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MEMORANDUM

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TO: THE COMMISSION

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FROM: Utilities Division

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Date: August 8, 1997

RE: IN THE MATTER OF THE COMPETITION IN THE PROVISION OF  
ELECTRIC SERVICES THROUGHOUT THE STATE OF ARIZONA.  
(DOCKET NO. U-0000-94-165)

On December 26, 1996, the Commission issued Decision No. 59943 in which it approved the issuance of new Rules (A.A.C. R14-2-1601 through A.A.C. R14-2-1616) to establish the framework under which retail electric markets in the State of Arizona will be opened to competition, and to streamline the regulatory process for setting rates for competitive electric services.

The Rules as approved clearly contemplate additional analysis and study to be undertaken to assure a fair, equitable and orderly transition to competition. They require the creation of various working groups to explore specific issues such as: stranded costs, unbundled and standard offer service, system benefits charges, reliability and safety, spot market development and independent system operation, the solar portfolio standard, legal issues associated with introducing competition into retail markets, and the method under which customers will be selected for participation in the phased-in transition. In connection therewith, six working groups were created and they, along with their respective subcommittees, have been meeting on a regular basis. These include:

- Stranded Cost Working Group
- Reliability and Safety Working Group
- Legal Issues Working Group
- Customer Selection Working Group
- ISO and Spot Market Development Working Group
- Unbundled Services and Standard Offer Working Group

The working groups and their respective subcommittees reflect a broad stakeholder participation, including representatives from investor-owned utilities, co-operatives, competitive power suppliers, consumer representatives, government agencies, and the Commission Staff.

Arizona Corporation Commission  
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Although consensus thus far has been difficult to achieve on a number of issues, work continues toward the development and issuance of working group reports to the Commission as provided in the Rules.

Based on the work done thus far, one thing is very apparent to Staff. In order to achieve an efficient transition to retail competition, there will undoubtedly have to be additions, deletions and modifications to the Rules in their present form. Examples of the need for such changes have been identified by each of the working groups.

In their present form, the Rules provide little guidance with respect to the manner by which stranded costs should be quantified and recovered. The Stranded Cost Working Group has achieved fairly substantial consensus that stranded costs should be allocated to jurisdictions and customer billing classes in a manner consistent with the specific company's current rate treatment of the underlying stranded asset in order to affect recovery of stranded costs in substantially the same proportions as the recovery of respective asset. The Commission should consider whether language covering this principle should be added to the Rules. The working group has also had considerable discussion with respect to the current Rule (R14-2-1607.J) limiting recovery of stranded costs to just those consumers taking competitive power. Depending on the method used to compute and recover stranded costs, and other relevant considerations, this may be impractical or lead to economic disincentives. Some modification of the Rule may be necessary.

The Reliability and Safety Working Group and the ISP and Spot Market Development Working Group have recognized the possibility of having to modify or add to the existing Rules. Both have been affected by the recent commencement of activities of an organization called Desert Star, a group of transmission-owning utilities, users and other interested parties, exploring the creation of an ISO covering Arizona, New Mexico, West Texas, and Southern Nevada. Depending upon the results of the Desert Star efforts, there may need to be some modification of the wording of the Rule related to reliability. Moreover, depending on the final results of the deliberations of the Reliability and Safety Working Group, there may be some additional recommendations to adopt specific rules covering reliability and safety standards.

The Unbundled Services and Standard Offer Working Group believes there is an ambiguity in the Rules (R14-2-1608.A) with respect to whether the systems benefit charge is intended to cover only the actual dollar amounts to fund specific programs (as approved by the Commission prior to adoption of the Rules), or whether the Commission's intent was to fund programs at whatever amount is necessary. Some clarification of the Rules in this regard is desirable. Within the Solar Portfolio Standard Subcommittee there is substantial agreement that the Standard (R14-2-1609) should be modified to better reach the objectives of the Standard.

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The Customer Selection Working Group has also recognized a need to modify or add to the current Rules. Some participants believe the existing phase-in provision should be replaced with a "flash cut" to competition as is contemplated in California. There is also a perceived need to add rules covering consumer education responsibilities, and to provide a process for reviewing the utilities' customer selection plans. Clarification is also required for rules covering Commission certification of energy service providers and what customer information can or should be provided by utilities to potential service providers.

Based on the foregoing, and numerous other concerns being raised by all stakeholders, it is Staff's belief that the Rulemaking Docket should be reopened so that the Working Group Reports can be added to the Docket and further proceedings scheduled. By examining the Rules in their current form, it is obvious that such a subsequent action was clearly anticipated. With the working group reports to be issued shortly, now is a good time to take this action. In order to achieve an effective and fair transition to retail electric competition, the Rules must be unambiguous and comprehensive.



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Utilities Division

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CWD:CWD/rkt/ACK