in Note 4. The charges and caps were designed to maintain the proportionality between customer classes in accordance with Decision No. 67744.

Sincerely,



Barbara Lockwood, P.E.
Manager, Renewable Energy

EXHIBIT 1:

	EPS Revenue ¹	Credit Purchase Program Expenditures ²
2002	\$12,589,152	\$59,050
2003	\$12,799,400	\$303,271
2004	\$13,043,206	\$933,462
2005	\$13,320,775	\$4,093,774
Total	\$51,752,533	\$5,389,557

¹ Includes \$6,000,000 SBC Revenue + EPS Surcharge Funds

² 2005 Expenditures include \$1,370,949 in anticipated payout for reservations for which systems have not yet been installed

ARIZONA PUBLIC SERVICE COMPANY
RES Surcharge Estimates

	ACC Staff Sample			APS Equivalent (3.90 x) ¹			\$50 million (6.14 x) ²			\$60 million (7.54 x) ³		
	kWh Rate	Monthly Cap	Annual Incr. ⁴	kWh Rate	Monthly Cap	Annual Incr. ⁴	kWh Rate	Monthly Cap	Annual Incr. ⁴	kWh Rate	Monthly Cap	Annual Incr. ⁴
Residential	\$ 0.004988	\$1.05	0.66%	\$ 0.003325	\$ 1.33	0.66%	\$ 0.005373	\$ 2.15	1.21%	\$ 0.006598	\$ 2.64	1.54%
Non-Residential < 3,000 kW	\$ 0.004988	\$39.00	2.20%	\$ 0.003325	\$ 49.40	2.20%	\$ 0.005373	\$ 79.82	4.04%	\$ 0.006598	\$ 96.02	5.14%
Non-Residential > 3,000 kW	\$ 0.004988	\$117.00	0.04%	\$ 0.003325	\$ 148.00	0.04%	\$ 0.005373	\$ 239.40	0.08%	\$ 0.006598	\$ 294.06	0.10%

Note 1: APS equivalent designed to collect revenue equal to ACC Staff RES Sample Tariff (\$29 million which excludes \$6 million in base rates). Multiple is based on current effective tariff.

	kWh Rate	Monthly Cap
Residential	\$ 0.000875	\$ 0.35
Non-Residential < 3,000 kW	\$ 0.000875	\$ 13.00
Non-Residential > 3,000 kW	\$ 0.000875	\$ 39.00

Note 2: Assumes \$6 million in base rates and \$44 million collected from RES surcharge. Multiple is based on current effective tariff.
 Note 3: Assumes \$6 million in base rates and \$54 million collected from RES surcharge. Multiple is based on current effective tariff.
 Note 4: Based on annual usage as follows (% increase will vary by usage):

	kWh
Residential	16,000
Non-Residential < 3,000 kW	49,500
Non-Residential > 3,000 kW	43,600,000