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EXCEPTION

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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
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WILLIAM A. MUNDELL
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Commissioner
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Commissioner

IN THE MATTER OF THE GENERIC PROCEEDINGS CONCERNING ELECTRIC RESTRUCTURING	DOCKET NO. E-00000A-02-0051
IN THE MATTER OF ARIZONA PUBLIC SERVICE COMPANY'S REQUEST FOR VARIANCE OF CERTAIN REQUIREMENTS OF A.A.C. 4-14-2-1606	DOCKET NO. E-01345A-01-0822
IN THE MATTER OF THE GENERIC PROCEEDING CONCERNING THE ARIZONA INDEPENDENT SCHEDULING ADMINISTRATOR	DOCKET NO. E-00000A-01-0630
IN THE MATTER OF THE APPLICATION OF TUCSON ELECTRIC POWER COMPANY'S APPLICATION FOR APPROVAL OF ITS STRANDED COST RECOVERY	DOCKET NO. E-01933A-98-0471
ISSUES IN THE MATTER OF TUCSON ELECTRIC POWER COMPANY'S APPLICATION FOR A VARIANCE OF CERTAIN ELECTRIC COMPETITION RULES COMPLIANCE DATES.	DOCKET NO. E-01933A-02-0069

EXCEPTIONS OF ARIZONA PUBLIC SERVICE COMPANY TO THE RECOMMENDED OPINION AND ORDER ON "TRACK A" ISSUES

Pursuant to A.A.C. R14-3-110, Arizona Public Service Company ("APS" or "Company") hereby submits its Exceptions to the Recommended Opinion and Order ("Recommended Order") filed by the Arizona Corporation Commission's

("Commission") Chief Administrative Law Judge ("ALJ") on July 23, 2002. Such Recommended Order would, if adopted, constitute a material breach of the 1999 APS Settlement Agreement ("Settlement" or "Agreement"), previously approved and joined by the Commission in Decision No. 61973 (October 6, 1999). It further compounds that error by failing to take or even propose any ameliorative action as was suggested by the Company in its April 22nd Motion and most recently in a letter to the Commission in this Docket dated July 11, 2002. Included in both these filings, and as further explained by the oral testimony of Company President, Jack E. Davis, at hearing, was a suggestion that APS acquire the Pinnacle West Energy Corporation ("PWEC") assets serving APS load ("PWEC Reliability Assets"), which in turn may require additional financing authority from the Commission.

The Recommended Order is also unreasonable and unlawful for the following additional reasons:

(1) In applying an ill-defined and one-sided "public interest" standard, the Recommended Order ignores the adverse impact of any Commission decision to delay or prevent divestiture of APS generating units to PWEC as presently authorized by Decision No. 61073 (October 6, 1999) and A.A.C. R14-2-1615 (A) ["Rule 1615(A)"].

(2) The Recommended Order improperly bases its conclusions on an unsupported finding of unmitigated market power attributable to APS and PWEC.

(3) The Recommended Order would require APS to submit a new Code of Conduct that is itself unnecessary or at the very least premature, and which might also conflict with the results of a proceeding presently before the Federal Energy Regulatory Commission ("FERC") on this same subject.

(4) The Recommended Order's transmission requirements are ambiguous and confusing, and thus will require clarification in a subsequent rulemaking or similar proceeding if they are to be implemented by APS and Tucson Electric Power Company ("TEP").

(5) The Recommended Order both misstates the "Jurisdictional Issue" related to divestiture and the Company's position thereon, as well as not fully addressing possible concerns about the jurisdictional implications (if any) of not-for-profit versus for-profit RTOs.

(6) The Recommended Order effectively or explicitly amends or rescinds prior Commission Orders without having afforded APS notice and hearing as required by A.R.S. § 40-252.

SUMMARY OF APS' POSITION

APS entered into the 1999 Settlement Agreement in good faith. It has fulfilled every promise it made in that Agreement, including giving over $600 million in rate reductions, taking a $234 million write-off, and expending many millions of dollars more to implement the Electric Competition Rules, including but not limited to preparing for the divestiture of all of its generation plants to PWEC.[1] Moreover, PWEC has invested over a billion dollars in generation needed to reliably serve APS customers. PWEC would not have made any of that investment without the Commission's promise that PWEC would receive the Company's existing generation by the end of 2002. Indeed, PWEC could not have done so because PWEC's own credit is contingent upon such divestiture by APS, and Pinnacle West Capital Corporation's ("Pinnacle West") interim or "bridge" financing of this new construction was similarly premised on divestiture. That is not to say that these new generating plants would not have been built, but instead that they would have built by APS rather than PWEC[2] and thus clearly would have come within the

[1] These other efforts include, but are not limited to, the development of new billing software and operational protocols to accommodate direct access and Commission-mandated rate unbundling, the implementation of a Commission-approved retail Code of Conduct and subsequent training thereon of over 2000 APS management and supervisory personnel, the funding and support for the Arizona Independent Scheduling Administrator and the Desert Star and WestConnect RTOs, the maintenance of then-existing low income programs, and the withdrawal with prejudice of litigation against the Commission and the corresponding write-off of the costs of such litigation.

[2] The combined effect of Rule 1615(A) and Decision No. 62416 (April 3, 2000), both of which would now be amended or stayed by the Recommended Order, prevented APS from constructing new generation in the period between April 2000 and the end of 2002, even if needed to reliably serve customers. Indeed, the implicit assumption in the Electric Competition Rules (which were silent on the issue of supply generation reliability) was that no new generation would need to be constructed or obtained by the Affected Utilities between 1999 and the end of 2002. Yet somebody had to step in, and PWEC's ability to do so in the form of the PWEC Reliability Assets was expressly premised upon the consolidation of these Assets with the Company's existing generation no later than the end of 2002. Of course, APS could have contracted for the new supplies it needed last summer, this summer, and

definition of the Company's "existing assets," as used in the Recommended Order. (Recommended Order at 32.)

To now selectively and unilaterally amend that Settlement without any mention of the need and the obligation of the Commission to address the Company's detrimental reliance on the Settlement—a reliance which now leaves both PWEC and Pinnacle West in the perilous financial situation discussed both by APS witness Jack Davis and in William Post's letter to the Commission dated July 11, 2002 ignores any balanced notion of "public interest." Indeed, it flies in the face of the Recommended Order's own admonition that the Commission should "take action in a manner that is fair to all parties" and that will "minimize the effects" of altering the Settlement. (*Id.* at 22.)

The Commission's choice is clear. It must either honor the Settlement that it approved, joined and defended against multiple appeals, or it must take steps to undo the significant harm caused by the breach of the Settlement. Simply put, APS must be permitted to acquire the PWEC Reliability Assets and provide them with long-term financing until the divestiture issue is finally and permanently resolved. This is the first and most essential step towards a compromise that will reconcile the promises made in the Settlement with the "change of circumstances" claimed in the Recommended Order.

Additionally, although less global in its implications to the Company and its affiliates, the Recommended Order makes findings of market power that are wholly unsupported by credible evidence, are unnecessary in any event, and which could be used to the detriment of the Company and its customers in future proceedings. The "market power study" the Recommended Order would require as a precondition to divestiture is so undefined as to be largely without value and is apparently pointless in any event because the "study" appears to presuppose the existence of market power even before it is

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succeeding summers, but the cost of obtaining such supplies during the volatile days of 2000-2001 would have been prohibitive. And, although West Phoenix and Redhawk would no longer be at issue, the Company and its customers would have been saddled with a 10-20 year contract at far higher costs.

conducted. The Recommended Order also proposes imposition of a new Code of Conduct before it is clear that such a document is actually necessary. This is especially true given similar proceedings pending before FERC and the real potential that PWEC would no longer be in the position of being a significant seller of power to APS, should APS acquire the PWEC assets presently serving APS or under construction for that purpose. The Recommended Order further requires APS and TEP to "develop a plan" and to "file [a] reliability must-run study" (*id.* at 32), while not clearly articulating what the "plan" is supposed to address and under what circumstances the "study" is to be required. Finally, the Recommended Order misses the point on the second "jurisdictional issue" that the Company believes was raised during the hearing and partially misstates the Company's position on both such issues in any event.

INTRODUCTION

On page 1, the Recommended Order begins its discussion by noting the Company's filing of a request for variance in October of 2001. It is as if that filing was somehow the cause of or even substantially related to the expansive re-examination of the Settlement and the Electric Competition Rules called for in Track A of the instant generic proceeding. It was not. Back in October of 2001, APS asked for one variance to one provision of many of the Electric Competition Rules. APS did so for one singular purpose—to request approval of a proposed purchase power agreement ("Proposed PPA") between itself and Pinnacle West Capital Marketing & Trading ("PWM&T") because APS believed and continues to believe that such an agreement was in the best interests of its Standard Offer customers. APS did not volunteer to surrender any right explicitly granted by the Settlement independent of the Electric Competition Rules, such as the clear and unconditional right of APS to divest its generation to PWEC, nor did it ask to be

relieved of any obligation explicitly imposed by the Settlement independent of the Electric Competition Rules, such as the obligation to grant five annual rate decreases.

The Company's variance request, despite its merits, effectively died on April 25, 2002. It was killed without allowing so much as a single witness to testify in its defense. It is disingenuous to suggest, as does the Recommended Order at page 24, that the Company somehow brought about its own dilemma or that there is some legal equivalence between the Company's request for a variance to a Rule only incorporated by reference into the Settlement (and which Rule the Settlement by its own terms specifically permitted the Commission to vary or amend) and the Commission's action to unilaterally violate rights expressly granted to the Company in the Settlement—rights that exist independent of Rule 1615(A) or any of the Commission's Electric Competition Rules.

Rather than try to blame the Company for the Recommended Order's desire to unilaterally abrogate one part of a comprehensive agreement, the Recommended Order's (and the Commission's) focus should now more properly be on the question of where we go from here. On July 11, 2002, the Company explained an earlier suggestion of April 22nd that, although not fully compensating APS for the breach of the Settlement Agreement, would in essence stop any further immediate harm to the Company and its affiliates and clear the way for future discussions on how to "unscramble the egg." In its Exceptions, the Company will try to build on this theme of reconciliation in addition to providing the more conventional critique of the Recommended Order.

EXCEPTION NO. 1 – DIVISION OF GENERATING ASSETS SERVING APS OR THE "BIFURCATION ISSUE"

It was uncontested at the hearing that APS has incurred millions of dollars in preparing for the transfer of its generation assets by December 31, 2002 as authorized by the APS Settlement and as required by Rule 1615(A). Likewise unchallenged was the fact that APS' affiliates will face increased financing costs and perhaps the inability to either

obtain or maintain an investment-grade debt rating so long as the generation assets devoted to serving APS are split into two entities. The Recommended Order misstates the point that APS was making it its Post-Hearing Brief. (*See* Recommended Order at 12, fn. 6.) APS was in fact "required" to form PWEC in order to construct needed generation capacity for APS customers. In other words, the regime that the Commission imposed through the Competition Rules did not itself address reliability and did not permit APS to perform this reliability function itself. In fact, the passage from Decision No. 61973 referenced in the Recommended Order was included in the context of justifying why APS was permitted to recover only two-thirds of the costs to transfer generation to the affiliate, not to suggest that APS had any alternative to the creation of PWEC. Thus, the apparent suggestion in the Recommended Order's footnote that it somehow would have been better had APS and its affiliates simply ignored the reliability requirements of APS customers or divested APS generation to a wholly-unaffiliated third party in contradiction to the Settlement or that the current situation of "bifurcation" was somehow the Company's own choice is perplexing to say the least, and wholly irrelevant to the Company's claims of detrimental reliance on such Settlement.

And unlike the wholly unsubstantiated claims of the merchant generator intervenors, the Company's detrimental reliance on the Settlement and Rule 1615(A) was both established by record evidence and uncontroverted by any witness. APS' and its affiliates' actions spared its customers from the turmoil and rate shock experienced throughout other parts of the Western United States and has ensured that there is sufficient capacity available to meet APS' reliability requirements last summer, this summer and into the future. Staff witnesses agreed that such increased costs were legitimate claims by APS should Staff's recommended delay, let alone an outright denial of divestiture, eventuate as a result of the Commission's Track A decision. (*See* Tr. vol. VI at 1347-49; Tr. vol. VII at 1606.) And, as noted above, the Recommended Order itself even posits a

desire that the Commission "take action in a manner that is fair to all parties . . ." (Recommended Order at 22.)

Despite all of this, the Recommended Order is entirely deficient on how its provisions are or can be "fair" to APS—which has complied with every obligation that it agreed to in the Settlement and commissioned construction of the PWEC Reliability Assets in reliance on the Commission-approved divestiture of APS generation to PWEC. Instead, the Recommended Order proposes simply to change those material provisions of the Settlement that the Recommended Order now finds troublesome. The Recommended Order then glosses over the resulting "bifurcation" issue under the throwaway category of "Miscellaneous Issues." Although the Recommended Order does suggest that the Company could make "appropriate application(s)" for acquiring the PWEC Reliability Assets (Recommended Order at 25), it makes no specific effort to address or recognize in this proceeding the costs that APS and its affiliates have incurred in detrimental reliance on the Settlement—and certainly evidences no tangible support for actually implementing a solution that is "fair to all parties."

In contrast, APS has suggested, first in its April 22nd Motion and later in its testimony and in the July 11th letter to the Commission in this Docket, one possible and readily-achievable method of resolving the "bifurcation" issue in a manner consistent with the Recommended Order's expressed desire to be "fair" to the parties—allowing APS to acquire and permanently finance those PWEC assets that were built for APS customers and which would have been built by APS were it not for the divestiture provisions of the Electric Competition Rules (and the associated Commission-mandated Code of Conduct) and the Settlement. Such action would not tie the Commission's hands as to the future determination of the prudence or "used and useful" inclusion of these assets in the Company's retail rate base and would at least mitigate the impact of the Recommended Order on APS and its affiliates. As such, "bifurcation," or more to the point, "re-

unification," is most certainly a Track A issue that should be addressed as part of any order in this proceeding.

Accordingly, to achieve the stated objective of being "fair to all parties," the Recommended Order must be modified to specifically address the "bifurcation" issue. The evidence presented in this proceeding, when properly viewed, supports permitting the divestiture that the Commission has already approved. At a minimum, however, the Commission's final order on Track A issues should expressly authorize APS to acquire and obtain financing for the generation assets that were built by PWEC for APS' customers without pre-judging any of the factors affecting the eventual rate-making treatment thereof.[3] APS has attached a proposed amendment to the Recommended Order in Appendix A to its Exceptions.

EXCEPTION NO. 2 – DIVESTITURE/BREACH OF THE SETTLEMENT

A. The Recommended Order, if adopted, would constitute a material breach of the Settlement.

In Decision No. 61973, the Commission entered into a binding agreement with the Company to permit divestiture without further conditions. The Settlement entered into by the Commission specifically granted:

> all requisite Commission approvals for . . . the creation by APS or its parent of new corporate affiliates . . . and the transfer thereto of APS' generation assets ...
>
> . . .
>
> The Commission has determined that allowing the [APS] Generating Assets to become . . . owned by an APS EWG affiliate will benefit consumers, (2) is in the public interest, and (3) does not violate Arizona law.

See 1999 APS Settlement Agreement at §§ 4.2 and 4.4 (emphasis supplied).

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[3] APS is aware that it may have to submit a financing application to the Commission if it otherwise lacks sufficient debt authorization under Decision No. 55017 (May 6, 1986) and its predecessor decisions to accomplish the above acquisition. The financing "approval" referenced above would be only an approval "in principle" pending such a formal application as is required under A.R.S. § 40-301, *et seq.*

In the decision approving the Settlement, the Commission also stated unequivocally that it:

> supports and authorizes the transfer by APS to an affiliate or affiliates of all its generation and [other] competitive electric service assets as set forth in the Agreement no later than December 31, 2002. [Decision No. 61973 at 10 (emphasis supplied).]
>
> . . .
>
> The terms and conditions of the Settlement Agreement as modified herein are just and reasonable and in the public interest. [*Id.* at 17, Finding of Fact No. 33 and Conclusion of Law No. 17 (emphasis supplied).]

The Arizona Court of Appeals in *Arizona Consumers Council v. Arizona Corporation Commission*, 1 CA-CC 99-0006 (Ariz. Ct. App., April 5, 2001) has already conclusively construed the legal meaning of the relevant provisions of the Settlement. In upholding the Settlement, the Arizona Court of Appeals held:

> The agreement requires APS to divest its generation assets by December 31, 2002, and requires the Commission approve the formation of an APS affiliate to acquire those assets at book value. [Opinion at ¶ 8.]
>
> ...
>
> Section 6.1 [of the Settlement] makes the Commission a party to the agreement, and section 6.2 precludes the Commission from taking or proposing any action inconsistent with the agreement and requires the Commission to actively defend it. [Opinion at ¶ 33.]
>
> ...
>
> The general rule, however, is that a contract that extends beyond the terms of the members of a public board is valid if made in good faith and if its does not involve the performance of personal or professional services for the board. [Citation omitted.] The [Arizona Consumers] Council has not alleged that the [settlement] contract was not entered into in good faith, and the contract does not involve personal services for Commission members. The [settlement] contract can therefore bind future commissions. [Citation omitted.] [Emphasis supplied.] [Opinion at ¶ 38.]

The Recommended Order proposes precisely the action that the Court of Appeals has already held the Commission cannot take without breaching the Settlement.[4] As discussed below, that issue has been decided as between APS and the Commission. The discussion in the Recommended Order that suggests that "if granting a variance from Rule 1606(B) would not violate the Settlement Agreement, then granting a stay or variance of [Rule 1615(A)] would similarly not violate the Settlement Agreement" (Recommended Order at 24) is simply incorrect. It ignores the fundamental distinction between those provisions of the Settlement that merely incorporate by reference whatever right or obligation as is imposed by the Electric Competition Rules (e.g., Section 4.1.3's language on competitive procurement post-divestiture), which Rules the Commission expressly reserved the right to modify (Section 7.1), from those Sections of the Agreement (Sections 2.2, 4.2, etc.) that are independent of the Electric Competition Rules, and which therefore cannot be modified unilaterally without breach of the entire Agreement. If the Commission in a final decision had determined that APS' Request for a Partial Variance constituted a breach of the Settlement, APS would have complied with the Settlement, as thus interpreted, irrespective of Rule 1606(B). The Commission should do no less.

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[4] The Court of Appeals' holdings regarding the meaning and impact of the Settlement is binding as a matter of law between the APS and the Commission. *See, e.g., Elec. Dist. No. 2 v. Arizona Corp. Comm'n*, 155 Ariz. 252, 259 & n.2, 745 P.2d 1383 (1987) (Arizona Supreme Court holding that the Commission is bound by a final Court of Appeals decision and noting that an unpublished memorandum decision is "just as binding on the parties as a published opinion"). In the litigated appeals to Decision No. 61973, the Commission had the opportunity to argue, and in fact argued, its position that the Settlement was not really a contract and did not really bind the Commission. As the quotations from the Court of Appeals' decision above note, those arguments were expressly rejected. As such, the matter is *res judicata* and the Commission is bound by the Court's interpretation. This result—that the Commission is bound to a settlement agreement that it enters into like any other party—is by no means a novel position in Arizona. *See U S West Comm. v. Arizona Corp. Comm'n*, 185 Ariz. 277, 280-82, 915 P.2d 1232 (Ct. App. 1996) (rejecting attempt by Commission to change settlement agreement that affected rate treatment of U S West). The Recommended Order fails to consider this legal issue or articulate a lawful reason as to why the Commission is not bound as the Court of Appeals has found.

The Commission should honor the Settlement, just as APS has honored its commitment to take a $234 million write-off of otherwise recoverable costs, to voluntarily reduce rates by some $600 million (to date), to dismiss with prejudice its pending litigation against the Commission, and to make the other concessions implicit and explicit in the APS Settlement. No legitimate legal or policy reason to the contrary has been presented in this proceeding or even discussed in the Recommended Order.

The Recommended Order also does not discuss less onerous alternatives to breaching the Settlement, such as consideration of the Proposed PPA that APS offered or a similar cost-based agreement covering the APS and PWEC assets. The Proposed PPA would permit the divestiture while both addressing the reliability issue by incorporating the PWEC Reliability Assets and protecting APS customers from the very market risk decried by the Recommended Order (Recommended Order at 22 and Finding of Fact Nos. 29 and 35) but to which customers would (ironically) be exposed by the very same Recommended Order. (*Id.* at 23 and Finding of Fact No. 36.) Neither does the Recommended Order address the damage occasioned by its breach as repeatedly urged by the Company as far back as its April 22, 2002 Motion for Determination of Threshold Issue and as recently as the letter from Mr. Post in this Docket of July 11th. The Company has suggested changes to the Recommended Order addressing the latter of these two options (acquisition by APS of the PWEC Reliability Assets) as APS Proposed Amendment No. 1 under Exception No. 1 in Appendix A.

B. There have been no changes in circumstances justifying a breach of the 1999 APS Settlement.

The Recommended Order lists several issues, such as the amount of retail competition active in the state, alleged incumbent market power, and the GAO Report on FERC oversight on competitive markets. It concludes that these issues are changes and "circumstances outside [the Commission's] control or the control of any party" that

warrant the Commission abrogating the Settlement. (Recommended Order at p. 22.) However, none of the issues actually represent a "change" of circumstances since 1999 or are changes irrelevant to the issue of divestiture.

Specifically, the lack of active retail competition today is no basis to breach the Settlement because the potential for an Electric Service Provider to offer service should APS Standard Offer service become unattractive itself protects consumers. If the Settlement remains intact, APS customers are protected through June 2004 from wholesale rate impacts, something that makes the GAO Report less significant particularly when coupled with the current effort at FERC to improve its oversight of the wholesale market or when mitigated through the cost-based Proposed PPA. Indeed, FERC's Standard Market Design Notice of Proposed Rulemaking ("SMD NOPR") is intended to address precisely those deficiencies cited in the GAO Report. Also, any alleged "market power" held by incumbent utilities is unquestionably less than in 1999 when the Commission approved divestiture without further conditions, so it cannot constitute changed circumstances. Similarly, transmission constraints were present in 1999 and will be present in the future regardless of divestiture. Regardless, the AISA has protocols to address related issues such as must-run generation even in the absence of an RTO. There has been no change in FERC's regulatory jurisdiction over wholesale power transactions since 1999. Staff has proposed no changes to APS' existing Code of Conduct or Policies and Procedures since its approval by the Commission in the spring of 2000, nor has APS ever been accused of breaching that Code of Conduct. In any event, given the rate protections afforded to APS customers under the Settlement, there is certainly time to address any Code of Conduct concerns the Commission may have before there would be any impact on APS customers and regardless of whether divestiture takes place as approved in the Settlement.

As APS noted in its Post-Hearing Brief and in Mr. Davis' testimony, the most significant change in circumstances was the formation of a new and separate generation affiliate as required by the Settlement to accommodate the divestiture. That "change", however, further supports compliance with the Settlement, rather than its abrogation by the Commission. But, even if all of the issues identified in the Recommended Order were accepted as "changes" and had evidentiary support as such, this would at best argue for rescinding or reforming the entire Settlement Agreement rather than selectively breaching the Settlement as proposed in the Recommended Order. The latter approach effectively allocates all of the risk of such "changes" to APS and to no other party. Such a result is inconsistent with the Recommended Order's own conclusion that APS was not at fault for the alleged "changes, and it is neither fair nor lawful.

C. The "public interest" justification given by the Recommended Order for abrogating a single portion of the Settlement is unsupported by any Arizona regulatory or judicial precedent and is, in any event, impermissibly vague and has been improperly and unfairly applied against just one party to the Agreement.

The Recommended Order concludes, without specifically articulating the applicable legal standard, that the "public interest" requires that the Commission breach the Settlement. (Recommended Order at 23.) APS would note at the outset that there is no legal authority in Arizona for the unilateral breach by the Commission of a prior settlement agreement. Even in the *U S West* decision cited above, the Commission attempted to argue that its actions did not constitute a violation of its agreement with the utility rather than claiming some manifest authority to simply disregard its previous promises.

The very lack of such precedent speaks volumes about what is, in fact, "in the public interest" under the present circumstances. As discussed throughout the United States Supreme Court's opinion in *United States v. Winstar Corp.,* 518 U.S. 839 (1996), the "public interest" is most directly served by the government keeping its regulatory

promises or "making good" to those adversely affected when it cannot. The Recommended Order thus fails the most compelling and authoritative definition of what is "in the public interest." Indeed, at no point does the Recommended Order explain how any definition of the "public interest" demands that:

- the breaching party be allowed to keep all the benefits of the very Agreement it has determined to breach
- the non-breaching party be forced to absorb without compensation all the damages occasioned by the breach
- the issue of detrimental reliance on the Settlement be entirely unaddressed.

Even when the contract at issue is only between private parties and does not implicate the "full faith and credit" of government, it is well recognized that the level of scrutiny and analysis given to a "public interest" justification is significantly more stringent when the abrogation of a contract is at issue, than if parties' reliance on the more general policy determinations of a regulatory agency, such as rulemakings, are the focus. *See, e.g., Texaco v. FERC*, 148 F.3d 1091, 1096-97 (D.C. Cir. 1998) (discussing the standard necessary to reform contracts under the public interest standard in *Mobile-Sierra* cases); *Atlantic City Elec. Co. v. FERC*, No. 97-1097, (D.C. Cir., July 12, 2002), at 20-21 (holding that generic findings of public interest were not sufficiently particularized to justify reforming a contract). Specifically, the appropriate standard to evaluate whether the "public interest" requires reformation of a contract should analyze and explain in detail both the manner in which the contract harms the public interest and the extent to which abrogation of the contract is required to mitigate the enumerated harms to that public interest. *See id.*

The Recommended Order does not undertake such a legal or factual analysis. Rather it simply posits "public interest" as an undefined standard against which the Settlement is to be measured. It next proffers a series of issues or concerns which, as discussed above, were either well known at the time the Commission approved the

Settlement, are already mitigated by the Settlement, can be mitigated with less onerous means, or are unrelated to divestiture. Accordingly, the "public interest" justification of the proposals in the Recommended Order is neither lawful nor supported by the evidence of record.

D. If divestiture is stayed, APS will not be a Utility Distribution Company and would not be subject to any mandatory competitive bidding requirement under Rule 1606(B).

In another inequitable and asymmetrical analysis, the Recommended Order discusses at length how Rule 1615(A) regarding divestiture is linked with Rule 1606(B)'s requirement for competitive bidding. Despite recognizing such linkage, the Recommended Order proposes staying all of the divestiture requirements in Rule 1615(A) and in the Commission-approved Settlement, but only some of the competitive bidding requirements in Rule 1606(B). If APS is prohibited from divesting its generation, it will not be a Utility Distribution Company and therefore will not be subject to Rule 1606(B). In such a case, APS should be permitted to acquire generation from whatever means is prudent and appropriate, with mandatory competitive bidding to be phased-in only as divestiture is phased-in. Thus, if Rule 1615(A) is stayed in its entirety until at least July 1, 2004, the Recommended Order also should stay Rule 1606(B) in its entirety for an equal period of time. Moreover, at a minimum, the rulemaking docket proposed at page 26 of the Recommended Order should be completed before any final decision is made in Track B, and the appropriate revisions needed to Rule 1606(B) should be addressed in that proceeding. This would maintain the linkage between the two provisions [Rule 1615 (A) and Rule 1606 (B)] that has historically existed.

APS has proposed amendatory language in Appendix A to address this last point. If the Commission agrees with the Company's more fundamental Exception concerning the sanctity of the 1999 APS Settlement, this would essentially require a complete

rewriting the Recommended Order. In such an eventuality, APS would suggest that the ALJ be so instructed by the Commission.

EXCEPTION NO. 3 – MARKET POWER

A. The evidence presented during the Track A hearing demonstrates that APS does not have wholesale market power and that PWEC will not have unmitigated wholesale market power post-divestiture.

APS witness Dr. William Hieronymus is probably the foremost authority on market power analyses in the United States—not just as it relates to traditional utilities such as APS, but regarding many of the merchant power entities as well. His analyses of market power have been routinely accepted by both FERC and the United States Department of Justice ("DOJ"). The market power analysis that he presented in this proceeding conformed to accepted and clearly-articulated FERC and DOJ standards for such analyses. Indeed, all the witnesses that even attempted to conduct a Supply Margin Assessment ("SMA") came to the conclusion that APS passes this most recent and stringent market power test proposed by FERC in determining whether or not a wholesale electric market is functionally competitive. (*See* Tr. vol. IV at 909-11; *see also* Rebuttal Testimony of William H. Hieronymus at 1 and 5.) FERC itself has so found as to both APS and its two major energy affiliates on several occasions. *See Re Arizona Public Service Company*, 79 FERC ¶ 61,022 (1997)[5]; *Re Pinnacle West Energy Corporation*, 92 FERC ¶ 61,248l (2000); and *Re Pinnacle West Capital Corporation*, 91 FERC ¶ 61,290 (2000). It was only when these other witnesses altered the fundamental assumptions of their study in order to obtain a pre-ordained result, or changed the scope of their analysis to study something not at issue (such as the existence of ephemeral market power in transmission constrained areas of the APS service territory) that their results differed in any material way from those of Dr. Hieronymus.

[5] The Commission was a participant in this proceeding and specifically did not contest the FERC finding that APS lacked significant market power.

But without meaningful explanation, the Recommended Order concludes that Dr. Roach's non-standard and fundamentally illogical SMA analysis should be adopted over any of the accepted FERC and DOJ market power tests, all of which APS passes. Dr. Roach himself did not even care if his study accurately measured wholesale market power, only that the Commission find the Proposed PPA to be a bad deal for consumers. (Tr. vol. III at 755.) Yet the only criticisms mentioned in the Recommended Order concerning the Company's SMA analysis are those of Panda witness Roach. (Recommended Order at 8.) These include (1) the inclusion in the SMA analysis of non-APS transmission in determining transmission import capability; and (2) the inclusion in the SMA analysis of generation not presently serving APS load. Aside from the fact that both Dr. Roach and Dr. Hieronymus used the same transmission import capability, which is how FERC requires the SMA test to be conducted, Staff witness Jerry Smith's own recent comments at the Track B Workshop held on July 24-25 validated the use of non-APS transmission resources in determining transmission import restrictions. The second "criticism" is no more than a meaningless tautology. If you exclude *a priori* all the possible competitors from a market power analysis, even the tiniest of suppliers will have, by definition, "market power," an obviously erroneous conclusion. (*See* Rebuttal Testimony of William H. Hieronymus at 5.)

The Recommended Order further states its disagreement that "must-run" protocols adequately mitigate market power within certain load pockets without providing any criticism of such protocols, which were developed through a stakeholder process, or explaining why they are not or will not be effective. Similarly, there is no explanation why prohibiting divestiture will ameliorate wholesale market power in constrained areas with must-run generation when no witness at hearing suggested that non-divestiture would (standing alone) provide any such amelioration. The Recommended Order further ignores the mitigation afforded by must-run contracts that will be required prior to divestiture

under A.A.C. R14-2-1609 (I)—mitigation that was intended to address precisely this type of "market power" issue identified with respect to load pockets. Thus, the market power conclusions in the Recommended Order, both in general and specifically as to load pocket areas, are not supported on sound public policy grounds or by the evidence of record in this proceeding. The Commission should vacate such findings or, in the alternative, adopt a more neutral position, as is set forth below.

B. At worst, the market power evidence in this proceeding is contradictory and the Commission should make no findings that APS has or does not have market power.

As discussed above APS believes that the evidence in this proceeding and the application of accepted tests warrants a finding of no market power, rather than the finding proposed in the Recommended Order. However, if the Commission does not agree, it should simply decline to rule on this issue now and allow for the future development of the more detailed market power studies suggested by Staff and included in the Recommended Order (as a pre-condition to divestiture) to finally resolve this question if and when such resolution becomes necessary. This would also allow time for the various reforms suggested in the SMD NOPR to become effective and in any event is more appropriate than adopting an unprecedented and unsanctioned market power test without providing a complete explanation of why such test was adopted and why it is more appropriate under the circumstances presented in this proceeding than any of the accepted FERC or DOJ methods. After all, these latter agencies are, at the very least, the bodies with the primary legal responsibility to identify, supervise and mitigate <u>wholesale</u> electric market power. The Commission should be extremely hesitant to second guess their findings based on, at best, conflicting evidence.

This is not just some abstract academic debate over whose witness was right and whose was wrong. A general and affirmative Commission finding that APS <u>does</u> have wholesale market power is a serious thing. It may produce unintended consequences and

have unpredictable ramifications in future FERC proceedings as well as in other contexts. For example, to the extent APS continues to own generation as contemplated by the Recommended Order, it is in the interest of APS retail customers that APS be able to make off-system sales on as favorable of terms as possible. A Commission finding of wholesale market power might be used by certain parties at FERC in an attempt to reduce competition in the Arizona wholesale market by limiting the Company's pricing flexibility for such off-system sales. APS has included a suggested amendment to the Recommended Order in Appendix A.

C. The market power study required by the Proposed Order as a precondition to divestiture after July 1, 2004 is unnecessary, ambiguous, and appears to prejudge the results of such study.

Staff witness Rowell proposes a mega-market power study encompassing unspecified features of the Herfindahl-Hirschman Index ("HHI"), the "Hub and Spoke" method, and the SMA market power analyses, all of which APS has already passed. Staff also recommends some manner of completely undefined "strategic behavior" analysis, which, as APS noted at the hearing, assumes illegal collusive behavior on the part of market participants. Thus, this type of strategic behavior analysis will always conclude that effective competition is impossible. This is all the more significant since market power arising from assumed illegal collusion can likely never be mitigated in any conventional meaning of that term, only deterred through vigorous enforcement of existing antitrust laws. Because APS has passed and passes the applicable FERC and DOJ market power tests, the additional market power analyses required by the Recommended Order are as unnecessary as they appeared biased in favor of a predetermined outcome. By purporting to adopt Staff's recommendation, the Recommended Order is also impermissibly ambiguous and, because Staff advocates a strategic behavior analysis that is likely impossible to overcome, appears to prejudge the outcome. At a minimum, the Recommended Order should be amended to not expressly "adopt" Staff's

recommendations but to simply order APS and TEP to work with Staff to develop a common approach to market power testing, monitoring, and mitigation. A suggested amendment to the Recommended Order is included in Appendix A.

EXCEPTION NO. 4 – CODE OF CONDUCT/AFFILIATE TRANSACTIONS

A. APS already has both a Commission-approved Code of Conduct and FERC Standards of Conduct, in addition to this state's comprehensive set of affiliate regulations, none of which are "broken" and in need of "fixing" by the Recommended Order.

APS presently has a Code of Conduct approved by the Commission in Decision No. 62416 (April 3, 2000), as well as Policies & Procedures ("P&P") to effectuate that Code. The latter were submitted and approved on June 2, 2000. The Commission has also had general rules and regulations concerning affiliate transactions since the early 1990s. And there have been individual Commission orders specific to APS and its affiliates. The Recommended Order does not explain how or why these existing protections are inadequate. Moreover, the evidence at the hearing shows that there is nothing improper regarding APS' relationship with either PWM&T or PWEC that warrants additional Commission action at the present time.

APS is also subject to FERC-imposed Standards of Conduct that prevent the subsidization of generation by transmission and prevent APS from granting preferential access to either its physical transmission system or to information concerning such system. At present, FERC is considering significant changes to its Standards of Conduct in FERC Docket No. RM01-10-000. A final order in that Docket is expected in the fourth quarter of 2002. These changes may serve to moot some Code of Conduct issues raised by Staff regarding the relationship of PWM&T, APS and PWEC. More significantly, however, any state-mandated Code of Conduct involving wholesale affiliates must be considered in the context of FERC's Standards of Conduct as they are most certainly to be revised. Finally, if APS acquires the PWEC assets constructed or under construction to

serve APS load, PWEC will no longer have the ability to make significant sales of power to APS.

Thus, if the Commission believes that a new Code of Conduct is required to address the generic issues identified by Staff, it should be prepared and submitted within 60 days of the final decision in the FERC docket listed above to avoid unnecessary conflict with FERC's final resolution on wholesale Standards of Conduct. It should also take into consideration the then-existing status of PWEC as a potential seller in the Arizona wholesale market. As APS has previously noted, the rate protections in the Settlement provide ample time to accommodate this request without jeopardizing consumer protection. Suggested language in provided in Appendix A.

EXCEPTION NO. 5 – THE RECOMMENDED ORDER'S TREATMENT OF TRANSMISSION CONSTRAINTS IS CONFUSING AND PREMATURE

The Recommended Order indicates that it is in general agreement with Staff's recommendations on transmission issues. It further directs APS and TEP to develop a plan regarding RMR generation concerns in the next Biennial Transmission Assessment. While the Track A hearings indicated more agreement between Staff and APS than might have been apparently from simply reading pre-filed testimony, the Recommended Order does not appropriately address transmission issues, does not consider or articulate the evidence regarding transmission issues, and, like other portions of the Recommended Order, asymmetrically imposes unreasonably vague obligations on APS and TEP, but not on other parties.

Specifically, the significance of Recommended Order's acknowledgement that it is in "general" agreement with Staff's recommendations is unclear, particularly given that much of Staff's recommendations depend on additional study work and the completion of the next Biennial Transmission Assessment. Thus, the Recommended Order should be clear that it does not in itself adopt any particular recommendations of Staff apart from

those specifically identified in the ordering paragraphs. For example, if Staff wishes to impose its non-industry standard reliability requirements on jurisdictional parties, the appropriate place and method is in the further rulemaking proceedings contemplated in the Recommended Order or a rulemaking proceeding following the Biennial Transmission Assessment. Either forum should explicitly consider the sort of cost/benefit analysis discussed by both Staff witness Smith and Company witness Deise in addition to the potentially significant impact on native load customers of jurisdictional transmission-owning utilities such as APS and TEP.

None of the RMR and transmission issues discussed in the Track A hearing were noticed as Track A issues in the Commission's Procedural Order of May 2, 2002, and all are ultimately unrelated to Track A or are otherwise addressed in different sections of the Recommended Order (i.e., localized market power). Because the Commission's Biennial Transmission Assessment is underway, the most appropriate way of addressing transmission issues is simply to defer to such Assessment or to the follow-on rulemakings contemplated in the Recommended Order. Including vague and unspecified findings and discussion on transmission issues in the Track A order risks confusing the issues and interfering with other pending or contemplated Commission proceedings. Specific amendatory language is provided in Appendix A.

EXCEPTION NO. 6 – THE RECOMMENDED ORDER'S DISCUSSSION OF CERTAIN "JURISDICTIONAL ISSUES" IS INCOMPLETE

The Recommended Order concludes at page 25—with no discussion or legal analysis—that "[All] [t]he parties are in agreement that once as asset transfer occurs, APS' acquisition of power would be wholesale transactions under the jurisdiction of FERC and that FERC has jurisdiction over both profit and not-for-profit RTOs." First, APS does not agree that this is a jurisdictional issue created solely by divestiture. FERC has had and will continue to have jurisdiction over most wholesale sales to APS and TEP

irrespective of any divestiture. Other wholesale transactions, such as the SRP sale to APS, are not regulated by either FERC or the Commission—a circumstance also unrelated to divestiture. Second, this conclusion accurately states the "form" but ignores the more important "substance" on the jurisdictional issue that was discussed in APS' Brief. Most of the Commission's historical oversight of the state-regulated operations of APS, including the determination of the prudence of resource acquisition, the deployment and use of resources, and when resources are "used and useful" will remain unaffected by divestiture. The Proposed PPA, because it involved an affiliate of APS, would have further preserved and complemented the historical oversight jurisdiction of the Commission as to APS. Thus, the Commission's "loss" of jurisdiction is more apparent than real, a fact which should be acknowledged in the Recommended Order.

On the RTO issue, the Recommended Order is certainly correct in so far as it goes. But APS believes that the jurisdictional issue posed by Chairman Mundell during the course of the Track A hearing had somewhat less to do with FERC's jurisdiction than the Commission's. Thus, the Recommended Order should also find that the Commission's own jurisdiction is unaffected by whether an RTO is for-profit or not-for-profit. The Company has provided amendatory language for this section of the Recommended Order in Appendix A.

EXCEPTION NO. 7 – A.R.S. § 40-252 REQUIRES SPECIFIC NOTICE TO APS AND HEARING "AS UPON COMPLAINT"

These proceedings do not and have not complied with the procedural requirements of A.R.S. § 40-252. Such a proceeding requires that the Commission give affected parties specific notice of both the Commission orders or portions of orders that are being considered for amendment or rescission and, in the case of the former, the specific amendments that are to be considered in such proceeding. The very fact that the parties were requested to identify in their post-hearing briefs the orders that will have to be

rescinded or amended is conclusive proof that the initial notice to the Company in this generic proceeding was legally inadequate to comply with A.R.S. § 40-252.

Also, the evidentiary hearing required under A.R.S. § 40-252 must be "as upon complaint." Although the literal requirements for a "complaint" are generally discussed in A.R.S. § 40-246, more fundamentally, a complaint is an adversarial process requiring that the accusing party, in this case the Commission (through Staff) first present its evidence before requiring the defending party, in this case APS, to respond. It is a process that is inherently inconsistent with an investigative "generic proceeding," where the focus is on general policies rather than the specific adjudicative facts, if any, warranting a change to or rescission of a prior Commission decision.

If the Commission will also recall, at the Special Open Meeting of July 12, 2002 held to consider TEP's own requested variance, several non-APS parties spoke. At least two indicated that they believed a further and separate evidentiary hearing would be required prior to any amendment of the Commission decisions approving the TEP and APS Settlements. The failure by the Commission to afford a party procedural rights provided by statute is per se reversible error. *Southern Pacific Co. v. Corporation Commission*, 83 Ariz. 333 (1958). Thus, the Commission should accept the Company's arguments on this important point of law and procedure.

CONCLUSION

The Settlement has been a good deal for APS customers and for Arizona. It has saved consumers hundreds of millions of dollars, insulated them from some of the most turbulent energy markets ever experienced, promoted regional transmission planning, and provided the promise of retail competition—a promise no less valuable simply because it has yet to be realized. The Recommended Order acknowledges as much by the fact that it has suggested changes to only one part of that Settlement. But such selective and one-

sided contract "reformation" is neither lawful nor, in the words of the Recommended Order, "fair." It leaves the PWEC Reliability Assets bifurcated from the balance of the Company's generation, something never contemplated by the Electric Competition Rules or the Settlement. It effectively punishes the Company for its successful efforts to meet the fast-growing needs of its customers during the period after the Settlement but before the divestiture and competitive procurement envisioned by those same Rules were implemented. It is also unnecessary given the Company's willingness to devote all of its generating assets, as well as the PWEC Reliability Assets constructed in its behalf, to APS customers at essentially cost-of-service, i.e., regulated prices, either through the Proposed PPA or the alternative of allowing APS acquisition of those same PWEC Reliability Assets.

As noted above, and in addition to the Proposed PPA, the Company has provided a viable and practical alternative short of divestiture by year-end 2002—one that both addresses the "bifurcation issue" (and the critical financial dilemma that continued "bifurcation" presents) and preserves the Commission's flexibility to reconsider both divestiture and increased reliance on the competitive wholesale market after July 1, 2004. As set forth most recently in the Company's July 11th letter, this requires the acquisition by APS of the PWEC Dedicated Assets subject to whatever additional formal financing approvals are required. The Commission's determination of all rate-making issues such as prudence and "used and useful" would be deferred for a later and more appropriate forum.

The inclusion by the Commission in any final order on Track A of specific language endorsing this compromise solution would constitute a critical first step to a "fair" and balanced reformation of the original Settlement in a manner the Company could affirmatively embrace rather than be forced to litigate. Moreover, other provisions of the APS Settlement that are thus affected by the Commission's determination herein should be subject to further reconsideration by the Commission during the Company's next rate

proceeding or, at the discretion of the Commission, in a separate proceeding held prior to the next rate case.

RESPECTFULLY SUBMITTED this 1st day of August 2002.

SNELL & WILMER L.L.P.

Jeffrey B. Guldner, Esq.
Faraz Sanei, Esq.

and

PINNACLE WEST CAPITAL CORP.
Law Department

Thomas L. Mumaw, Esq.

Attorneys for Arizona Public Service Company

Original and 18 copies of the foregoing filed this 1st day of August 2002, with:

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

Copies of the foregoing mailed, faxed or transmitted electronically this 1st day of August 2002, to:

All parties of record

Sharon Madden

1218369.1

APPENDIX A

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #1
(Exception No. 1)

Page 24, line 4

INSERT - "While we conclude that the public interest requires us to stay the divestiture requirement found in R14-2-1615(A) and approved as to APS in Decision No. 61973, we believe that our decision must be fair to all parties, including APS and its affiliates who have performed their obligations under the settlement agreement approved in Decision No. 61973. Accordingly, we support APS in acquiring and obtain financing for Redhawk Units 1 and 2, West Phoenix Units 4 and 5, and Saguaro Unit 3, which were or are being constructed by APS' affiliate, Pinnacle West Energy Corporation. We do so without prejudice to our traditional rate-making determinations in a future proceeding of whether such acquisition was prudent on the part of APS or whether the capacity and energy so obtained was "used and useful" in the provision of electric service by APS to its retail customers—issues common to all APS-owned assets.

DELETE paragraph starting at line 4 to line 12.

DELETE paragraph starting at line 13 to line 18.

Page 25, line 23

DELETE paragraph starting on line 23 to line 26 ½.

Page 30, line 12

DELETE Finding of Fact No. 43.

INSERT new Finding of Fact No. 43 - "APS may acquire Redhawk Units 1 and 2, West Phoenix CC Units 4 and 5, and Saguaro CT Unit No. 3 and associated property at its discretion and may secure financing for such units up to the limits heretofore established by the Commission, with any additional financing authority to be requested by APS in a separate proceeding in accordance with the provisions of A.R.S. § 40-301, *et seq.*"

RENUMBER other Findings of Fact accordingly.

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #2
(Exception No. 2)

Page 23, line 13

INSERT at conclusion of paragraph - "Because R14-2-1615(A) and R14-2-1606(B) have always been paired together and have historically been treated the same, we will likewise stay R14-2-1606(B) until at least July 1, 2004 and also until the asset transfers discussed above are implemented."

DELETE paragraph beginning on line 13 ½ to line 21 ½.

Page 29, line 15 ½

DELETE Finding of Fact No. 36.

INSERT new Finding of Fact No. 36 - "A.A.C. R14-2-1606(B) should be stayed and any portions of Decision Nos. 61973 and 62103 which refer to A.A.C. R14-2-1606(B) should be modified to stay the requirement that 100 percent of power purchased for Standard Offer Service shall be acquired from the competitive market, with at least 50 percent through a competitive bid process until at least July 1, 2004 and until the asset transfers discussed in Finding of Fact No. 35 are implemented."

Page 29, line 21 ½

DELETE Finding of Fact No. 37.

RENUMBER Findings of Fact accordingly.

Page 31, line 25 ½

INSERT after "...competitive bid process" the words "until at least July 1, 2004 and until the asset transfers are implemented."

DELETE ordering paragraph beginning on line 26 ½ and ending on page 32, line 2 ½.

Page 32, line 3

DELETE ordering paragraph beginning on line 3 and ending on line 6 ½.

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #3
(Exception No. 3)

Page 21, line 17 to line 21½

DELETE sentence (beginning on page 21, line 17 through sentence ending on page 21, line 21 ½).

INSERT - "We believe that the evidence on market power is contradictory, and we will decline to make a specific market power finding at this time pending submission of the additional market power analyses suggested herein."

Page 28

DELETE Findings of Fact Nos. 17 through 21.

INSERT new Finding of Fact No. 17 - "We believe the evidence on market power is contradictory, and we will decline to make a specific market power finding at this time."

RENUMBER Findings of Fact accordingly.

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #4
(Exception No. 3)

Page 21, lines 25-26

DELETE - "Accordingly, we adopt Staff's recommendations and"

INSERT - "We"

Page 21, line 27

DELETE – "with AECC and RUCO that the parties"

INSERT – "that APS and TEP"

Page 21, line 28

DELETE – "seek a consensus"

INSERT – "work with Staff to develop a common"

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #5
(Exception No. 4)

Page 32, line 18

DELETE - "within 60 days of the effective date of this Decision".

INSERT - "within 60 days of a final decision by FERC on Standards of Conduct in FERC Docket No. RM01-10-000, but no later than January 1, 2003".

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #6
(Exception No. 5)

Page 25, line 14 ½

DELETE paragraph starting on line 14 ½ to line 22 ½.

INSERT new paragraph at line 14 ½ - "We agree that transmission issues are important in transitioning to a competitive marketplace and we encourage an industry-wide planning process to address transmission constraints. However, transmission issues, including studies relating to RMR generation, should be addressed in our Biennial Transmission Assessment or in a subsequent rule making or similar docket as opposed to this proceeding. These issues should be considered in the light of their potential impact on native load customers and after rigorous cost/benefit analysis."

Page 30, line 1 ½

DELETE Finding of Fact No. 39.

INSERT new Finding of Fact No. 39 - "Transmission issues, including studies relating to RMR generation, should be addressed in our Biennial Transmission Assessment or in a subsequent rule making or similar docket as opposed to this proceeding. These issues should be considered in the light of their potential impact on native load customers and after rigorous cost/benefit analysis."

DELETE Finding of Fact No. 40.

DELETE Finding of Fact No. 41.

RENUMBER Findings of Fact accordingly.

Page 32, line 10

DELETE ordering paragraph beginning at line 10 to line 12.

DELETE ordering paragraph beginning at line 13 to line 14 ½.

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED AMENDMENT #7
(Exception No. 6)

Page 25, line 7 ½

DELETE - paragraph beginning at line 7 ½ to line 9 ½.

INSERT - "While FERC will continue to have jurisdiction over wholesale power sales after the assets transfer occurs, the Commission will still have significant jurisdiction over the service by electric public service corporations to retail customers. Further, the Commission's jurisdiction over such public service corporations is unaffected whether an RTO approved by FERC is for-profit or not-for-profit."

Page 30, line 20 ½

INSERT new Finding of Fact No. 46 - "The parties agree that the Commission's jurisdiction over public service corporations is unaffected whether an RTO approved by FERC is for-profit or not-for-profit."

Page 31, line 19

INSERT new Conclusion of Law No. 11 – "The Commission's jurisdiction over public service corporations is unaffected by whether such public service corporations participate in a for-profit or not-for-profit RTO."