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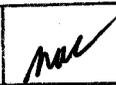
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BEFORE THE ARIZONA CORPORATION COMMISSION

MARC SPITZER
Chairman
WILLIAM A. MUNDELL
Commissioner
JIM IRVIN
Commissioner
JEFF HATCH-MILLER
Commissioner
MIKE GLEASON
Commissioner

Arizona Corporation Commission
DOCKETED

APR 04 2003

DOCKETED BY 

IN THE MATTER OF THE APPLICATION
OF SOUTHWEST GAS CORPORATION
FOR APPROVAL OF ACQUISITION PLAN
AND, IF APPROPRIATE, WAIVER
SELECTED PROVISION OF THE
AFFILIATE RULES

DOCKET NO. G-01551A-02-0425

**BLACK MOUNTAIN GAS POST -
HEARING BRIEF**

Black Mountain Gas Company ("BMG") hereby submits the following post-hearing brief in support of the Southwest Gas Corporation's ("Southwest") acquisition plan. In its brief, BMG limits its remarks to the issues of (1) whether the acquisition is in the public interest, (2) whether the Arizona Corporation Commission Utility Division Staff ("Staff") correctly applied the relevant standard for approving a stock purchase agreement between two Arizona public utility companies, and (3) whether the proposed condition requiring BMG's customers to pay Southwest rates prior to Southwest's next general rate case exceeds the Arizona Corporation Commission's ("Commission") authority.

I.
THE PROPOSED ACQUISITION IS IN THE PUBLIC INTEREST.

Southwest has proposed the acquisition of all of BMG's stock and its associated Certificate of Convenience and Necessity ("CC&N") and the ultimate merger of BMG into Southwest. BMG is the smallest utility subsidiary of Xcel Energy, Inc. ("Xcel"), a Minnesota corporation owning 100 percent of outstanding shares of stock in BMG, and

1 is somewhat geographically remote from the other utility systems. (Public Service
2 Company of Colorado serves portions of Colorado, and Southwestern Public Service
3 Company provides electric service in eastern New Mexico.) Southwest provides a good
4 fit for the BMG's natural gas utility operation in Cave Creek because Southwest's
5 headquarters in Las Vegas and its large Arizona operations are geographically closer
6 than Minnesota. In fact, Southwest almost surrounds BMG's natural gas service area,
7 and BMG purchases a portion of its natural gas supply from Southwest.¹ BMG Reiber
8 Rebuttal at 2.

9 Although, BMG provides a safe, reliable natural gas service at a reasonable cost,
10 the reality is that there are several programs conducted by Southwest that are not now
11 available to BMG customers due to the size of BMG's Cave Creek Operations. BMG's
12 current customers in the Cave Creek operating area would begin to enjoy the benefits of
13 those programs immediately upon consummation of the stock purchase transaction. As
14 stated by Southwest, this transaction is similar in size or materiality to Southwest
15 extending service to a new subdivision or development. Southwest Janov Rebuttal at 5;
16 see *also* RUCO Testimony of Rodney Moore at 7-8. The Cave Creek customers would
17 have access to Southwest programs such as summary billing, core aggregation, e-
18 billing, low-income assistance programs, automated account systems, and defined
19 customer-appointment windows. Burke Rebuttal at 12.

20 In addition, consummation of the stock purchase transaction would have no
21 discernible impact on the Page Division propane customers. As reflected in Southwest's
22 Application, the Page Division operations would continue "business as usual" by
23 Southwest until such time as Southwest markets the Page Division properties;

24
25 ¹ In addition, Staff testified that Southwest has "at least the same financial capability as Xcel." Reiker
26 Direct at 11. Moreover, both Southwest (one complaint per 10,000 customers from 2000-2003) and BMG
(eight complaints per 10,000 customers from 2000-2003) provide a comparable and high level of customer
service. *Id.* at 12; see *also* RUCO, Moore Direct at 20-22.

1 scheduled to begin immediately upon consummation of the stock purchase transaction.
2 Janov Rebuttal at 9. Southwest has already identified a number of potential buyers for
3 the propane operations, which it anticipates accomplishing within a year of finalizing this
4 transaction. Further, so long as the Page Division properties are owned by Southwest,
5 the operations will be conducted separately and the change in ownership is expected to
6 be transparent to current BMG Page customers.

7 As the witness for RUCO also recognized, Southwest is a proper company to
8 acquire and operate BMG, and it's acquisition of BMG is consistent with the public
9 interest. Moore Direct at 22-23.

10 **II.**
11 **ADDITIONAL, TANGIBLE PUBLIC BENEFITS ARE NOT REQUIRED FOR**
12 **APPROVAL OF THE PROPOSED STOCK PURCHASE TRANSACTION.**

13 Southwest has requested approval by the Commission pursuant to A.R.S. § 40-
14 285(A) and (D). They have also requested approval or waiver under Arizona's Affiliate
15 Rules (Arizona Administrative Code R14-2-801, et seq.) if the Commission concludes
16 that Southwest's acquisition of Xcel's BMG shares (1) constitutes the utilization of funds
17 to form a subsidiary, (2) constitutes the reorganization of a public utility holding
18 company, or (3) constitutes the divestiture of an established subsidiary. Staff Reiker
19 Direct at 4; Moore Direct at 3. Staff has requested the imposition of 14 conditions on any
20 approval to "ensure" what Staff has characterized as "obvious and significant immediate
21 consumer benefit." Reiker at 13. In doing so, Staff wholly misconstrues the applicable
22 standards of review for approval of Southwest's application. Regardless of whether
23 the proposed transaction is approved under A.R.S. § 40-285(A) and (D) as an
24 acquisition or under the Affiliate Rules as a reorganization or divestiture, the Commission
25 would exceed its authority by extracting conditions to meet a standard not required
26 under Arizona law, particularly since no actual detriment has been found either by RUCO
or by Staff in this proceeding.

1 A.R.S § 40-285 requires Commission approval for the acquisition or sale of a
2 public utility company. While no standard for approval is set forth in the statute, the
3 Arizona Court of Appeals determined that approval by the Commission for transfer of
4 assets and the CC&N of one public utility to another public utility is whether or not the
5 transfer is "detrimental to the public interest." See *Pueblo del Sol Water Co. v. Arizona*
6 *Corp. Comm'n*, 160 Ariz. 285, 286, 772 P.2d 1138, 1130 (App. 1988). In so holding, the
7 Court in *Pueblo del Sol* essentially equated the "public interest" with a lack of detriment
8 to the public, or a "no harm" standard. *Id.*

9 Similarly, in *Arizona Public Service Co. v. Mountain States Tel. & Tel. Co.*, 149
10 Ariz. 239, 717 P.2d 918 (App. 1985), the Arizona Court of Appeals examined a
11 transaction between two utilities concerning joint utility pole rentals. Although it
12 eventually determined that A.R.S. § 40-285 did not apply, it noted that the purpose of the
13 statute was "to prevent a utility from disposing of resources devoted to providing its utility
14 service, thereby 'looting' its facilities and impairing its service to the public." *Id.* at 242,
15 717 P.2d at 921. The clear implication of such a statement is that where it can be shown
16 that a transaction has not impaired service to the public, the Commission cannot, nor
17 does the statute authorize the Commission to, deny the approval of transaction.

18 In Arizona Attorney General Opinion No. 62-7, the Attorney General concluded
19 that prior approval provisions such as A.R.S. § 40-285 were "permissive statutes passed
20 for the protection of the public interest" and to determine whether or not "the proposed
21 transfer will be injurious to the rights of the public." Op. Atty. Gen. No. 62-7, at 22. The
22 Opinion goes on to say that the Commission's authority to deny a proposed purchase or
23 sale extended solely to transactions "injurious to the rights of the public." *Id.* Thus,
24 when a transaction, such as Southwest's acquisition, is not injurious to or does not harm
25 the public, the Commission's approval is required. There is simply no requirement under
26 any of these authorities that there be an "obvious and significant immediate consumer

1 benefit” as Staff now suggests.

2 Like the Arizona Appellate Court and the Attorney General, the Commission has
3 determined that “public interest” equates to a lack of detriment or “no harm” standard
4 through promulgation of its Affiliate Rules. The Affiliate rules clearly set forth a standard
5 for review of transactions under A.A.C. R14-2-803, which is not the “obvious and
6 significant immediate consumer benefit” standard proposed by Staff. Under the Affiliate
7 Rules, the Commission must approve this transaction unless one of the following is
8 demonstrated by the evidence presented at the hearing: (a) the transaction would impair
9 the financial status of a public utility; (b) the transaction would otherwise prevent a public
10 utility from attracting capital at fair and reasonable terms; or (c) the transaction would
11 impair the ability of a public utility to provide safe, reasonable and adequate service.
12 See A.A.C. R14-2-803(C) and R14-2-804(C). Waiver of the Affiliate Rules by the
13 Commission is proper if “such a waiver is in the public interest.” A.A.C. R14-2-806(A).

14 Unless the Commission determines that one or more of the criteria set forth in the
15 Affiliate Rules exist, the transaction must be approved as in the public interest. Put
16 another way, if a proposed formation or reorganization of a utility holding company²
17 would have a neutral impact on the affiliated Arizona utility, the Commission cannot,
18 under the “no detriment/no harm” standard, reject the acquisition of BMG’s stock by
19 Southwest and its interim reorganization or use Southwest’s application as a basis to
20 extract conditions on the local utility. There is simply no basis under the Affiliate Rules
21 (or the applicable statutes) for Staff to propose or the Commission to adopt additional
22 conditions upon such a transfer.

23 In this case, there was no evidence that the transaction would impair the financial
24 status of Southwest. Reiker Direct at 11. Further, there was no evidence that the

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26 ² Under R14-2-801, Southwest would be defined as a “public utility holding company” until such time after
the stock purchase as BMG is dissolved. Reiker Direct at 13-14.

1 transaction would prevent Southwest from attracting capital at fair and reasonable terms
2 (which is inconceivable given the relative sizes of BMG and Southwest). Reiker Direct at
3 7-8. In fact, to the extent the transaction affects Southwest's ability to attract capital, that
4 impact would be positive based on Xcel's lower market risk assessment. *Id.* at 9, 11.
5 Finally, there was no evidence that the transaction would impair Southwest's ability to
6 provide safe, reasonable and adequate service within Arizona or in BMG's service
7 territory. The transaction will not result in a detriment to the public, and the evidence in
8 the record supports that the criteria set forth in R14-2-803(C) and 804(C) have been
9 satisfied. Therefore, the Commission has no basis for imposing the conditions proposed
10 by Staff for the sole purpose of establishing "obvious and significant immediate
11 consumer benefit" not required by law.

12 This analysis answers the question asked by the Administrative Law Judge
13 ("ALJ") during the hearing on this application – if two equally qualified companies want to
14 transfer a utility subsidiary's territory or groups of customers from one to another, how
15 does the Commission evaluate that transfer? Transcript of Hearing, Vol. II (March 3,
16 2003) at 371-72. The answer is not as Staff suggested, "if everything is exactly equal"
17 (which it will not be), the desire of one company to serve the area and the desire of the
18 other to sell its assets creates the obvious and significant public benefit. *Id.* Rather, the
19 answer to that question is if two companies wish to transfer a subsidiary's service
20 territory or a group of customers, the transfer should be approved unless the
21 Commission finds that the transaction creates a detriment to the public, the transferred
22 customers, or the customers of the acquiring or transferring entity. *Cf.* Op. Atty. Gen.
23 No. 62-7, at 22. The applicable statutes and the Affiliate Rules require the Commission
24 to determine if the public will be harmed by the transaction. If the transaction creates no
25 detriment, it should be approved and no additional conditions may or should be imposed
26 upon it. It is the opinion of Southwest, the AUIA and BMG that the Affiliate Rules are not

1 intended to provide an opportunity for Commission Staff to exact concessions from
2 utilities that are not otherwise authorized under the Arizona Constitution and statutes
3 governing the Commission.

4 **III.**
5 **STAFF'S RATE PROPOSAL WOULD EXCEED THE COMMISSION'S AUTHORITY**

6 Southwest Gas proposed that the current rates and charges established for
7 BMG's Cave Creek Division remain in effect for new and existing customers until the
8 next Southwest general rate case.³ BMG concurs with Southwest's position and further
9 believes the current rates to be just and reasonable as determined by the commission in
10 Decision #63545 and should not be changed outside of a rate case. In response, Staff
11 recommends that upon the dissolution of BMG (on or before July 1, 2004), the tariffed
12 rates and charges for Southwest "be deemed the authorized rates and charges for Cave
13 Creek Division customers' effective the noticed date of BMG's dissolution." Staff Gray
14 Direct at 3. Mr. Gray explains the basis of Staff's recommendation to be that because
15 Southwest's tariffed rates and charges are lower than those of BMG's, "[c]ontinued
16 application of higher Black Mountain margins to Cave Creek Division customers after
17 Black Mountain is dissolved into Southwest would inequitably burden the former Cave
18 Creek customers with higher rates than any other similarly situated Southwest
19 customers in Arizona are paying . . ." *Id.* RUCO, the AUIA, BMG and Southwest
20 oppose Staff's recommendation because, if adopted, it would change rates outside a
21 rate case. Arizona courts have repeatedly held that such actions are impermissible and
22 violate Arizona's Constitution.

23 The Commission's rate-making authority is subject to the "just and reasonable"
24 clauses of Article 15, Section 3 of the Arizona Constitution. Under most circumstances,

25 ³ These rates were established by the Commission in Decision No. 63545, *In the Matter*
26 *of the Applications of Black Mountain gas Company, Cave Creek operations, for a*
Hearing to Determine the Earnings, Etc., Docket No. G-03703A-00-0283 (March 30,
2001).

1 the Commission is prohibited from either increasing or decreasing a public service
2 corporation's rates without first determining "fair value". See Ariz. Const. Art. XV, §§ 3,
3 14; *Simms v. Round Valley Light & Power Co.*, 80 Ariz. 145, 294 P.2d 378 (1956);
4 *Scates v. Arizona Corp. Comm'n*, 118 Ariz 531, 578 P.2d 612 (App. 1978). In *Simms*, a
5 power company challenged the Commission's authority to reduce its rates. The Arizona
6 Supreme Court unequivocally held that before the Commission may reduce a utility's
7 rates, it must ascertain the fair value of the company's property and employ that value in
8 establishing rates. See *id.* at 151, 294 P.2d at 382.

9 [U]nder our constitution as interpreted by this court, the commission is
10 required to find the fair value of the company's property and use such
11 finding as a rate base for the purpose of calculating what are just and
12 reasonable rates. . . . While our constitution does not establish a formula
13 for arriving at fair value, it does require such value to be found and used as
14 the base in fixing rates. The reasonableness and justness of the rates must
15 be related to this finding of fair value.

16 *Id.*

17 In *Scates*, the Commission granted Mountain Bell permission to increase charges
18 for installation, moving and changing of telephones without determining the fair value of
19 the company's rate base and without considering the effect of the increase on the
20 company's overall rate of return. 118 Ariz. at 533, 578 P.2d at 614. The Court of
21 Appeals reversed the Commission's decision finding that it failed to satisfy Arizona's
22 constitutional requirements. *Id.* at 537, 578 P.2d at 618. "We . . . hold that the
23 Commission was without authority to increase the rate without any consideration of the
24 overall impact of that rate increase upon the return of Mountain States, and without, as
25 specifically required by our law, a determination of Mountain States' rate base." *Id.*

26 The Arizona Supreme Court has recently enforced the constitutional provisions
requiring the Commission to conduct fair value determinations before establishing utility
rates. See *U S WEST Communications, Inc. v. Arizona Corp. Comm'n*, 201 Ariz. 242,

1 34 P.3d 351 (2001). In this recent U S WEST case, the Commission granted CC&N's to
2 competitors of U S WEST and permitted those companies to set initial rates for their
3 services without ascertaining the fair value of the competitors' rate base. The Supreme
4 Court rejected the regime created by the Commission that permitted these public service
5 corporations to establish initial rates, including maximum and minimum rates, and then
6 raise the maximum and minimum rates without a finding of fair value. *Id.* at 245-46, 20
7 P.3d at 354-55.

8 In this case, the Staff's recommendation fails to satisfy Arizona's constitutional
9 requirements as articulated in *Simms* and *Scates*. Staff would have the Commission
10 authorize a rate decrease without having conducted a fair value analysis of Southwest
11 Gas' rate base and without having considered the effect of the decrease on Southwest
12 Gas' rate of return.

13 In limited circumstances, the Commission can exercise its authority when rates
14 are predicated on an emergency basis or when the rate changes are pursuant to an
15 automatic adjustment clause. See *Scates*, 118 Ariz. at 535, 578 P.2d at 616. According
16 to *Scates*, and the Attorney General Opinion cited therein, the Commission may
17 establish *interim* rates in an emergency situation, so long as appropriate safeguards are
18 in place. See *id.* citing 71-17 Op. Att'y Gen. (1971). This case, however, does not fall
19 within the narrow parameters of the *Scates* exception because: (1) Staff presented no
20 evidence that an emergency existed; and (2) Staff's recommendation would establish
21 permanent, not interim rates.

22 Neither does Staff's recommendation constitute the type of automatic adjustment
23 contemplated under *Scates*. "An automatic adjustment clause is generally established
24 by the Commission as part of a utility's overall rate structure. It is usually established
25 during a full rate hearing to allow a utility to decrease rates automatically 'in relation to
26 fluctuations in certain, narrowly defined, operating expenses.'" *Residential Utility*

1 *Consumer Office v. Arizona Corp. Comm'n*, 199 Ariz. 588, 591-92, 20 P.3d 1160,
2 1172-73 (App. 2001) *citing Scates*, 118 Ariz. at 535, 578 P.2d at 616. In this case,
3 Staff's recommendation cannot be characterized as an "automatic adjustor" because no
4 such clause had been established previously in the context of a full rate hearing for
5 either BMG or Southwest. *Residential Utility* at 593, 10 P.2d at 1174. Neither does
6 Staff's recommendation reflect an automatic adjustment in rates due to changes in
7 specific operating costs. *Id.*

8 Although Staff may argue that the Court of Appeals opinion in *Pueblo Del Sol*
9 supports its position here, that decision, however, supports BMG's argument. *Pueblo Del*
10 *Sol* involved the sale of one utility's assets to another utility. The selling utility had been
11 authorized to charge a higher rate to its customers than had the buying utility. The
12 Commission allowed the buying utility to continue charging the higher rate to the selling
13 utility's customers as an interim rate pending a formal rate hearing. Although depicted as
14 an "interim rate," the rate that was being charged by the selling utility was a final rate set by
15 the Commission for *that particular company*. In effect, the *Pueblo Del Sol* court permitted a
16 buying utility to continue to charge the rates that the newly acquired customers had already
17 been paying. *See Residential Utility* at 592, 10 P.2d at 1173. Staff's recommendation
18 here, however, presents the opposite scenario. Instead of continuing existing customer
19 rates, which were established in by the Commission in a rate case, Staff seeks to impose
20 new and permanent rates upon both the customers and the new buyer, never having
21 considered the impact of including this new service territory on the buyer's rate base.

22 RUCO also acknowledged that such a result, even when motivated by a desire to
23 lower rates, would be improper. Noting the difference between the tariffed rates for BMG
24 and Southwest, RUCO's witness (Rodney Moore) stated that the customer "saving[s] is
25 based on SWG's current base rate tariffs and its current PGA rate." Moore Direct at 15.

26

1 Q. When will Black Mountain customers realize these rate
2 savings?

3 A. Immediately upon acquisition, BMG customers will realize
4 any savings generated through the cost of gas. SWG will adjust the PGA
5 rate for BMG customers so that both SWG and BMG pay the same total
6 cost of gas on a going forward basis. The base rate BMG tariffs will not
7 change until a determination is made through a rate case. Thus, BMG
8 customers will not realize any savings achieved in margin until SWG files a
9 rate application. I recommend that Southwest be required to file a rate
10 application within three years to flow through any margin savings to BMG's
11 customers.

12 Q. Do you agree with this procedure?

13 A. Yes.

14 *Id.* at 15-16. In explaining the basis for his opinion, Mr. Moore stated that "[T]he full
15 impact of this acquisition on the customers ...can only be determined by a complete
16 analysis within the framework of a rate case application." *Id.* at 19.

17 IV. 18 CONCLUSION

19 The proposed acquisition of BMG stock by Southwest will have a positive effect
20 on BMG's current ratepayers and is, therefore, in the public interest. Under the standard
21 set by the applicable statutes and rules, the transaction should be approved because it
22 is not detrimental to either Southwest's or BMG's rate payers. Staff proposed "obvious
23 and significant immediate consumer benefit" standard requiring the imposition of 14
24 conditions is not allowed under Arizona law. Further, Staff would have the Commission
25 authorize a rate decrease without having conducted a fair value analysis of Southwest's
26 rate base and without, as specifically required by Arizona law, having considered the
effect of the decrease on Southwest Gas' rate of return. Therefore, Southwest's
application should be approved without the conditions proposed by Staff as in the public

1 interest.

2 RESPECTFULLY SUBMITTED this 4th day of April, 2003

3 FENNEMORE CRAIG, P.C.

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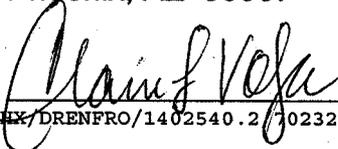
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