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October 14, 1997

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DOCUMENT CONTROL

Arizona Corporation Commission

DOCKETED

RE: Docket No. U-00094165
In the Matter of Competition in the Provision
of Electric Services Throughout the State of Arizona

OCT 15 1997

Gentlemen:

DOCKETED BY

For the past nine months the Arizona Utility Investors Association has been an active participant in nearly all of the deliberations of the various working groups created by the Commission in its rule authorizing retail electric competition. AUIA has also participated in the feasibility work on the proposed independent system operator dubbed Desert STAR.

Having been immersed in detail in the issues involved in implementing retail competition, we now believe it may not be possible for the Commission to meet all of its rulemaking and other regulatory obligations in time to achieve an orderly start to competition on January 1, 1999.

I am writing on behalf of the AUIA Board of Directors to urge you to undertake a review of Commission responsibilities to determine whether the start date in the rule is still feasible or whether the phase-in should be postponed. If your analysis concludes that the start date is viable, then we strongly recommend that you establish a firm schedule for completing the required tasks by September 1, 1998.

As I will discuss in more detail, there is a massive amount of procedural work to be done and a whole catalogue of decisions to be made before consumers can be exposed to a competitive electric industry. The fact is that the working groups have provided little practical guidance other than a very long list of issues to be resolved.

This does not imply any criticism of the Commission or its staff. It is the result of an abbreviated rulemaking and a follow-up process in which almost none of the participants except utilities and their investors share any risk of failure and therefore are not motivated to resolve the issues.

In examining the work remaining to be done, the Commission should be realistic about timing. You do not have until end of 1998 to get ready. As a practical matter, if preparations aren't completed by the end of next summer, it will be too late to provide adequate public education and to prevent utility investors from suffering in the financial markets. That leaves about nine months to deal with the following:

1. Continued Rulemaking

The Commission recently reopened the competition docket to consider changes to the rule to clarify its meaning or fill in gaps and provide missing links. Presumably, most of the proposed changes will relate to the issues that were assigned to the working groups. Included in these assignments were questions regarding the quantification and collection of stranded cost, methods of customer selection, solar requirements, system benefits, metering and billing procedures, safety and reliability, unbundled and standard offer service, tax and accounting issues and so on.

As you are probably aware by now, the working groups reached almost no consensus on key issues. That means that almost any proposed changes will be contested by some of the intervenors. Not all working group reports have been completed, so we do not have a precise count of unresolved issues that require a Commission decision. However, to date more than 50 policy issues have been identified which must be decided before competition can begin. This will be a contentious and time-consuming process which must be completed before much other progress can be made.

In addition to clarifying the competition rule (Article 16) it is also not compatible with a number of existing provisions elsewhere in Title 14 of the Commission's rules which will have to be amended.

2. Operating Protocols

Once the policy issues have been decided, there are critical licensing and protocol agreements which must be negotiated and approved by the Commission before competition can proceed. The essence of retail competition is that many new entities will aggregate and schedule loads and some will introduce their own metering and billing systems. These entities may include unregulated cities and towns. According to Desert STAR timelines, there will be no independent system operator (ISO) in place until after 2000, so existing Control Area Operators will be in charge of the grid.

Extensive protocols involving scheduling, metering, load profiling, connections and disconnections, billing, reserve requirements, system imbalances and other operating issues will have to be in place to head off massive disputes and system breakdowns. These protocols must be operational before competition can even be described accurately to consumers. They have barely been mentioned in the working groups.

3. Unbundled Tariffs, System Benefits

The rule requires Affected Utilities to file tariffs for unbundled services and standard offer service by the end of this year. We assume that the Commission will have to provide an opportunity for hearings on these tariffs. Based on the working group discussions, there will be a number of intervenors with significant disagreements on the content of the filings.

Consumer groups and environmental organizations will battle to expand the scope of programs funded by system benefits; solar proponents will argue for additional applications to be included; new market entrants will seek guarantees against cross-subsidies in the rates; and various contracting organizations will campaign to ban utilities from offering certain competitive services. These will also be contentious proceedings, but we've hardly started.

4. Stranded Cost Proceedings

The rule identifies 12 Affected Utilities. How many will attempt to recover stranded costs is unknown, but it is certainly possible that the Commission will face about 10 simultaneous stranded cost proceedings. In essence, these are rate cases requiring a fair value rate base determination, a rate of return, a revenue requirement and a calculation of the effects of retail competition.

Each of these cases will be contested. Typically, the ACC requires one to two years to resolve a contested electric rate case. (In fact, the last rate reduction took eight months to settle.) Obviously, this is a critical issue for thousands of Arizona utility investors. Given a Jan. 1, 1999 start date, if stranded cost recovery isn't resolved before next fall, the Affected Utilities will risk a financial beating from market analysts, rating agencies and accounting rules.

5. Intergovernmental Agreements

Simultaneous with these other requirements the Commission must negotiate and hold hearings on an intergovernmental agreement (IGA) with Salt River Project and perhaps other municipal utilities which may want to enter the competitive market. It is probable that any proposed IGA will draw intervenors who have divergent interests in its provisions.

6. Public Information and Education

Nearly everyone agrees that a public communications program using a variety of media is essential to the success of retail competition. Only informed consumers will reap benefits from the competitive market. In order to achieve adequate market penetration, a communications program should be in operation several months before the start of competition, especially to overcome the distractions of the holiday season. Regardless of who is ultimately responsible for public education, every entity involved in this proceeding will want to help design it. If we started to develop this program today, we would be fortunate to have it ready in time.

7. New Market Entrants

Although the timing may not be as critical as for the issues already discussed, it is nevertheless true that the Commission will also have to review, approve and perhaps hold hearings on numerous applications for CC&Ns along with associated tariffs. It would not be surprising if some of the applications and tariffs were disputed by other parties. In any case, these applications would have to be dealt with well in advance of the start date of competition.

8. The Fail-Safe Syndrome

Finally, there is a disturbing trend lurking in the working group reports. There are several areas in which the substitute for a policy decision is to cast the Affected Utilities as the final defense against failure. They are designated as the providers of last resort, the metering and collection agents of last resort, the guarantors of assured power reserves, the defenders against system imbalances and so on. In other words, if the competitive system fails in any respect, the utilities and their investors are expected to come to the rescue. There is no such thing as a fail-safe competitive market. The Commission should examine these concepts and adopt policies that will lead to an unshackled marketplace.

Summary

AUIA is sure you will agree that none of the tasks we have cited can be glossed over or treated lightly. A deliberate and thoughtful approach to resolving them is critical to the smooth operation of a competitive market for electricity. The alternative is to court disaster in the marketplace resulting in great harm to utility customers and investors alike.

We urge you to examine carefully the time and resources you have at your disposal to determine how competition involving all customer classes can be achieved by Jan. 1, 1999. If that continues to be your goal, AUIA resolves to assist in every way possible to reach it, but there must be a road map and we must step on the accelerator.

Sincerely,



Bill Meek
President

cc: Distribution
Legislative Study Committee
Docket Control