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September 12, 1996

Arizona Corporation Commission

DOCKETED

SEP 12 1996

DOCKETED BY 

Gary Yaquinto
Director
Utilities Division
Arizona Corporation Commission
1200 W. Washington St.
Phoenix, AZ 85007

RE: Retail Electric Competition

Dear Mr. Yaquinto:

Enclosed are the original and 10 copies of SRP's comments on the Commission's proposed rules relating to retail competition in Arizona (Docket No. U-0000-94-165). Because of the limited response time granted participants in this proceeding, SRP is still in the process of compiling a summarization of our comments for your use. We anticipate completing and submitting to you this summary prior to the public hearing on this matter.

Please contact me if you have any questions.

Sincerely,

Jessica Youle

JY/lmb

Enclosures

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Arizona Corporation Commission

DOCKETED

SEP 12 1996

DOCKETED BY *LS*

6 **BEFORE THE ARIZONA CORPORATION COMMISSION**

7	IN THE MATTER OF COMPETITION)	DOCKET No. U-0000-94-165
8	IN THE PROVISION)	SRP'S COMMENTS ON PROPOSED
9	OF ELECTRIC SERVICES)	RULE - RETAIL ELECTRIC
10	THROUGHOUT THE STATE)	COMPETITION
11	OF ARIZONA)	

12
13 Salt River Project Agricultural Improvement & Power District ("SRP") submits the
14 following comments on the proposed rules relating to retail electric competition ("Proposed
15 Rules") submitted by Commission staff on August 28, 1996. SRP provides these comments as
16 part of its voluntary participation in this docket proceeding. SRP also incorporates by reference
17 herein its prior comments filed in this docket proceeding on June 28, 1996, attached hereto as
18 Exhibit B.

19 SRP actively supports the implementation of retail competition for all citizens of
20 Arizona. SRP has already committed to opening its own electric service area, on a reciprocal
21 basis, to allow its customers to purchase electricity from other generators. SRP also has
22 committed to establish a new business entity that will sell electricity to customers outside SRP's
23 present service area. This new business entity ("GENCo") is anticipated to be a private, for
24 profit corporation. Accordingly, GENCo will be subject to the jurisdiction of the Commission
25 and will comply with applicable Commission rules and regulations governing retail electric
26 competition.

1 At the same time, SRP recognizes that restructuring of the electric industry to permit
2 retail competition is a complex process. It raises unique jurisdictional and legal issues that must
3 be addressed. Moreover, it involves complicated technical and logistical problems that need to
4 be resolved to ensure an orderly transition to a competitive structure and maintain a reliable
5 system of electric services. A safe, reliable and economic supply of electricity is critically
6 important to the people of Arizona.

7 The Proposed Rules raise significant constitutional and other legal issues as well as
8 technical concerns relating to the continued reliability of electric service. These issues must be
9 resolved before any Proposed Rules are adopted by the Commission. SRP's comments focus on
10 some of the issues and SRP has attached, as Exhibit A hereto, a red-lined version of the
11 Proposed Rules that incorporates some changes necessary to avoid constitutional violations,
12 clarify the scope and terms of the Proposed Rules, and avoid costly and time consuming legal
13 challenges.

14 SRP's specific comments on critical portions of the Proposed Rules follow.

15
16 **1. Certain Proposed Rule Provisions Must Be Modified to Eliminate**
17 **Ambiguity and Avoid the Arizona Constitutional Prohibition Against Commission**
18 **Regulation of Municipal Corporations.**

19 The Arizona Constitution creates the Arizona Corporation Commission and expressly
20 limits its jurisdictional authority. Article 15, § 3 gives the Commission regulatory authority
21 over "public service corporations". Article 15, § 2 defines "public service corporations" as "[all
22 corporations other than municipal engaged in furnishing . . . electricity for light, fuel or power
23" (emphasis supplied.) Courts have consistently upheld this constitutional prohibition
24 against Commission jurisdiction over municipal corporations. *See, e.g., City of Mesa v. Salt*

1 *River Project Agricultural Improvement & Power District*, 92 Ariz. 91, 373 P.2d 722 (1962);
2 *City of Phoenix v. Wright*, 52 Ariz. 227, 80 P.2d 390 (1938).

3 As an agricultural improvement district, SRP is constitutionally a “political subdivision
4 of the State, and vested with all rights, privileges and benefits, and entitled to the immunities
5 and exemptions granted municipalities”. Ariz. Const. Art. 13, § 7. Like other such municipal
6 entities, SRP is not and cannot be subject to the jurisdiction of the Commission. *City of Mesa v.*
7 *Salt River Project Agricultural Improvement & Power District*, *supra*; *Rubenstein Construction*
8 *Co. v. Salt River Project Agricultural Improvement & Power District*, 76 Ariz. 402, 265 P.2d
9 455 (1954).

10 The Proposed Rules fail to clearly acknowledge this critical limitation on the
11 Commission's jurisdiction. Certainly, the Commission does not want to adopt rules that violate
12 the Arizona Constitution. Therefore, certain provisions in the Proposed Rules must be revised.
13 This can be easily accomplished with minor drafting revisions and additional definitions.

14 Proposed Rules R14-2-xxx5(A) and R14-2-xxx11 refer respectively to the terms
15 “electric company” and “electric utility”. Numerous other provisions simply use the term
16 “company” to determine rule applicability. See R14-2-xxx3, R14-2-xxx5(B), R14-2-xxx6(H),
17 R14-2-xxx9, and R14-2-xxx12 through xxx14. R14-2-xxx6(F) refers to a “supplier of services”.
18 These terms, unlike the term “affected utility”, are not defined in the Proposed Rules and are not
19 differentiated from one another. This results in confusion and ambiguity as to the applicable
20 scope of the provisions involved. Additionally, these undefined terms could arguably be
21 construed to include electric service providers that are political subdivisions or municipal
22 corporations. Such an interpretation would, of course, unlawfully expand the jurisdiction of the
23 Commission and violate the Arizona Constitution.

24 The solution is simple. The terms “electric utility”, “electric company”, “company” and
25 “supplier of services” should be deleted from the Proposed Rules and replaced with the term
26

1 "electric service provider". The term "electric service provider" should be defined in R14-2-
2 xxx1 as "any person, including public service corporations, brokers and marketers, but
3 excluding Arizona municipal corporations and Arizona political subdivisions, who provide or
4 arrange to provide electric service to Arizona consumers". For further clarification, the terms
5 "person", "broker" and "marketer" should also be defined in R14-2-xxx1. These changes are
6 reflected in the attached Exhibit A.

7 These minor drafting changes will ensure consistent use of defined terms, clear up
8 confusion as to the scope of applicability of the Proposed Rules and eliminate the problem of an
9 unconstitutional expansion of Commission jurisdiction over municipal corporations and
10 political subdivisions. At the same time, these changes will clarify the Commission's
11 jurisdiction over the variety of new entrants into the electric service market, including GENCo.

12 13 **2. Reciprocity.**

14 Rule R14-2-xxx11 on reciprocity has been rewritten in Exhibit A to broaden its scope to
15 include entities located both within and without the State of Arizona. Arizona consumers will
16 not want to limit their choices to electric service providers physically located within the State of
17 Arizona. To avoid disadvantaging Arizona citizens, the Proposed Rules should extend
18 reciprocity to everyone participating in retail competition in the State of Arizona.

19 The redraft of Rule R14-2-xxx11 accomplishes three objectives. It makes out-of-state
20 public service corporations, as well as out-of-state municipal corporations and political
21 subdivisions, who want to sell on a retail basis in Arizona, subject to the jurisdiction of the
22 Commission to the extent they conduct business in Arizona. It also avoids the unconstitutional
23 regulation of Arizona political subdivisions and municipal corporations by the Commission,
24 while providing assurance that the Commission will not grant an "electric service provider" a
25 CCN for retail sales in a service area which does not have terms and conditions for pricing
26

1 individual elements of competitive electric service or a procedure for handling complaints
2 arising therefrom.

3 If a political subdivision or municipal corporation wishes to participate in sales to
4 customers within the service territories of "affected utilities", then they, in turn, should allow
5 affected utilities to sell to customers located in the service territory of that political subdivision
6 or municipal corporation. In many instances, and in the case of SRP, the governing body has
7 the authority, if it chooses to exercise it, to allow other electric service providers to supply
8 generation services in its service territory. In other instances, the Arizona Legislature may have
9 to grant that authority to the governing body. Nevertheless, the appropriate governing authority
10 should be able to "signal" the Commission that it has adopted its own procedures which
11 accommodate individually priced competitive electric services. At the same time, these entities
12 are unlikely to want to open up their own service territories if they cannot participate in retail
13 electric competition in the service territories of the "affected utilities." The redraft of Rule R14-
14 2-xxx11 provides for reciprocity while avoiding the unconstitutional regulation of Arizona
15 political subdivisions and municipal corporations by the Commission.

16
17 **3. Distribution Monopolies Must Be Maintained to Assure an Economical and**
18 **Reliable Supply of Electricity for Consumers.**

19 The Proposed Rules do not expressly provide for the continuance of distribution
20 monopolies within the existing service areas of electric utilities. Unlike other industries which
21 have been restructured, the electric utility industry has certain unique features which argue for
22 the continuation of distribution monopolies within a given service area.

23 In today's world, electricity has become a necessity. In a world in which *anyone* may
24 serve *everyone*, no one would have the obligation to serve a customer located in a remote area
25 where no distribution system currently exists, or where the service to the customer is deemed
26

1 uneconomic. In return for assuming an obligation to serve customers within its service area, an
2 electric utility should be able to continue to operate as a monopoly with respect to its
3 distribution system. Other generation service providers could make use of its distribution
4 system, but the electric utility with the obligation to serve would have a guaranteed, i.e.
5 regulated, rate of return. This ensures all customers have access to essential electric service.

6 Furthermore, from an economic and a system reliability point of view, and as a matter of
7 public safety, it makes no sense to duplicate or triplicate distribution wiring systems within an
8 existing service area. Customers within an existing service area can be given the choice of
9 generation suppliers to provide electricity without imposing additional costs and delays on
10 consumers to secure installation of new distribution lines to their homes and businesses.
11 Distribution monopolies can and will be established in a manner that will support new
12 distributed generation.

13 Moreover, distribution monopolies are key to a reliable distribution system. The electric
14 system must be operated and maintained on an integrated basis to ensure safe, dependable
15 electric service. A single distribution entity provides the means to do this.

16 Finally, retention of distribution monopolies eliminates some legal issues related to the
17 historical exclusivity component of a CCN issued by the Commission. The CCN was created
18 by the Arizona Legislature by Title 9, Paragraph 2326(a) of Revised Statutes of 1913. Since
19 that time, the courts construing the CCN statutory provisions have consistently reaffirmed the
20 CCN as granting a utility an exclusive right to distribute electric services within the described
21 territory. *City of Tucson v. Polar Water Co.*, 76 Ariz. 404, 409, 265 P.2d 773, 775-76 (1954);
22 *application of Trico Electric Cooperative, Inc.*, 92 Ariz. 373, 381-82, 377 P.2d, 309, 315
23 (1962). The Commission can avoid unilaterally upsetting this legislative framework by
24 maintaining existing distribution monopolies within service territories covered by the present
25 CCN structure.

1
2 **4. Buy-Through Provisions Should Be Eliminated.**

3 All customers of "affected utilities" should have the opportunity to benefit from
4 competition. The buy-through provision appears to favor a small number of large customers at
5 the expense of the remaining majority of customers. Select large customers will be primarily in
6 the position to request such services. The bulk of the population will be unable, for various
7 reasons, to directly access the wholesale power market. In addition, the provision suggests that
8 buy-through customers may be relieved of their responsibility to bear their fair share of the cost
9 of service (e.g. facilities, reliability, etc.). Other customers should not be responsible for costs
10 associated with any customer that moves to a buy-through rate.

11 Additionally, a buy-through date of January 1998 would effectively accelerate an already
12 ambitious schedule. This may encourage utilities to devote resources to this small piece of the
13 restructuring proposal recommendation rather than concentrating on the entire package of
14 competitive shifts.

15 Finally, if "affected utilities" are to move to a competitive situation, the Commission
16 should not mandate a specified mark-up. The competitive environment must be allowed to
17 function without regulatory intervention for all parties to receive the benefits of such a shift.

18 Therefore, R14-2-xxx4(G)(4) and the definition of the term "buy-through" should be
19 eliminated.

20
21 **5. The Proposed Requirements for Solar Energy Should Be Broadened to Encourage
22 and Allow the Development of Additional Renewable Energy Sources.**

23 Proposed Rule R14-2-xxx9 imposes requirements regarding the inclusion of solar
24 resources in the providing of electric services. This provision is unduly restrictive and should
25 be expanded to include other renewable energy sources, such as wind, waste, biomass, hydro,
26

1 and geothermal. The point is to encourage the development and use of renewable sources of
2 energy -- not just solar resources. Additionally, expanding the cover of this Proposed Rule to
3 include other forms of renewable resources will not inequitably penalize electric service
4 providers that have developed, or are in the process of developing, renewable sources of energy
5 other than solar.

6 Finally, the arbitrary requirement of a "new" source of renewable energy should be
7 eliminated so as not to penalize utilities who have previously established and developed
8 renewable sources of energy.

9 Revisions broadening R14-2-xxx9 and adding a definition of "renewable energy
10 source(s)" are included in Exhibit A.

11
12 **6. The Commission's Schedule May Not Allow Enough Time for "Affected Utilities"**
13 **to Efficiently Transition to the Competitive Environment.**

14 Because SRP is not subject to the Commission's jurisdiction, it is not directly affected by
15 the implementation schedule imposed on "affected utilities" by the Commission. Nonetheless,
16 SRP questions whether a smooth transition to retail competition can be accomplished within the
17 time frames set out in the Proposed Rules.

18 SRP believes that retail electric competition should begin in the year 2000 and should be
19 phased in first to the largest customers, and then over a reasonable period of time, as
20 appropriate, to the remaining customer classes. This schedule would eliminate the need for a
21 Commission-mandated process for recovery of stranded investment. Should the Commission
22 institute retail electric competition at an earlier date, or phase-in competition more quickly, then
23 clearly defined and consistent rules for the recovery of stranded investment would have to be
24 developed prior to the start date of competition. The stranded investment issue is complex and
25 critical to an accelerated implementation of retail competition. Should the Commission decide
26

1 to implement retail electric competition prior to the year 2000, SRP suggests that a separate
2 process be established to deal with this issue with important implications for all Arizona electric
3 customers.

4 SRP believes that a phased-in approach recognizes that the technology does not exist
5 today to provide for competition for all customers at the same time. (See Exhibit C for a list of
6 some of the technical issues that must be resolved in order for all customers to have the choice
7 of electric service provider and, at the same time, a reliable electric system.) The electric
8 industry has unique characteristics which distinguish it from, for example, the gas or telephone
9 industry. As recent electric system outages have shown, the technology of providing electric
10 service is complex. Small events can provoke unexpected or drastic consequences. A phase-in
11 of retail competition ensures that the transition will be orderly and that one customer will not
12 pay for another customer's service.

13 14 **7. Other General Comments**

15 A. Moving to a competitive environment for providing electricity and the
16 "unbundling of services" means generation will be separated from other services. Some
17 mechanism, such as a clearinghouse, should be developed to inform customers what prices other
18 customers are being charged for various electric services, as well as for generation itself. Such a
19 mechanism will help ensure the development of consistent generation pricing and foster a truly
20 competitive marketplace for different types and combinations of electric services. The New
21 York Stock Exchange is an example of a highly successful clearinghouse whose actions have
22 promoted growth and prosperity in the United States.

23 B. In many instances, it is difficult to understand how portions of the Proposed
24 Rules will actually operate. In order to effectively assess the impact on a reliable and economic
25 electric system SRP believes it would be helpful for the Commission to establish a procedure
26

1 whereby interested parties and participants could submit specific written questions on the
2 meaning and operation of numerous provision in the Proposed Rules. The Commission staff
3 would then provide written responses to clarify the scope and meaning of these provisions.

4 Respectfully submitted this 12th day of September, 1996.

5
6 **Salt River Project Agricultural
Improvement and Power District**

7 

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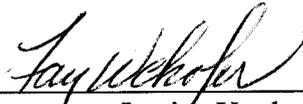
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26

CERTIFICATE OF SERVICE

The original and ten (10) copies of the foregoing SRP's Response to Request for Comments on Electric Industry Restructuring were filed this 12th day of September, 1996, with:

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Secretary to Jessica Youle

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EXHIBIT A

PROPOSED RULE - RETAIL ELECTRIC COMPETITION

Docket No. U-0000-94-165

R14-2-xxxI. Definitions

In this Article, unless the context otherwise requires:

1. "Affected Utilities" means the following public service corporations providing electric service:

Tucson Electric Power Company, Arizona Public Service Company, Citizens Utilities Company, Arizona Electric Power Cooperative, Trico Electric Cooperative, Duncan Valley Electric Cooperative, Graham County Electric Cooperative, Mohave Electric Cooperative, Sulphur Springs Valley Electric Cooperative, Navopache Electric Cooperative, Ajo Improvement District, and Morenci Water and Electric Company.
2. *"Broker" means a Person who arranges the sale and purchase of electric energy, transmission and other services between buyers and sellers, but does not take title to any of the power sold.*
3. "Bundled Service" means electric service provided as a package to the consumer including all generation, transmission, distribution, ancillary and other services necessary to deliver useful electric energy and power to the consumer's residence or place of business.
4. ~~"Buy through" refers to a purchase of electricity by an Affected Utility at wholesale for a particular retail consumer or at the direction of a particular retail consumer.~~
5. *"Electric Service Provider" means a Person, including public service corporations, brokers and marketers, but excluding Arizona municipal corporations and political subdivisions of the State of Arizona, who provides or arranges to provide electric service to Arizona consumers.*
6. *"Indian Tribe" means an Indian Tribe, band, nation, or community that is recognized by the United States Secretary of the Interior and that has a governmental body exercising substantial duties and powers.*
7. *"Marketer" means a Person who buys electric energy, transmission and other services from traditional utilities and other suppliers, and then resells those services at wholesale or to an end-use customer.*
8. *"Person" means an individual, corporation, partnership, association, state, Indian Tribe, political subdivision, municipality or other legal entity.*

9. *"Renewable Energy Resource" means any source of energy that is continually available or that can be renewed or replaced. Examples include wind, solar, geothermal, hydro, photovoltaic, and waste. Nonrenewable energy sources include coal, oil and gas, which all exist in finite amounts.*
10. "Standard Offer" means Bundled Service offered to all consumers in a designated area at regulated rates.
11. "Stranded Investment" means the verifiable net difference between the value of all the prudent jurisdictional assets under traditional regulation of Affected Utilities and the market value of those assets directly attributable to the introduction of competition under this Article.
12. "System Benefits" means Commission-approved utility low income, demand side management, environmental, renewables, and nuclear power plant decommissioning programs.
13. "Unbundled Service" means electric service elements provided and priced separately, including such service elements as generation, transmission, distribution, and ancillary services. Unbundled Service may be sold to consumers or to other suppliers of consumers.

R14-2-xxx2. Filing of Tariffs by Affected Utilities.

Each Affected Utility shall file tariffs consistent with this Article by June 30, 1997 to allow retail electric competition in its service territory.

R14-2-xxx3. Certificates of Convenience and Necessity.

- A. *The monopoly of electric distribution service existing prior to the date stated in Rule R14-2-xxx2 shall continue under these Rules even after competition is fully achieved in the provision of other electric services, including generation and transmission services. Any Electric Service Provider holding, or applying for and receiving, a Certificate of Convenience and Necessity to supply distribution services under this Article shall have the privilege of a monopoly over distribution services in its service area as against any other Electric Service Provider. An Electric Service Provider applying for and receiving a Certificate of Convenience and Necessity to provide services other than distribution services, shall receive a non-exclusive privilege to provide those services in the areas defined by the Certificate.*
- B. Any ~~company~~ Electric Service Provider intending to supply services described in Subsections R14-2-xxx5 or R-14-2-xxx6, other than wholesale generation services, shall obtain a Certificate of Convenience and Necessity from the Commission (unless the ~~company~~ Electric Service Provider already has an applicable Certificate).

- C. Any ~~company~~ *Electric Service Provider* desiring such a Certificate of Convenience and Necessity shall file with the Docket Control Center the required number of copies of an application. In support of the request for a Certificate of Convenience and Necessity, the following information must be provided:
1. A description of the electric services which the applicant intends to offer.
 2. The proper name and correct address of the applicant, and
 - a. The full name of the owner if a sole proprietorship,
 - b. The full name of each partner if a partnership,
 - c. A full list of officers and directors if a corporation, or
 - d. A full list of the members if a limited liability corporation.
 3. A tariff for each service to be provided that states the maximum rate and terms and conditions that will apply to the provision of the service.
 4. A description of the geographic areas to be served, provided that these areas are restricted to geographical areas served by the Affected Utilities as of the date this Article is adopted and to service areas added under the provisions of Subsection R14-2-xxx11.
 5. Appropriate city, county and/or state agency approvals.
 6. A description of the applicant's technical ability to obtain and deliver electricity and provide any other proposed services.
 7. Documentation of the financial capability of the applicant to provide the proposed services, including the most recent income statement and balance sheet, the most recent projected income statement, and other pertinent financial information. Audited information shall be provided if available.
 8. A description of the form of ownership (e.g., partnership, corporation).
 9. An Arizona business plan; if this information is confidential, the plan may be submitted only to Staff and need not be filed in Docket Control.
 10. Such other information as the Commission or the Staff may request.
- D. At the time of filing for a Certificate of Convenience and Necessity, each applicant shall notify the Affected Utilities in whose service territories it wishes to offer service of the application.
- E. The Commission may deny certification to any applicant who:
1. Does not provide the information required by this Article.
 2. Does not possess adequate technical or financial capabilities to provide the proposed services.
 3. Fails to provide a performance bond, if required.

- F. Every ~~company~~ *Electric Service Provider* obtaining a Certificate of Convenience and Necessity under this Article shall obtain certification subject to the following conditions:
1. The ~~company~~ *Electric Service Provider* shall comply with all Commission rules, orders, and other requirements relevant to the provision of electric service and relevant to resource planning.
 2. The ~~company~~ *Electric Service Provider* shall maintain accounts and records as required by the Commission.
 3. The ~~company~~ *Electric Service Provider* shall file with the Director of the Utilities Division all financial and other reports that the Commission may require and in a form and at such times as the Commission may designate.
 4. The ~~company~~ *Electric Service Provider* shall maintain on file with the Commission all current tariffs and any service standards that the Commission shall require.
 5. The ~~company~~ *Electric Service Provider* shall cooperate with any Commission investigation of customer complaints.
 6. Failure to comply with any of the above conditions may result in recision of the ~~company's~~ *Electric Service Provider's* Certificate of Convenience and Necessity.
- G. In appropriate circumstances, the Commission may require, as a precondition to certification, the procurement of a performance bond sufficient to cover any advances or deposits the applicant may collect from its customers, or order that such advances or deposits be held in escrow or trust.

R14-2-xxx4. Competitive-Phases Phase

- ~~A. Each Affected Utility shall make available at least 20 percent of its 1995 system retail peak demand for competitive generation supply to all customer classes (including residential and small commercial consumers) by January 1, 1999.~~
- ~~1. No more than one half of the eligible demand may be procured by consumers whose individual contract demand is greater than 3 MW each.~~
 - ~~2. At least 10 percent of the eligible demand shall be reserved for residential consumers.~~
 - ~~3. Aggregation of loads of multiple residential, commercial, or industrial consumers shall be permitted.~~
- ~~B. Each Affected Utility shall make available at least 50 percent of its 1995 system retail peak demand for competitive generation supply to all customer classes (including residential and small commercial consumers) by January 1, 2001.~~
- ~~1. No more than one half of the eligible demand may be procured by consumers whose individual contract demand is greater than 3 MW each.~~

2. ~~At least 20 percent of the eligible demand shall be reserved for residential consumers.~~
 3. ~~Aggregation of loads of multiple residential, commercial, or industrial consumers shall be permitted.~~
- C. ~~Prior to 2001, no single consumer shall receive more than 20 percent of the available kW in a given year in an Affected Utility's service territory.~~
- D. ~~Each Affected Utility shall make available all of its retail demand for competitive generation supply by January 1, 2003.~~
- E. ~~By the date indicated in Subsection R14-2-xxx2, Affected Utilities shall propose for Commission review and approval how customers will be selected for participation in the competitive market prior to 2003.~~
1. ~~Possible selection methods are first come, first served, random selection via a lottery among volunteering consumers, or designation of geographic areas.~~
 2. ~~The method for selecting customers to participate in the competitive market must fairly allow participation by a wide variety of customers of all sizes.~~
 3. ~~All customers who produce or purchase at least 10 percent of their annual electricity consumption from photovoltaic or solar thermal resources installed in Arizona after January 1, 1997 shall be selected for participation in the competitive market if those customers apply for participation in the competitive market.~~
- F. Consumers served under existing contracts are eligible to participate in the competitive market prior to expiration of the existing contract only if the Affected Utility and the consumer agree.
- G. ~~Buy throughs.~~
1. ~~Each Affected Utility shall file by the date indicated in Subsection R14-2-xxx2 a mechanism which enables all classes of its customers to engage in a Buy-through, including customers who wish to use the Buy-through mechanism to obtain electricity from photovoltaic or solar thermal generating resources.~~
 2. ~~Buy throughs shall be permitted as early as January 1, 1998.~~
 3. ~~Each Affected Utility shall make at least 5 percent of its 1995 system retail peak demand available for competitive procurement under this Buy-through mechanism.~~
 4. ~~The Affected Utility shall permit customers to identify electricity sources which the Affected Utility would obtain on behalf of the customer and provide to the customer at unbundled rates described in Subsection R14-2-xxx6, below, plus the cost of the electricity plus a mark-up on the cost of electricity not to exceed 15 percent of the cost of the electricity.~~
 5. ~~Buy throughs shall not be considered as meeting the requirements of Subsections R14-2-xxx4(A), R14-2-xxx4(B), or R14-2-xxx4(D).~~

R14-2-xxx5. Competitive Services

- A. A properly certificated ~~company~~ *Electric Service Provider* may offer any of the following services under bilateral or multilateral contracts with consumers:
1. Distributed energy services at market based rates (serving one or more consumers located in proximity, and not necessarily requiring transmission service from others).
 2. Central station generation services at market based rates (generation serving one or more consumers located at a distance from consumers and requiring transmission service, some ancillary services, and possibly distribution service).
 3. Combinations of distributed and central station generation services.
- B. ~~A company~~ *An Electric Service Provider* other than an Affected Utility may provide services described in Subsection R14-2-xxx6 after filing appropriate tariffs and receiving Commission approval of those tariffs.

R14-2-xxx6. Services Required To Be Made Available by Affected Utilities

- A. Until the Commission determines that competition has been substantially implemented, each Affected Utility shall make available to all consumers in its service area, as defined on the date indicated in Subsection R14-2-xxx2, Standard Offer bundled generation, transmission, ancillary, distribution, and other necessary services at regulated rates.
1. An Affected Utility may request that the Commission determine that competition has been substantially implemented to allow discontinuation of Standard Offer service and shall provide sufficient documentation to support its request.
 2. The Commission may, on its own motion, investigate whether competition has been substantially implemented and whether Standard Offer service may be discontinued.
- B. By the date indicated in Subsection R14-2-xxx2, each Affected Utility may file proposed tariffs to provide Standard Offer Bundled Service and such rates shall not become effective until approved by the Commission. If no such tariffs are filed, rates and services in existence as of the date in Subsection R14-2-xxx2 shall constitute the Standard Offer.
- C. By the date indicated in Subsection R14-2-xxx2, each Affected Utility shall file Unbundled Service tariffs to provide the services listed below to all eligible purchasers on a nondiscriminatory basis.
1. Distribution service
 2. Metering and meter reading services.
 3. Open access transmission service (as approved by the Federal Energy Regulatory Commission, if applicable).

4. Ancillary services as defined by the Federal Energy Regulatory Commission in Order 888 (III FERC Stats. & Regs. ¶ 31,036, 1996).
 5. Information services such as provision of customer information to other suppliers.
 6. Other ancillary services necessary for safe and reliable system operation.
- D. To manage its risks, an Affected Utility may employ reasonable credit checks, deposit requirements, and advance payment requirements for Unbundled Services.
- E. The Affected Utilities must provide transmission and ancillary services according to the following guidelines:
1. Services must be provided consistent with applicable tariffs filed with the Federal Energy Regulatory Commission.
 2. Affected Utilities must accept power and energy delivered to their transmission systems by others and offer wheeling services comparable to services they provide to themselves.
- F. Upon authorization by the customer, an Affected Utility shall release in a timely and useful manner that customer's load and usage data to a certificated ~~supplier of services~~ *Electric Service Provider* authorized by this Article.
- G. Rates for Unbundled Services:
1. The Commission shall review and approve rates for services listed in Subsections R14-2-xxx6(C) and R14-2-xxx6(D), where it has jurisdiction, before such services can be offered.
 2. Such rates shall reflect the costs of providing the services.
 3. Such rates may be downwardly flexible if approved by the Commission.
- H. ~~Companies~~ *Any Electric Service Provider* offering services under this Subsection R14-2-xxx6 shall provide adequate supporting documentation for their proposed rates. Where rates are approved by another jurisdiction, such as the Federal Energy Regulatory Commission, those rates shall be provided to this Commission.

R14-2-xxx7. Recovery of Stranded Investment of Affected Utilities

- A. The Affected Utilities shall take every feasible, cost-effective measure to mitigate or offset Stranded Investment by means such as accelerated depreciation of assets, expanding wholesale or retail markets, or offering a wider scope of services for profit, among others.
- B. The Commission may allow recovery of unmitigated Stranded Investment by Affected Utilities.
- C. The Affected Utilities may file estimates of Stranded Investment. Such estimates shall be fully supported by appropriate analyses and by market transactions undertaken by willing buyers and willing sellers.

- D. An Affected Utility may request Commission approval of exit fees, distribution charges, or other means of recovering Stranded Investment from customers who reduce or terminate service from the Affected Utility as a direct result of competition governed by this Article, or who obtain lower rates from the Affected Utility as a direct result of the provisions of this Article.
- E. The Commission shall determine for each Affected Utility which files Stranded Investment data and recovery proposals consistent with this Article appropriate Stranded Investment recovery mechanisms and charges. In making its determination, the Commission shall consider at least the following factors:
1. The impact of Stranded Investment recovery on the effectiveness of competition.
 2. The impact of Stranded Investment recovery on customers of the Affected Utility who do not participate in the competitive market.
 3. The impact of partial or no recovery of Stranded Investment on the Affected Utility and its shareholders.
 4. The impact of Stranded Investment recovery on prices paid by consumers who participate in the competitive market.
 5. The degree to which the Affected Utility has mitigated or offset Stranded Investment.
 6. The degree to which some assets have values in excess of their book values.
 7. Appropriate treatment of negative Stranded Investment.
 8. The time period over which such Stranded Investment charges may be recovered. The Commission shall limit the application of such charges to a specified time period.
 9. The ease determining the amount of Stranded Investment.
 10. The amount of electricity generated by renewable generating resources owned by the Affected Utility.
- F. Stranded investment may only be recovered from customers served competitively under the provisions of this Article.
- G. The Commission may order ~~a utility~~ *an Affected Utility* to file estimates of Stranded Investment and mechanisms to recover or, if negative, to refund Stranded Investment.
- H. The Commission may order regular revisions to estimates of the magnitude of Stranded Investment.
- I. In no event shall recovery of Stranded Investment occur after December 31, 2004.

R14-2-xxx8. System Benefits Charges

- A. By the date indicated in Subsection R14-2-xxx2, each Affected Utility shall file for Commission review rates or related mechanisms to recover the costs of System Benefits from all consumers located in the Affected Utility's service area who participate in the competitive market.
- B. Each Affected Utility shall provide adequate supporting documentation for its proposed rates for System Benefits.
- C. An Affected Utility shall recover the costs of System Benefits only upon approval by the Commission of the recovery charge and mechanism.

R14-2-xxx9. Renewable Energy Resource Portfolio Standard

- A. Starting on January 1, 1999, any ~~company~~ *Electric Service Provider* selling electricity under the provisions of this Article must derive at least 1 percent of the total retail energy sold competitively from ~~new solar resources~~ *Renewable Energy Resources*, whether that ~~solar energy~~ *Renewable Energy Resource* is purchased or generated by the seller. ~~Solar resources include photovoltaic resources and solar thermal resources that generate electricity. New solar resources are those installed on or after January 1, 1997.~~
- B. Starting on January 1, 2002, any ~~company~~ *Electric Service Provider* selling electricity under the provisions of this Article must derive at least 2 percent of the total retail energy sold competitively from ~~new solar resources~~ *Renewable Energy Resources*, whether that ~~solar energy~~ *Renewable Energy Resource* is purchased or generated by the seller. ~~Solar resources include photovoltaic resources and solar thermal resources that generate electricity. New solar resources are those installed on or after January 1, 1997.~~
- C. Any ~~company~~ *Electric Service Provider* certificated under the provisions of this Article shall be able to credit two times the electric energy generated before January 1, 1999 using ~~photovoltaic or solar thermal resources~~ *Renewable Energy Resources* installed on or after January 1, 1997 in Arizona to the electric energy requirements of Subsections R14-2-xxx9(A) or R14-2-xxx9(B).
- D. ~~Companies~~ *Electric Service Providers* selling electricity under the provisions of this Article shall provide reports on sales and ~~solar power~~ *Renewable Energy Resources* as required in this Article, and the Commission may conduct necessary monitoring to ensure the accuracy of these data.
- E. If ~~a company~~ an *Electric Service Provider* selling electricity under the provisions of this Article fails to meet the requirement in Subsection R14-2-xxx9(A) or Subsection R14-2-xxx9(B) in any year, the Commission may impose a penalty on that ~~company~~ *Electric Service Provider* up to \$0.30 per kWh for deficiencies in the provision of ~~solar energy~~ *Renewable Energy Resources*. In addition, if the provision of ~~solar energy~~ *Renewable Energy Resources* is consistently deficient, the Commission may void ~~a company's~~ *an Electric Service Provider's* contracts negotiated under this Article.

- F. The ~~solar~~ *Renewable Energy Resource* portfolio standard described in this Subsection is in addition to renewable resource goals for Affected Utilities established in Decision No. 58643.

R14-2-xxx10. Pooling of Generation and Centralized Dispatch of Generation or Transmission

- A. The Commission shall conduct an inquiry into pooling and dispatch arrangements for transmission and generation of electricity.
- B. The Commission may establish a pool for generation or centralized dispatch of generation or transmission by an independent system operator or by other means.
- C. The Commission may work with other entities to establish pooling or centralized dispatch of generation or transmission.

R14-2-xxx11. In-State Reciprocity

- A. The service territories of ~~Arizona electric utilities~~ *Electric Service Providers*, which are not Affected Utilities, shall not be *required to be* open to competition under the provisions of this Article. ~~nor shall Arizona electric utilities which are not Affected Utilities be able to compete for sales in the service territories of the Affected Utilities. However, an Arizona electric utility which is not an Affected Utility may voluntarily participate under the provisions of this Article if it makes its service territory available for competing sellers, if it agrees to all of the requirements of this Article, and if it obtains an appropriate Certificate of Convenience and Necessity.~~
- B. *If an Arizona political subdivision or municipal corporation has an existing service territory, then such territory shall be deemed to be open to competition by Arizona Electric Service Providers if the political subdivision or municipality provides to the Commission a duly adopted action of the governing body of such political subdivision or municipal corporation, certifying that the governing body has adopted terms and conditions providing separate pricing for the retail electric competition listed in R14-2-xxx6.C within its service territory and has adopted a procedure for bill complaints arising therefrom.*
- C. *If an Electric Service Provider has an existing out-of-state service territory, then, prior to the granting of a Certificate of Convenience and Necessity, such Electric Service Provider must demonstrate, by providing the Commission documentation, that there are in place terms and conditions providing separate pricing for the retail electric competition listed in R14-2-xxx6.C within its out-of-state service territory and that it has a procedure for bill complaints arising therefrom.*

R14-2-xxx12. Rates

- A. Market based rates for competitively provided services shall be deemed to be just and reasonable.
- B. Each ~~company~~ *Electric Service Provider* under this Article shall have on file with the Commission tariffs describing such services and maximum rates for those services, but the services may not be provided until the Commission has approved the tariffs.
- C. For competitive services provided under standard contracts (that is, non-customized rates, terms, and conditions), a ~~company~~ *an Electric Service Provider* governed by this Article shall file in a timely manner with the Director of the Utilities Division current price lists, terms and conditions consistent with approved tariffs.
- D. Competitively negotiated contracts customized to individual customers which comply with approved tariffs do not require further Commission approval. However, all such contracts must be filed with the Director of the Utilities Division at least 30 days prior to becoming effective; if a contract does not comply with the provisions of this Article it shall not become effective without a Commission order.
- E. An Affected Utility or ~~company~~ *Electric Service Provider* holding a Certificate pursuant to this Article may price its competitive services, as defined in Subsection R14-2-xxx5, at or below the maximum rates specified in its filed tariff, provided that the price is not less than the marginal cost of providing the service.
- F. Requests for changes in maximum rates or changes in terms and conditions of previously approved tariffs may be filed. Such changes become effective only upon Commission approval.

R14-2-xxx13. Service Quality, Consumer Protection, Safety, and Billing Requirements

- A. All customer bill complaints concerning services rendered under this Article shall be governed by the provisions of Subsections R14-2-212(B) and R14-2-212(C).
- B. All customer service complaints concerning services rendered under this Article shall be governed by the provisions of Subsections R14-2-212 (A) and R14-2-212(C).
- C. Establishment of competitive service to consumers whose estimated demand is less than 1,000 kilowatts shall be governed by the provisions of Subsections R14-2-203(A) and R14-2-203(B).
- D. No consumer shall be deemed to have changed suppliers of any service authorized in this Article (including changes from supply by the Affected Utility to another supplier) without written authorization by the consumer for service from the new supplier. If a consumer is switched to a different ("new") supplier without such written authorization, the new supplier shall cause service by the previous supplier to be resumed and the new supplier shall bear all costs associated with switching the consumer back to the previous supplier.

- E. Each ~~company~~-*Electric Service Provider* providing service governed by this Article shall be responsible for maintaining in safe operating condition all equipment owned by and under the control of that ~~company~~-*Electric Service Provider* that is used to provide electric service to its customers.
- F. Responsibilities of suppliers of distribution service and of customers receiving distribution service are governed by Subsection R14-2-208.
- G. Each ~~company~~-*Electric Service Provider* providing service governed by this Article shall be responsible for meeting applicable reliability standards and shall work cooperatively with other companies with whom it has interconnections, directly or indirectly, to ensure safe, reliable electric service. Construction standards and safety for each ~~company~~-*Electric Service Provider* providing service under this Article are governed by Subsection R14-2-208(F).
- H. Termination of service.
1. Termination of service prior to the termination date specified in the contract with the consumer is governed by Subsection R14-2-211.
 2. In addition to the above requirement, any ~~provider of service~~-*Electric Service Provider* to consumers shall provide at least 14 days notice to all of its affected consumers if it is no longer obtaining generation, transmission, distribution, or ancillary services necessitating that the consumer obtain service from another supplier of generation, transmission, distribution, or ancillary services.
- I. All ~~companies~~-*Electric Service Providers* providing service under this Article shall provide accident reports as provided in Subsection R14-2-101.
- J. ~~A company~~-*An Electric Service Provider* providing firm electric service governed by this Article shall make reasonable efforts to reestablish service within the shortest possible time when service interruptions occur and shall work cooperatively with other companies to ensure timely restoration of service where facilities are not under the control of the ~~company~~-*Electric Service Provider*.
- K. Each ~~company~~-*Electric Service Provider* providing service governed by this Article shall bill monthly for services rendered. The following minimum information must be provided on all customer bills, whether the bill is rendered by the ~~company~~-*Electric Service Provider* or by another party on behalf of the ~~company~~-*Electric Service Provider*:
1. The amount of each service provided.
 2. The monthly charges for each service provided.
 3. The ~~company's~~-*Electric Service Provider's* toll free telephone numbers for billing, service, and safety inquiries and the telephone number of the Consumer Services Section of the Arizona Corporation Commission Utilities Division.
 4. The amount or percentage rate of any privilege, sales, use, or other taxes that are passed on to the customer as part of the charge for the service provided.
 5. The date on which the bill becomes delinquent.

- L. ~~A company~~ *An Electric Service Provider* providing service governed by this Article may include in its tariffs a fee for each instance where a customer tenders payment with an insufficient funds check.
- M. ~~A company~~ *An Electric Service Provider* providing service governed by this Article may include in its tariffs a late payment penalty which may be applied to delinquent bills. The amount of the late payment penalty shall be stated on the customer's bill.
- N. Working group on system reliability and safety:
1. The Commission shall establish, by separate order, a working group to monitor and review system reliability and safety.
 - a. The working group may establish technical advisory panels to assist it.
 - b. The working group shall commence activities by the date indicated in Subsection R14-2-xxx2.
 - c. Members of the working group shall include representatives of Staff, consumers, utilities, and other suppliers.
 - d. The working group shall be chaired by the Director of the Utilities Division of the Commission or by his or her designee.
 2. All ~~companies~~ *Electric Service Providers* governed by this Article shall cooperate and participate in any investigation conducted by the working group, including provision of data reasonably related to system reliability or safety.
 3. The working group shall report to the Commission on system reliability and safety annually, and shall make recommendations to the Commission regarding improvements to reliability or safety, with the first report due no later than March 31, 1998.
- O. Affected Utilities and other ~~parties~~ *Electric Service Providers* offering service under the provisions of this Article shall comply with applicable reliability standards and practices established by the Western Systems Coordinating Council and the North American Electric Reliability Council or successor organizations.
- P. Affected Utilities and other ~~certificated companies~~ *Electric Service Providers* shall provide notification and informational materials to *its* consumers about competition and consumer choices as ordered by the Commission.

R14-2-xxx14. Reporting Requirements

- A. Reports covering the following items shall be submitted to the Director of the Utilities Division by Affected Utilities and all ~~companies~~ *Electric Service Providers* granted a Certificate of Convenience and Necessity pursuant to this Article. These reports shall include the following information pertaining to competitive service offerings, Buy-throughs, Unbundled Services, and Standard Offer services:
1. Type of services offered.

2. kW and kWh of sales, disaggregated by customer class (e.g., residential, commercial, industrial).
3. ~~Solar energy~~ *Renewable Energy Resource* sales (kWh) and sources.
4. Revenues from sales by customer class (e.g., residential, commercial, industrial).
5. Number of customers disaggregated by size of contract load (0-99 kW, 100 kW-499 kW, 500 kW-999 kW, 1 MW-9.999 MW, 10 MW-49.999 MW, and 50 MW and above).
6. Number of customers disaggregated by class (e.g., aggregators, residential, commercial, industrial).
7. kWh sales and revenues disaggregated by term of the contract (less than one year, one to four years, longer than four years), and by type of service (for example, firm, interruptible, other).
8. Amount of and revenues from each service provided under Subsection R14-2-xxx5, and, if applicable, Subsection R14-2-xxx6.
9. Value of all Arizona specific assets and accumulated depreciation.
10. Other data requested by Staff or the Commission.

B. Reporting Schedule:

1. For the period through December 31, 2003, semi-annual reports shall be due on April 1 (covering the previous period of July through December) and October 1 (covering the previous period of January through June). The first such report shall cover the period January 1 through June 30, 1998.
 2. For the period after December 31, 2003, annual reports shall be due on April 1 (covering the previous period of January through December). The first such report shall cover the period January 1 through December 31, 2004.
- C. The information listed above may be provided on a confidential basis if reasonable to do so. However, Staff or the Commission may issue reports with aggregate statistics based on confidential information that do not disclose data pertaining to a particular seller or purchases by a particular buyer.
- D. Any ~~company~~ *Electric Service Provider* governed by this Article which fails to file the above data in a timely manner may be subject to penalty imposed by the Commission or may have its Certificate rescinded by the Commission.
- E. Any ~~company~~ *Electric Service Provider* holding a Certificate pursuant to this Article shall report to the Director of the Utilities Division the discontinuation of any competitive tariff as soon as practicable after the decision to discontinue offering service is made.
- F. In addition to the above reporting requirements, ~~companies~~ *Electric Service Providers* governed by this Article shall participate in Commission workshops or other forums whose purpose is to evaluate competition or assess market issues.

- G. Reports filed under the provisions of this Subsection R14-2-xxx14 shall be submitted in written format and in electronic format. ~~Companies~~ *Electric Service Providers* shall coordinate with the Commission Staff on formats.

R14-2-xxx15. Administrative Requirements

- A. Each ~~company~~ *Electric Service Provider* governed by this Article shall file with the Director of the Utilities Division a written statement containing the name, business address, and telephone numbers of at least one officer, agent, or employee responsible for the general management of its Arizona operations. This information shall be updated, in writing, within five days from the date of any change.
- B. Any ~~company~~ *Electric Service Provider* certificated under this Article may propose additional services at any time by filing a proposed tariff with the Commission describing the service, maximum rates, terms and conditions. The service may not be provided until the Commission has approved the tariff.
- C. Contracts filed pursuant to this Article shall not be open to public inspection or made public except on order of the Commission, or by the Commission or a Commissioner in the course of a hearing or proceeding.
- D. Each ~~company~~ *Electric Service Provider* governed by this Article shall keep general and subsidiary accounting books and records reflecting the cost of its Arizona properties, assets and liabilities, operating income and expenses, and all other accounting and statistical data which reflect complete, authentic, and accurate information regarding its properties and operations. These records shall be organized and maintained in such a way as to provide an audit trail through all segments of the ~~company's~~ *Electric Service Provider's* accounting system.
- E. Each ~~company~~ *Electric Service Provider* governed by this Article shall maintain its books and records in accordance with Generally Accepted Accounting Principles as promulgated by the Financial Accounting Standards Board and its successors, as amended.
- F. All ~~companies~~ *Electric Service Providers* governed by this Article shall immediately make available, at the time and place the Commission may designate, any accounting and related records pertinent to the subject matter of this Article that the Commission may request.
- G. All ~~companies~~ *Electric Service Providers* governed by this Article shall file with the Director of the Utilities Division a copy of all annual reports required by the Federal Energy Regulatory Commission or by the Securities and Exchange Commission.
- H. The Commission may consider variations or exemptions from the terms or requirements of any of the rules in this Article upon the application of an affected party. The application must set forth the reasons why the public interest will be served by the variation or exemption from the Commission rules and regulations. Any variation or exemption granted shall require an order of the Commission. Where a conflict exists

between these rules and an approved tariff or order of the Commission, the provisions of the approved tariff or order of the Commission shall apply.

- I. The Commission may develop procedures for resolving disputes regarding implementation of retail electric competition.

EXHIBIT B

COMPETITION IN THE ELECTRICITY MARKET

SRP's Position On Industry Restructuring and Customer Choice

The restructuring of the electric industry is being discussed throughout our nation. The catalyst for these discussions is the desire of electricity customers for a choice of provider, lower cost electricity service, and enhanced service options.

SRP's mission is to be the best water and power organization, dedicated to improving service, lowering costs, resource stewardship, and market focus through involved change-oriented employees.

SRP Supports Customer Choice Of Generation Provider

In keeping with this mission and SRP's long history of meeting customer needs and expectations, SRP's board of directors supports an electric industry in which customers are free to choose the generation provider that delivers the highest value products and services.

Industry restructuring should not introduce new rules to limit or eliminate the number or types of providers in the marketplace. To do so would reduce competition in the electricity market.

Choice of generation supplier should begin by the year 2000, and, when appropriate, should be phased-in for all customers thereafter. This schedule allows adequate time to consider the economic, social, financial, technical, operational, system planning and environmental implications of an industry restructuring.

Distribution Monopolies Will Remain

SRP's board believes that the electricity industry should be characterized by a fully competitive generation market in which all customers will eventually have choice of generation provider; a federally-regulated, tariff-based "open access" transmission system; distribution service territories operating under the existing regulatory framework and territorial agreements; and a fully-competitive market for energy services.

Distribution systems will remain monopolies and will be managed and operated by traditional suppliers under existing state laws, regulatory structures, tax obligations and public responsibilities. Existing territorial agreements and Commission-granted certificates of convenience and necessity will remain in effect for distribution services.

Traditional distribution suppliers will ensure reliable operation of the electrical system.

SRP Will Continue As A Political Subdivision

SRP will continue as a political subdivision of the state of Arizona ("Traditional SRP"). Traditional SRP will provide a full range of electricity service to retail customers (should they choose SRP for their generation needs) within its existing service territory. Traditional SRP will do business under existing state law and regulatory structures, and in particular, will continue to fulfill its responsibilities for the storage and delivery of water within its traditional water service area.

Assuming appropriate statutory and regulatory requirements provide for reciprocal service among electric utilities, customers in SRP's service territory would be free to choose an alternative supplier for their electricity supply and energy services needs.

The continued operation of SRP and other non-public service corporations within traditional territories under existing state law and regulatory structures is appropriate. The different structures of industry participants, investor-owned and public power utilities, result in certain tax and financial benefits and burdens that differ for each participant. Each structure carries with it its own set of advantages and disadvantages that result in roughly equal competitive positions for both structures.

SRP will form an Affiliate to Compete Outside Its Service Territory

To facilitate the implementation and acceptance of retail competition in Arizona, SRP will form an affiliate to do business outside its traditional service area. The affiliate will be subject to equivalent rules and requirements as other players in the competitive sector, including appropriate tax obligations and regulatory requirements.

SRP's board plans to operate as a traditional supplier within SRP's service territory and to form an affiliated power marketer to compete outside its service territory in the retail wheeling arena.

As customers choose alternate suppliers, SRP will contract with its non-traditional affiliate to market surplus, including the output of assets stranded by these customers, putting resources to effective use. SRP's affiliate will compete for retail customers with other competitive, non-traditional suppliers. It will be subject to equivalent rules and requirements as other players in the competitive sector, including appropriate tax obligations and regulatory requirements. It will not be bound by agreements pertaining to service area. SRP's affiliate will contract for additional resources to maximize the value of resources contracted from Traditional SRP.

All competitive suppliers will participate in the market under laws, rules and structures applicable specifically to the competitive sector. They will have the ability to compete and provide generation and energy services to all customers and will acquire new resources to do so. In the public interest, all market participants must comply with reliability criteria established by the North American Electric Reliability Council (NERC) and the Western Systems Coordinating Council (WSCC).

SRP believes the foregoing is a fair and balanced structural outline, preserving the benefits of traditional suppliers (delivery, reliability, obligation to serve), embracing the benefits of competitive suppliers (choice and competition), and enabling existing traditional suppliers to compete in the competitive sector, on equal footing, with all participants. Work is continuing on defining the details of this proposed approach.

SRP PROPOSAL FOR A RETAIL WHEELING PILOT PROGRAM

If a pilot program were implemented, how should it be implemented? We are seeking specific proposals on implementing the activities listed on Attachment A in a pilot program. Your suggestions could be formulated as tariffs or rules which would then be implemented by the Commission and by utilities, other suppliers of electricity, and consumers.

Choice of generation supplier should begin by the year 2000, and should be appropriately phased-in for all customers thereafter. This schedule allows adequate time to consider the economic, social, financial, technical, operational, system planning and environmental implications of an industry restructuring.

In keeping with this timetable, SRP management proposes the Commission establish a Working Group on a Pilot Retail Wheeling Program in Arizona. The Working Group should be made up of industry experts from Arizona utilities, Commission Staff, RUCO, new market players and representatives from each of the major customer classes. The Working Group should review the issues involved and simulate the elements of a pilot program.

In addition, the Working Group should obtain, study and analyze the results of pilot programs in other states to obtain the answers necessary to implement choice of generation provider in Arizona.

The Working Group should be established by December 31, 1996, and should develop, implement and evaluate a simulated program and provide results to the Commission by January 1, 1998.

SRP management believes that a simulated pilot program, as described above, will allow for a more orderly introduction of customer choice than the implementation of a physical pilot program. A physical pilot program is not the most effective means of investigating and addressing issues arising from retail wheeling. A simulated pilot program does not present any constitutional, statutory and regulatory issues which might be raised if a physical pilot is adopted. The combination of information from pilot programs currently underway in other states and experience from a simulated pilot program should allow the successful introduction of retail electric competition in Arizona in a timely and cost-effective manner. In addition, a physical program may develop customer expectations that are unachievable in a fully competitive market

SRP Recommendations if ACC Proceeds With Physical Pilot Program

If the Arizona Corporation Commission believes and decides that a physical pilot program is necessary, SRP management proposes that the Commission establish a Working Group as described above. The Working Group should formulate a mutually agreeable pilot program that will enable the Commission to identify problems with open access and be in a position to develop solutions for these problems.

The Working Group should be established by December 31, 1996, and should provide a detailed recommendation to the Commission by January 1, 1998. The Commission should take appropriate action for a retail wheeling pilot program to start June 1, 1998. The timetable for restructuring the electric industry in Arizona should be adjusted accordingly.

The following framework is proposed for consideration by the Working Group.

Framework for Retail Wheeling Pilot Program

PHASE-IN

The physical pilot program should be phased-in, starting with industrial customers. If a successful pilot of industrial customers is accomplished, then the pilot should be expanded to include commercial, and with continued success should be further expanded to include all customers.

SIZE:

The physical pilot program should be limited to a specific number of customers.

	Number
Industrial	10 customers
Commercial	25 customers
Residential	100 customers

Total participation would be limited to 25 megawatts in 1st year and 50 megawatts in 2nd year. All schedules from supplier to local utility must be scheduled on a whole megawatt basis.

TERM:

The pilot program would commence June 1, 1998, and last for two years.

SELECTION:

Use a lottery system. Announce the pilot and have customers submit an application answering specific questions about the location of load, etc. Allow enough time to advertise the pilot, develop and send out applications, receive responses, pick those selected and notify those selected through direct contact and local advertising.

ENERGY SUPPLY:

A list of potential generation suppliers must be available to those selected. For the pilot program, one utility should solicit bids for suppliers and post these bids. The suppliers would provide energy and capacity needed to meet the specific program the customer has signed up for and deliver it to the host utility using Western Systems Coordinating Council scheduling procedures.

OPTIONS:

All options should be evaluated by the Working Group, with close consideration of the costs and benefits of each option. The following options should be considered by the Working Group.

a) Standard kWh Meter

Energy from supplier would be scheduled on a static basis and would meet at least part of the forecasted energy needs of customer.

The local host utility would continue to provide regulation, backup reserves, transmission, distribution, etc.

b) New Time of Use Meter

Computers belonging to the by host utility would interrogate and record usage.

Schedule from suppliers would change hourly to meet changing customer demand but would be static during each hour.

The local "host" utility would continue to provide regulation, backup reserves, transmission, distribution, etc.

c) New Telemetry System

The wholesale supplier and local utility would transmit usage instantaneously on a dynamic basis. Usage must be greater than 1 megawatt and would be tracked on a whole megawatt basis.

The local "host" utility would provide essentially "zero" load regulation. Regulation is provided by the wholesale supplier.

For the pilot program, the local "host" utility would continue to provide backup reserves, transmission, distribution, etc. In the future, backup reserves, which should be provided as a separate ancillary service, must be paid for and customers must have a meter with remote disconnect capability.

COST OF PILOT:

Customers requiring special metering should pay for that metering, if they are to benefit from lower energy rates. Given the timeframe of the pilot program and the number of meters involved, participants should lease meters in order to have a truer indication of the costs involved.

BILLING:

Customer bills would be modified to reflect unbundled services. Charges from the generation supplier should be clearly separated from the local utility charges. Local "host" utility ancillary costs would be included in the customer's monthly bill.

Conclusion

SRP management believes that a simulated pilot program will allow for a more orderly introduction of customer choice than the implementation of a physical pilot program. If the Arizona Corporation Commission believes and decides that a physical pilot program is necessary, SRP management believes that the aforementioned process elements are essential to a physical pilot program. Participation by SRP in a physical pilot program is subject to appropriate legal authority, and approval by SRP's Board of Directors.

**SRP RESPONSE TO ARIZONA CORPORATION COMMISSION
QUESTIONS REGARDING ELECTRIC INDUSTRY
RESTRUCTURING**

A1. Affected Utilities. Which utilities should open their markets to competition?

Every utility should have the option of participating in the competitive market place. No utility should be precluded from offering choice of generation provider to customers in its service area if it chooses to do so.

However, reciprocity must apply. Utilities who offer choice of generation providers to customers must have reciprocal rights to compete for customers in the service territories of all other utilities who choose to participate, either directly or through an affiliated power marketer. The absence of reciprocity would severely hamper the competitive market and could lead to unfair competitive advantage by some players.

Industry transformation should not introduce new rules to limit, eliminate or restrict the number or types of providers in the marketplace. To do so would reduce competition in the electricity market and reduce the range of choices available to customers.

The continued operation of SRP and other non-public service corporations within traditional territories under existing state law and regulatory structures is appropriate. The different structures of industry participants, investor-owned and public power utilities, result in certain tax and financial benefits and burdens that differ for each participant. Each structure carries with it its own set of advantages and disadvantages that result in roughly equal competitive positions for both structures.

A2. Scope of Restructuring.

a. How much of the utilities' markets should be opened to competition?

SRP believes that the electricity industry will be characterized by a fully competitive generation market in which all customers will eventually have choice of generation provider; a federally-regulated, tariff-based "open-access" transmission system; distribution monopoly service territories operating under the existing regulatory framework; and a fully-competitive market for energy services.

- b. **Which consumers should be allowed to shop around for power and energy? Consider both geographic areas and consumer classes.**

SRP believes that all customers eventually, and when appropriate, should have choice of generation provider.

- c. **Should utility customers served under existing contracts be eligible to participate in the competitive market prior to expiration of the existing contracts?**

Customers with existing contracts should participate in the competitive market upon expiration of the contracts unless otherwise mutually agreed by the customer and the contracting utility.

- d. **If divestiture were undertaken, how should it be accomplished?**

SRP does not support mandatory divestiture. SRP believes that in a fully competitive marketplace, market forces would be sufficient to ensure that utilities and other industry participants make appropriate decisions to successfully provide reliable, competitively priced electricity to customers.

A3. Term of Restructuring.

- a. **When should competition start?**

Choice of generation supplier should begin by the year 2000, and should, when appropriate, be phased-in for all customers thereafter. This schedule would allow adequate time to consider the economic, social, financial, technical, operational, system planning and environmental implications of an industry restructuring. All suppliers who intend to participate in the competitive market, when such market is implemented, should have the opportunity to begin participating at the same time. This will ensure that customers of all entities that choose to participate will have choice of generation supplier at the same time, and no supplier, or customer, is disadvantaged..

- b. **If competition is in the form of a pilot or phase-in, how long should the pilot or phases run? Please describe the phases of a phase-in. Please consider that many larger customers of utilities are currently under contract and may not be able to shop around until those contracts expire.**

See previous comments on pilot program.

- c. **If competition is in the form of a pilot, how can the term of the pilot be set so as to avoid discouraging long term contracts signed under the pilot?**

A simulated pilot program would allow interested parties to evaluate the impacts of retail wheeling without the need for new contracts.

A4. Services Available on a Competitive Basis. Which services should be available in a competitive market?

- Distributed energy services at market based rates (serving multiple consumers located in proximity, and not requiring transmission service from others); this is distinct from on-site self generation for just one consumer.**

See below.

- Central station generation services at market based rates (generation serving one or more consumers located at a distance from consumers and requiring transmission service).**

See below.

- Other services described in Sections A5, A6, A7, and A8.**

See below.

- Other services (please describe).**

Historically the legislative and regulatory framework has treated the U.S. electric industry as one industry - - integrated through the generation, transmission and distribution sub-markets - - with the belief that a natural monopoly existed in each of these sub-markets. Technological and philosophical changes have led policymakers to conclude that a natural monopoly no longer exists in the generation market. In addition, a new market is forming in energy services which includes the procurement of electricity supply.

Consequently, changes to each sub-market will be different. The generation or power development and production business of the future will be fully competitive. All customers, eventually, when appropriate, will have a choice of generation provider.

The transmission business is moving toward a federally-regulated tariff-based "open access" system under the Federal Energy Regulatory Commission (FERC). Many of these changes currently taking place were initiated by passage of the Energy Policy Act of 1992 and regulatory guidelines put in place by FERC. FERC Order 888 has made open access to the transmission system the industry standard. SRP is developing open access tariffs and will file them the Southwest Regional Transmission Association (SWRTA).

The distribution business essentially is a natural monopoly and therefore should stay a regulated, service-territory business under existing regulatory frameworks and laws.

A fully-competitive market is developing for energy services. Customers will choose who would procure generation for them, as well as energy-related services beyond normal distribution services.

Within this new overall structure of competitive generation and energy services, open access transmission, and locally-regulated, monopoly distribution there would be two types of electricity service suppliers with different purposes, roles and responsibilities - "traditional" and "non-traditional" suppliers.

Traditional Suppliers: These entities would continue to provide the full range of services to customers in existing service territories under existing laws, regulatory structures, tax obligations and public responsibilities. Existing territorial agreements and Commission-granted certificates of convenience and necessity would remain in effect.

Traditional suppliers would have an obligation to serve that, minimally, would cover delivery of power. For customers other than those who, either individually or by aggregation, have a peak load of 1 MW or greater for three consecutive months, the obligation would also extend to generation or reserves therefor, for which the traditional supplier would be due just compensation.

SRP believes a level of 1 MW would provide an adequate measure of which customers could potentially obtain favorable deals from traditional suppliers to the detriment of the traditional supplier's other customers. However, as market conditions change, this level may change, and SRP believes that periodic assessments should be undertaken to determine an appropriate threshold.

Traditional suppliers would ensure reliable operation of the electrical system.

Direct access to generation and energy services would be phased in, eventually, when appropriate, for all customers. Customers within a traditional supplier's service territory would have choice of providers for generation and energy services. Other entities could sell generation and energy services to these customers.

As some customers choose alternate suppliers, traditional suppliers would need a mechanism to market assets stranded by these customers, thus putting

resources to effective use to the benefit of customers and investors. Traditional suppliers could, if deemed appropriate, form non-traditional affiliates to compete with all players in the competitive market. Alternatively, traditional suppliers could choose to compete directly without the formation of an affiliate, subject to rules and regulations applicable to non-traditional suppliers. System economics would be protected and improved for the benefit of customers and investors. Existing resources would be put to beneficial use to the extent that entities have the competitive capability to do so.

Non-Traditional Suppliers: These entities would compete for retail customers with traditional suppliers and other non-traditional suppliers in the traditional supplier's service territory. Non-traditional suppliers would compete in the market under equivalent rules and comparable structures. They would have the ability to compete and provide generation and energy services to all customers and would acquire new resources to do so. Non-traditional suppliers would have no obligation to serve.

A5. Necessary Services. Utilities and perhaps other parties will have to address the services listed below. Please indicate how these services should be offered, measured (metered), and priced on an unbundled basis.

The services listed below are necessary for the reliable provision of electricity to retail customers. Retail customers now pay traditional electric suppliers for these services on a bundled basis through the traditional supplier's retail rates. Under competition, the arrangement for these services may change for some customers, but not necessarily for others.

Large manufacturing or industrial customers may want to arrange for these services in the same manner that wholesale customers arrange for service. These customers would likely make separate arrangements for each service from their traditional electric supplier or from a non-traditional supplier where applicable in order to access or shop competitive markets on their own.

Residential and small commercial customers may want their non-traditional suppliers of electricity to arrange for some or all of these services with the customer's traditional electric provider. These customers may still pay for these services on a bundled basis through the non-traditional supplier's rates. The non-traditional supplier would have to arrange for these services with the customer's traditional electric supplier.

The prices for services that cannot be competitively supplied, typically distribution and transmission related services, should be based upon the costs associated with providing those services plus a reasonable rate of return. The prices for the sale of such services to the traditional electric utility's retail customers would be subject to the current regulatory framework. Existing

federal law and Federal Energy Regulatory Commission (FERC) policy governs how transmission service and associated ancillary services should be priced for purchase by a non-traditional supplier. Again, the prices for distribution related services would be regulated under the existing regulatory framework.

For those services that may be competitively supplied, such as supplemental generation services, market prices should prevail.

The services identified may be measured and priced through several mechanisms. Cost causation principles should apply in all cases. The cost of some services are essentially fixed; these would be attributable to the customer irrespective of use, or attributable to the capacity made available for the customer to use, which is measurable through the maximum kilowatts a customer has used in the past. Some of these costs are more dynamic, and are measurable through a customer's monthly, daily, or hourly kilowatt and kilowatt-hours of use.

○ **distribution service**

The distribution system is defined generally as the system from the meter to the high voltage (transmission) network. Distribution services cover activities required to install and maintain a metered connection to the transmission network.

The costs to provide this service are relatively fixed in nature and could be recovered through a combination of a flat charge and a charge based on the maximum capacity (kilowatts) used by a customer.

○ **transmission service**

The transmission system is generally defined as the high voltage facilities providing a connection between generating resources and the distribution system. Transmission services cover activities required to install and maintain metered connections between generating facilities and the distribution system.

The cost of this service has been guided by FERC's pricing policies; the charge should be related to the amount of capacity reserved by a customer or reserved by a non-traditional supplier.

○ **supplemental generation service**

Supplemental generating services can be defined as generation maintained in standby or backup to replace primary generating services. Without special metering the distribution company would have to provide, or contract for, regulation services. Facilities required to constantly match generating resources and demand must be included as a supplemental service.

These services have elements of both fixed and variable costs. The costs associated with reserving supplemental or back-up generation for a customer would likely be recovered through a capacity reservation charge based on kilowatts. Energy (kilowatt-hour) charges would also apply when energy is actually utilized by the customer. These services may be able to be supplied by a customer's traditional electric supplier, the customer's non-traditional supplier, or by other players in the market.

○ **imbalance service (including accounting for losses)**

Imbalance service is defined as the process of banking energy with the local control area. The difference between monthly kWh metering of demand and the delivery of energy supply each month, to the control area, would be maintained in an account for each retail customer.

Imbalance service might also include the difference between instantaneous customer demand, which is monitored real-time by specific metering, and the instantaneous delivery of energy for that customer's account.

System losses can be covered a number of ways but calculating actual losses for a customer might be applied to energy deliveries or a monetary payment might be considered.

FERC has addressed pricing for this service. FERC guidelines should be applicable.

○ **back-up (standby) service**

Generation back-up service could be tied to supplemental generation service. Generation back-up service requires generating resources.

Transmission backup services could be purchased if a primary path is established between the generation supplier and customer.

For distribution backup service, no change in the current planning criteria is required. The distribution company for a particular geographic area would continue to build redundant services as it does today.

○ **voltage control**

Along with frequency control, voltage control would be provided by the distribution or traditional supplier. Generation and transmission system elements work hand in hand to provide system VAR requirements and thus coordination by system operators is essential.

FERC has addressed pricing for this service. FERC guidelines should be applicable.

- other ancillary services necessary for maintaining system reliability

Dispatchers must watch the system 24 hours each day. Generators, transmission and distribution elements must be scheduled for maintenance and construction. All outages must be coordinated by a central facility.

- scheduling of supplies and demands

Supplies must be scheduled through control areas and must be instantaneously matched with demands. Transmission must be available to move supply to demand. Metered instantaneous demand must be telemetered to the generation supplier and the entity responsible for matching supply and demand. Without special metering, the customer's demand would automatically be included in the local control area's load profile.

The cost of scheduling transmission services is embedded in the price of transmission paid by customers. Where no competition is present, the scheduling of generation services should be priced based on cost-based pricing principles

- repairs/consumer complaints

Customer complaints should be handled by those parties responsible for providing specific services. If a customer has arranged for service through a traditional provider, repairs/consumer complaints should be handled by that provider and those costs should be a part of the cost of providing service.

- other necessary services -- please describe

A6. Market Center Services. The market may benefit from the services listed below. Please indicate how these services should be offered and priced.

SRP believes that the regional market benefits from the availability of market center services. In response to market demand, effective April 1, 1996, SRP has opened the SRP Market Center to offer these types of services. Customers requiring market center services for their energy needs can purchase them from the SRP Market Center.

- title transfer

To satisfy Western System Coordinating Council (WSCC) operating reliability criteria, each entity in a transaction string must designate the entity and control area generating the energy, all contracting intermediaries, and the entity and

control area recovering the energy. If an entity wishes to identify only the parties immediately before or after it in a given transaction, SRP offers bus transfer services for a fixed price per schedule day to research and identify all the other parties in the transaction string.

- **transaction confirmation**

All parties to transactions must be known and must confirm transactions before, during and after-the-fact. To comply with this requirement, a 24-hour dispatch capability is needed. Billing personnel must be connected to transaction checkout. SRP offers scheduling and dispatch services to customers seeking those services. Customer needs vary widely, and therefore SRP provides prices on a case-by-case basis.

- **establishing credit standards**

Membership in the Western Systems Power Pool (WSPP) currently includes a credit worthiness check.

- **invoicing**

SRP is currently developing a variety of billing services including aggregation at multiple transmission path segments, final checkout and invoice preparation and limited dispute resolution services. Since the needs of individual customers vary, prices will be quoted on a case-by-case basis, although SRP expects a market for standardized products, and hence prices, to develop.

- **dispatching of transmission/generation**

Dispatching services should be a required service for electricity purchasers, although SRP offers integration and dispatch if operational conditions permit.

- **exchanges/swaps**

- **interruption notification**

Customers located in SRP's service area may choose not to purchase backup supply from SRP if they purchase their electricity from an alternate supplier. Upon loss of their alternate supplier, SRP will interrupt service. SRP will provide notification of reasons for interruption to customers in this situation.

- imbalance trades

SRP can provide a mechanism for different customers or groups of customers with equal and off-setting energy balances to zero out those account balances. SRP is developing terms and conditions and a fee for this service.

A7. Spot Market Services. The market may benefit from the services listed below. Please indicate how these services should be offered and priced.

- electronic bulletin boards for spot transactions/prices

See below.

- power pooling services

See below.

- coordination with futures/options markets

Electronic bulletin board service will be offered on the region-wide Transmission Information Services Network (TSIN) being developed by SRP and other utilities in the region. SRP has offered to any of the transmission providers in the region an opportunity to participate in and use the TSIN to post their transmission and ancillary services that FERC's Order 888 might require.

While developed to post transmission availability and pricing information, the TSIN will have the flexibility to post other information. This information can be data for marketing products or services. Such information could be spot transaction/prices and power pooling services.

A8. Transmission Service. For a competitive market to work, utilities owning transmission facilities must provide transmission service. Please indicate how the following objectives would be met:

- services must be provided consistent with FERC tariffs.

See below.

- utilities must accept power delivered to their transmission systems by other suppliers and offer wheeling services comparable to services they provide to themselves.

See below.

- all sellers supplying consumers must have interconnection agreements with owners of necessary transmission facilities.

As discussed in section A7, the development of the TSIN will provide all the transmission provider's transmission availability and pricing information plus additional back up information. Historical transactional information will also be posted primarily for audit purposes.

Under FERC Orders 888 and 889, all transmission users, including the host utility and affiliates, will have to request and purchase the transmission service they need through the TSIN. Through the Regional Transmission Groups, transmission service will also be made part of a transmission provider's tariff. The transmission providers must offer transmission service not being used to anyone on a nondiscriminatory basis. The RTG's define what transmission capability they can reserve for themselves through the TSIN. The remaining capacity on an hourly, weekly, monthly and yearly basis through a 10 year period must be made available (Available Transfer Capability or ATC) to anyone by the transmission provider. SWRTA bylaws make it clear that transmission providers include both transmission owners and those holding contract rights.

While one is not sure what ancillary services will be have to be offered through the FERC tariff, whatever ancillary services that are offered must be posted on the TSIN.

As noted above, requests for transmission service will be made through the TSIN. Before a request can or will be granted, both parties must execute an agreement to define the transmission providers obligations and limitations for service. The agreement will also identify the users' obligations such as paying for the service.

A9. Recovery of Stranded Investment. Please indicate how the recovery (if any) of stranded investment should be accomplished. Address each of the following issues:

- a. The definition of stranded investment.

See below.

- b. **The fraction of stranded investment which should be recovered.**

See below.

- c. **How the Commission will determine the amount of stranded investment, taking into account: revenues under traditional tariffed rates (or existing special contracts); actual utility revenues from customers who obtain discounted rates or obtain service from others; increases in net revenues from wholesale sales and additional retail sales, including the effects of price elasticity of demand; increases in the value of assets due to new pricing or competition; mitigation of stranded investment; and other relevant factors.**

See below.

- d. **Preliminary estimates of the magnitude of stranded investment (please provide supporting analyses).**

See below.

- e. **The proper ratemaking treatment of negative stranded investment.**

See below.

- f. **From whom stranded investment should be recovered.**

See below.

- g. **The mechanism for recovery of stranded investment.**

See below.

- h. **The time period over which stranded investment is to be recovered.**

See below.

- i. **How utilities can mitigate stranded investment?**

See below.

All industries which have undergone the transformation from a regulated to a market system have had to deal with transition issues. As the electric utility industry evolves towards an environment characterized by customer choice for generation suppliers, one of the critical transition issues to be addressed is

stranded cost recovery. Given the critical implications as to the length of the transition period and key assumptions as to the computation of stranded costs, SRP will address this question generically, recognizing that specific responses to the sub-questions set forth in the Commission's docket item can change based on the assumptions that are used.

Because the implications of retail stranded investment depend on the timetable for the introduction of retail wheeling, SRP advocates a reasonable transition period in which utilities should work through any variety of approaches to mitigate any potential stranded cost exposure. The objective should be to eliminate all such costs within a reasonable transition period of eight to ten years. However, an overriding proviso should operate to avoid negative consequences for all customer classes and for investors. In this regard, the stranded investment equation should not be looked at as a "zero sum game," wherein some customer classes or investors benefit at a cost to others.

"Stranded investment" consists of those legitimate, prudently incurred costs that may be avoided by a departing customer who switches energy suppliers. Costs stranded by self-generation or relocation are not considered stranded investment. Similarly, under SRP's assumption that the transmission system will be a federally regulated, tariff-based system, and that distribution service monopolies will continue, some transmission costs and most distribution costs should not be considered stranded investment. Rather, stranded costs principally include generation, the cost of which may exceed anticipated future market prices; decommissioning and environmental costs which are not reflected in rates; demand-side management obligations and uneconomic federal, state or local mandates; and regulatory assets consisting of various cost deferrals arising from resource contract buydowns, debt refinancings and in the case of investor owned utilities, deferred taxes and generation investment which are excluded from current rate base calculations. Consistent with the foregoing, Power Marketing Administration (PMA) output should be considered as a stranded benefit of the customers who have purchased it. Those customers have relied on the legislative and regulatory system that provided them with this output, and as the system changes, those customers should have the opportunity to purchase those assets at book value.

As electric industry participants in California and in other states have learned, agreement on the recovery of stranded costs is essential in the transition to a restructured industry. FERC recognized this in its Order 888 which provides for full recovery of stranded costs associated with wholesale requirements contracts signed before July 11, 1994, and contractual recovery of such costs after that date. This Order permits recovery of wholesale stranded costs from departing customers.

Unlike investor-owned utilities, locally-owned utilities such as SRP have no equity owners to help absorb the costs of assets built in a prior environment

which may be rendered uncompetitive in a deregulated environment. Additionally, to the extent they recover stranded investment, the tax-exempt status of bonds used to finance those assets may be jeopardized under complex IRS private use regulations that have yet to be finalized. The consequences of running afoul of these regulations, even in their proposed form, are serious and can result in the interest on said bonds becoming taxable to the investor, absent costly early redemption of the debt by the issuer. Irrespective of the problems posed by these regulations, an exit fee or "wires charge" may ultimately prove to be bad public policy and damaging to customer relationships which are so essential in a truly competitive marketplace.

The only other recourse would be to raise customer rates to recover stranded investment.

Instead, SRP advocates affording market participants flexibility in recovering stranded costs by allowing an adequate period of time in which to deal with this critical transition issue equitably, and without negative consequences to customers and investors. Moreover, in the case of locally-owned utilities such as SRP, it is essential that investments which may become stranded as a result of departing customers can be remarketed, as necessary, to supply new customers outside historic territorial boundaries, subject to the laws, rules and structures set forth for the competitive sector. This solution will result in the fair and economic use of resources and work to the benefit of all customers.

A10. Recovery of Costs of Commission-Mandated Utility Low Income, DSM, Environmental, Renewables, and Nuclear Power Plant Decommissioning Programs ("Mandated Programs").

- a. How shall costs of mandated programs be recovered from participants in the competitive market?

See below.

- b. How shall the magnitude of the costs of mandated programs be determined?

With the opening the electric industry to competition, market mechanisms will drive both the demand and supply of generation, resulting in the optimal allocation, mix and use of scarce energy. Any government policies regarding resource mix and energy efficiency should be implemented through mechanisms outside of the competitive marketplace. For example, a fee tied to distribution service is one way to recover such costs.

A11. Encouragement of Renewables.

- a. **How shall renewables be encouraged in a competitive environment? Please discuss such mechanisms as a requirement that x percent of energy sold in the competitive market must come from solar resources.**
- b. **How could progress in encouraging renewables be measured?**
- c. **How could a renewables program be enforced by the Commission?**

See response to A10.

A12. Pooling of Generation and Centralized Dispatch of Generation or Transmission.

- a. **Should pooling of generation or centralized dispatch of generation or transmission be mandatory or voluntary?**

Formation of transmission and generation pooling arrangements, or centralized dispatch should be approached on a voluntary basis. Where it makes sense to establish such pools, they will be formed by those interested in doing so under terms that best apply to the specific situation.

On the wholesale level in Arizona, and in the west in general, utilities have demonstrated a willingness to foster open competition, have established an active wholesale market, and have embraced the concept of Regional Transmission Groups, such as SWRTA. It took several years to establish SWRTA but now interested parties have a forum to bring transmission issues forward for resolution.

Looking at SWRTA and the wholesale market as an example, it takes a significant amount of effort to establish arrangements that address the positions of the many participants in the utility market. The development of a centralized operation for generation and transmission would also likely be a long complex process. Furthermore, at this time it is difficult to show that the benefits provided by this type of operation over that those from the voluntary development would exceed the costs of its development and operation.

Today there are others who are working to develop centralized dispatch arrangements and centralized transmission operation (Independent System Operators), such as the PJM Power Pool, and the recent activities in California. SRP believes that it is prudent to watch the development of these pools and learn

from their experiences before consideration is given to mandating similar arrangements for utilities in Arizona.

- b. **What technical requirements will be necessary to ensure reliable and efficient use of generation and transmission resources? Please propose specific requirements, if possible.**

Given that centralized operation should not be mandated, it is unnecessary to establish additional technical requirements at this time.

A13. Non-Public Service Corporations. How shall non-public service corporations such as municipal utilities be involved in a competitive market? For example, the service territories of Arizona utilities not regulated by the Commission may not be open to competition and Arizona utilities not regulated by the Commission may not be able to compete for sales in the service territories of the utilities identified in Section A1. Alternatively, an Arizona utility not regulated by the Commission may voluntarily participate in a competitive program if it makes its service territory available to competing sellers and if it agrees to all of the requirements of the Commission's competitive program.

The purpose of a competitive electric industry is to increase efficiency and lower costs. In this environment, well-managed, efficient and innovative companies, whether existing entities or new entrants, will survive and prosper, regardless of what organizational form they take. Competition will not discriminate: the market will dictate which providers survive. Industry transformation should not introduce new rules to limit, eliminate, or restrict the number or types of providers in the marketplace. To do so would reduce competition in the electricity market.

Territorial agreements may require modification to facilitate the introduction of competition in the electric industry. To the extent that such modification is necessary or appropriate, parties should proceed to develop and implement such modification.

The different structures of industry participants, investor-owned and public power utilities, result in certain tax and financial benefits and burdens that differ for each participant. Each structure carries with it its own set of advantages and disadvantages that result in roughly equal competitive positions for both structures.

To facilitate the implementation and acceptance of retail competition in Arizona, SRP will form an affiliate to do business outside its traditional service area. The affiliate would meet all applicable requirements of a competitive program and compete on the same footing and basis as other non-traditional suppliers. Other

locally-owned utilities may have different proposals to meet any requirements of a competitive program. SRP's proposal does not speak for other locally-owned utilities other than SRP.

A14. Conditions for Returning to Utility Service After the Conclusion of a Pilot Program. If a pilot were adopted, please indicate what conditions are appropriate for returning utility service after the conclusion of the pilot.

A simulated pilot program will allow interested parties to evaluate the impacts of retail wheeling without the need for customers to leave existing utility service.

A15. Conditions for Returning to Utility Service. Please indicate what conditions (if any) are appropriate for returning to utility service if a competitive market is on-going.

Traditional suppliers would have an obligation to serve that minimally covers delivery of power. For customers less than 1 MW, the obligation would also extend to generation or reserves therefor, for which the traditional supplier is due just compensation, including those who wish to return after purchasing generation or other energy services from other providers, although they could be subject to differential pricing.

Customers of 1 MW or more are those who by virtue of their size, individually or through aggregation are in a strong position to obtain electric service under terms and conditions that would be detrimental to other customer segments and individual customers.

A16. Administrative Requirements.

- a. **A utility may require consumers obtaining generation from another entity to adhere to reasonable scheduling notification requirements, accept reasonable delivery points, adhere to reasonable metering requirements, and accept reasonable remote control requirements for interruptions or other purposes. Please specify what you consider to be reasonable.**

All transactions scheduled from one control area to another must comply with NERC and WSCC guidelines for system reliability.

b. How should the utilities identified in Section A1 notify their customers of the adoption of a competitive program by the Commission?

Each electric utility should be responsible for designing and implementing its own procedures for notifying its customers of the available competitive program options. Each utility should have the flexibility to develop notification procedures, such as media advertising, direct mail and interviews, that it believes most appropriate for its particular customer base. Additionally, this will allow utilities to design procedures tailored to various classes of customers served.

Information on generation provider choices would be made available by those competing in the market.

A17. Impacts on Other Utility Customers. Please indicate how adverse impacts on rates or service quality for utility customers not participating in the competitive market could be minimized.

Under competition, all customers should benefit from lower costs and increased services, including those not participating in the competitive market. Service to those customers participating in the competitive market must not be subsidized by traditional utility customers who do not participate.

A18. Reporting Requirements for All Sellers of Electricity to End Users. Please indicate what reporting requirements (to the Commission) are appropriate and who should file reports.

SRP believes the current framework for reporting should be maintained for existing electric utilities.

"New entrants" into the Arizona electric market should be subject to some type of reporting requirements to adequately protect consumers and service reliability. However, SRP believes the appropriate regulatory mechanisms may depend on the structure and nature of such entities.

A19. Certificates of Convenience and Necessity. Please comment on whether competitive sellers who supply electricity to an end user must obtain a Certificate of Convenience and Necessity from the Commission (unless the seller already has an applicable Certificate). Please describe whether any conditions on the certificate would be necessary.

Traditional suppliers would provide service to customers in existing service territories under existing territorial allocation agreements, state law, regulatory

structures, tax obligations and public responsibilities. Existing territorial agreements and Commission-granted certificates of convenience and necessity would remain in effect for distribution services.

Non- traditional suppliers would be subject to the same requirements as all players in the competitive marketplace.

EXHIBIT C

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Much more discussion is required covering the implications of customer choice on electric system operations.

- A. How do we handle generators that have to operate during high load periods to maintain the valley voltage profile? Include these additional costs in the transmission or distribution charges as voltage control?
- B. Arizona utilities are already buying as much "cheap" power as can be imported over the existing transmission system. If some customers have choice, they will take these cheaper supplies away from the remaining customers. There is no more energy to buy so what is available today will be redistributed. This includes the "buy-through" provision where less expensive resources go directly to certain customers and the average cost of the remaining generation is paid for by the remaining customers.
- C. Utilities work in "megawatts and megawatthours". Customers deal in "kilowatts and kilowatthours". Bulk electric system metering is not accurate enough to convert to kw and kwh.
- D. Choice of supplier depends upon the availability of transmission. Initially there will not be any new transmission so access will have to be allocated. How will we allocate this limited transmission on an hourly basis?
- E. How do we insure that adequate resources are built, especially if the obligation to provide generating resources no longer exists? Our obligation to serve distribution is separate from the obligation to build power plants.
- F. Existing computer systems, including power system control computers, cannot handle customer choice. New systems will have to be built and since this type of thing does not exist today, we would expect a lengthy development and startup period.
- G. Solar energy, without expensive storage capability, will not be producing energy over peak hours. The electric system will require surplus generation to compensate for the lack of solar energy over peak hours.
- H. Metering is one of the major issues. Without metering changes, including remote control and reading of each meter, utilities do not know what each customer is using. There are numerous options to the metering issue and each should be carefully reviewed. Customers with new metering

capability will have options that a customer with a normal kwh meter won't have.

- I. What about automatic load shedding programs that protect the system in an emergency. Whose load will be tripped first and restored last? It may more than likely depend upon the supplier and/or the supplier's location.
- J. Utilities serve customers today on an aggregated or simultaneous basis. If customers are given choice, each customer's demand must be scheduled, by aggregation or others, on a non-simultaneous basis. The result is a much larger non-simultaneous demand for generation versus the current simultaneous demand.

More meetings or forums with utility planning and operating experts are needed to iron out technical details created by or needed for customer choice.