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ADMITTED TO PRACTICE IN:  
ARIZONA, COLORADO, MONTANA,  
NEVADA, TEXAS, WYOMING,  
DISTRICT OF COLUMBIA

November 22, 2006

Chairman Jeff Hatch-Miller  
Arizona Corporation Commission  
1200 West Washington  
Phoenix, Arizona 85007

Arizona Corporation Commission  
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Re: Arizona Public Service Company General Rate Case  
Docket Nos. E-01345A-05-0816, E-01345A-05-0826,  
and E-01345A-05-0827

Dear Chairman Hatch-Miller:

This letter is written upon behalf of Mesquite Power, L.L.C., Southwestern Power Group II, L.L.C., Bowie Power Station, L.L.C. and the Arizona Competitive Power Alliance (collectively "Merchant Generators") in response to your October 24, 2006 letter to APS and the Parties in Docket Nos. E-01345A-05-0816, E-01345A-05-0826, and E-01345A-05-0827 (the "Consolidated Proceedings").

Your letter contains the following statements:

"Additional information related to whether APS has the financial resources to maintain a reliable and adequate electric system for its customers would be helpful in my review of this matter. As part of the APS rate case, I would like the company to explain its resource planning (including financing of it) through 2020 for the development of new generation and transmission projects. (APS' August 1, 2006 letter refers to the subject generally.) This information should include preliminary RFPs for long-term power resources, potential self-build generation projects requiring Commission approval and major interstate transmission projects that would increase import capabilities. [Emphasis added]

I am also concerned that since APS agreed to a self-build moratorium in the Rate Case Settlement (Decision No. 67744), the company may face challenges in procuring additional power supplies through 2015. In the interim, competitive procurement of generation resources may prove problematic as natural gas prices remain volatile and subject to possible supply and delivery constraints. I would

like APS and the Parties to provide information on this topic as well, in order to develop the evidentiary record in this area. [Emphasis added]

The Merchant Generators are concerned by the foregoing statements for several reasons. First, it is not clear at this juncture what you may have in mind when you express a desire to “develop the evidentiary record” on the subject of the “self-build moratorium” which was approved by the Commission in Decision No. 67744, as issued on April 7, 2005 in Docket No. E-01345A-04-0437. As you may recall, the Merchant Generators were active Intervenors in that proceeding, and they were signatory parties to the August 18, 2004 Settlement Agreement which was the subject of Decision No. 67744. The “self-build moratorium” was the central consideration in their willingness to support the Settlement Agreement and its rate-basing of the Pinnacle West Energy Corporation generation units. In fact, collectively the Merchant Generators incurred approximately \$1,000,000 in attorneys’ and consultants’ fees in order to achieve that key settlement objective. Accordingly, anything pertaining to the integrity of the “self-build moratorium” is of critical importance to us.

Second, in the context of the issues presented in the Consolidated Proceedings, the relevance of “information” pertaining to APS’ future “potential self-build generation projects” must be questioned. The financing costs associated with such projects are unknown and speculative at this juncture. Thus, “information” (in the form of speculations) relating to the same would not constitute evidence which could materially assist the Commission in determining APS’ cost of capital and rate of return for purposes of the Consolidated Proceedings. Moreover, the concept of “potential self-build generation projects” presupposes that the competitive wholesale market has failed to satisfy APS’ projected power resource needs. There is no basis for such a supposition, and the Consolidated Proceedings are not an appropriate procedural vehicle for an inquiry of that nature.

Third, to the extent that the Commission did attribute a hypothetical financing cost to one or more of such future “potential self-build generation project(s),” it might risk creating an appearance that it had favorably prejudged the merit(s) of request(s) for exception(s) to the “self-build moratorium” it was yet to receive and fully consider. Presumably, that is both a reality and an appearance that the Commission does not wish to create.

Fourth, it is conceivable that, your indicated desire to introduce the subject of the “self-build moratorium” into the “evidentiary record” in the Consolidated Proceedings might also occasion some due process problems, given that there may be parties who might have sought to intervene in Docket No. E-01345A-05-0816, had they had notice that information pertaining to the “self-build moratorium” might be considered. Needless to say, they did not have such notice.

Fifth, there is currently pending in Docket No. E-01345A-06-0464 a request by APS for an exception to the “self-build moratorium”. That proceeding represents the “case of first impression” as to how the “self-build moratorium” provisions of the Settlement Agreement are to be interpreted and applied to a specific set of facts. The Merchant Generators are deeply involved as parties in that proceeding, which is on an expedited procedural schedule concurrent with the Consolidated Proceedings. Consequently, the Merchant Generators will be unable to

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participate as fully in the Consolidated Proceedings as would otherwise be the case to the extent that information relating to the "self-build moratorium" is offered by APS "to develop the evidentiary record."

Accordingly, for the reasons discussed above, the Merchant Generators respectfully request that the Commission not receive into the evidentiary record in the Consolidated Proceedings, and not consider in connection with any opinion(s) and order(s) issued therein, any information pertaining to "potential self-build generation projects". Thank you for your consideration of our serious concerns.

Respectfully submitted,

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