

OPEN MEETING



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ORIGINAL

MEMORANDUM RECEIVED

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2007 JUN 12 P 3:47

TO: THE COMMISSION

FROM: Utilities Division

AZ CORP COMMISSION
DOCKET CONTROL

DATE: June 12, 2007

RE: IN THE MATTER OF THE ARIZONA PUBLIC SERVICE COMPANY APPLICATION FOR AUTHORIZATION TO (1) ENTER INTO A TRANSFORMER SHARING AGREEMENT, (2) TRANSFER A PORTION OF THE ROUND VALLEY SUBSTATION, (3) TRANSFER THE WADDELL SUBSTATION, AND (4) FOR PRE-APPROVAL OF CERTAIN FUTURE TRANSACTIONS UNDER A.R.S. §40-285(A) - (DOCKET NO. E-01345A-06-0770)

On December 8, 2006, Arizona Public Service Company ("APS") submitted an application to the Arizona Corporation Commission ("Commission") for authorization to:

- I. Enter into an Edison Electric Institute ("EEI") Spare Transformer Sharing Agreement ("Sharing Agreement") with other utilities for high voltage and extra high voltage transformers in the event of an act of deliberate destruction.
- II. Sell a portion of its Round Valley Substation to Southwest Transmission Cooperative.
- III. Sell its Waddell Substation property to Suburban Land Reserve, Inc. ("SLR").
- IV. Pre-approve certain transactions up to \$1 million.

I. Transformer Sharing Agreement

APS desires to enter into a Transformer Sharing Agreement with approximately 50 other utilities in the United States and Canada to ensure that critical high voltage (230 kV) and extra high voltage (345 kV and 500 kV) transformers will be available to APS or other affected utilities in the event of an act of deliberate destruction. The benefit to APS and its customers is that transformers would be available to APS to rebuild damaged portions of its transmission system due to an act of deliberate destruction, and the inventory of spares available to APS would be greater in number and lower in cost than APS could obtain as an isolated utility preparing for a similar event. The Sharing Agreement will also require APS to possibly sell or otherwise dispose of or encumber these assets in this program on short notice to other participants, and it is this "selling of these assets" as described in A.R.S. §40-285(A) for which APS is specifically requesting approval.

Arizona Corporation Commission

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APS states that it desires to participate specifically in the 500/230 kV class of transformers utilizing two units it now has available at its Westwing Substation. Also, it is anticipated that APS will join the 345/230 kV class (as soon as a sufficient number of other companies commit to this class) utilizing one unit it now has available at Pinnacle Peak Substation. Additionally, APS expects its participation would soon thereafter extend to the 230/69 kV class based on further review with other utilities and a determination of requirements to participate in this class. The review in the 230/69 kV class is ongoing; however, APS expects its participation would be four 230/69 kV transformers (as updated in APS' March 9, 2007 data response) for which it does have candidate spares and, therefore, it requests the approval to also include these transformers in the Sharing Agreement.

In total, the Application requests commitment for two 500/230 kV transformers, one 345/230 kV transformer and four 230/69 kV transformers to be included in the Sharing Agreement, and as a condition of that Sharing Agreement, these transformers could then be sold (as defined in A.R.S. §40-285(A)) to other participants in the Sharing Agreement on the required short notice. This transaction would then proceed without further Commission approval of the sale of these assets.

Utilities Division Staff ("Staff") has reviewed the particulars of the Application with regard to the Sharing Agreement and makes the following observations:

- a) APS owns and operates 500 kV, 345 kV and 230 kV stations in Arizona and New Mexico and has an obligation to ensure timely restoration of service in the event of an act of deliberate destruction. The Sharing Agreement addresses acts of deliberate destruction.
- b) The longest manufacturing lead time of transmission components for electric utilities is for 230 kV high voltage and 345 kV and 500 kV extra high voltage transformers (approximately 18 months), and it is therefore necessary for utilities to plan for access to readily available transformers if certain unforeseen events occur.
- c) APS owns or is a participant owner in a sufficient number of spare high voltage and extra high voltage transformers to participate in the Sharing Agreement depending on the level of participation of other utilities in each voltage class. A minimum MVA (million volt-amp, closely equivalent to MW) requirement for each voltage class is set by EEI, and as members commit to that class, the MVA requirement is then divided among the members. As the number of utilities participating in any voltage class increases, the MVA requirement for each participant in that overall class decreases accordingly.
- d) APS has 11 in-service 500/230 kV transformers and four 500/230 kV single phase transformers (two of which are "in service" spares). The capacity of the two spare transformers APS is prepared to commit to this program totals 931 MVA. This is insufficient to meet the requirement for joining this class at this time which is 1,029

MVA for the next member (11th) to join. APS would wait until the 13th membership is open as its 931 MVA commitment would meet the then reduced requirement of 848 MVA.

- e) APS has three in-service 345/230 kV transformers and one 345/230 kV spare plus one jointly owned spare at Four Corners that could be utilized for local needs. The capacity of APS' single spare transformer is 600 MVA which is insufficient to meet the requirement for joining this class at this time. APS would wait until sufficient membership is achieved such that a 600 MVA commitment in this voltage class would allow membership.
- f) APS has 48 in-service 230/69 kV transformers and four 230/69 kV spares. The capacity of these four spare transformers is 486 MVA which is insufficient to meet the requirement for joining this class at this time. APS would wait until sufficient membership is achieved such that a 486 MVA commitment in this voltage class would allow membership.
- g) Acts of deliberate destruction are appropriate events for utilities to prepare for, and the Sharing Agreement provides the necessary inventory to be prepared for this class of event. Additionally, other localized emergencies and/or failures require similar planning and are addressed by individual utilities through maintaining a suitable number of spares on its system and some reliance on other utilities. Both programs, the acts of deliberate destruction and the localized emergency/failure events, may complement each other; i.e., the same transformer may be used in both categories as long as due consideration is given to depletion of the spares inventory for localized use.
- h) Utilities may use their spare units under the acts of deliberate destruction category for any other purpose (for their own routine failed unit needs for example) as long as it or a replacement is restored to the acts of deliberate destruction inventory within 18 months.¹ Additionally, APS has protected its own local emergency needs for all transformers that are or will be included in the Sharing Agreement through a "Permitted Disposition" provision in the Sharing Agreement. This provision provides APS with the discretion to assess their own imminent reliability or other pertinent considerations before proceeding with a transformer sale, and if APS conditions so warrant, APS will maintain that transformer for its own use.
- i) This Sharing Agreement will allow APS to transfer or sell the transformer equipment included in this Application on the very short notice required in emergencies associated with acts of deliberate destruction.
- j) Staff has inspected the two 500/230 kV single phase transformers at Westwing Substation and finds them both to be acceptable inventory for use as may be needed

¹ Pg. 23 of July 18, 2006 EEI Spare Transformer Sharing Agreement

under the acts of deliberate destruction program or other emergency or failure incidents. Staff also finds that the quantity of two 500/230 kV single phase transformers requested for the acts of deliberate destruction program is appropriate considering the possible exposure of this class of transformer on the APS system. It is also noted that APS shares ownership of these 500/230 kV transformers with Western Area Power Administration and Salt River Project. These co-owners are in agreement with the use of these transformers as spares under the acts of deliberate destruction program. The APS net book values for the respective transformers are \$201,656 and \$740,004. Both units are presently stored on site as spares ready for future use as required.

- k) Staff has inspected the single 345/230 kV three-phase transformer at Pinnacle Peak Substation and finds it to be acceptable inventory for use as may be needed under the acts of deliberate destruction program or other localized emergency or failure incidents. Staff also finds that the quantity of one 345/230 kV transformer requested for the acts of deliberate destruction program is appropriate considering the reduced exposure in number of this class of transformer on the APS system as compared to the 500/230 kV class. It is also noted that APS owns 100 percent of this 345/230 kV transformer and it has a net book value of \$253,536. The unit is presently on site and in service; however, it is to be replaced by June 1, 2007, at which time it would become available as a spare ready for future use as required.
- l) Staff has not inspected the four 230/69 kV transformers requested in this Application as the study for this requirement is ongoing. The use of 230/69 kV transformers on the APS system is widespread and there are multiple available spares to handle previously expected contingencies. It is expected that a requirement of four 230/69 kV transformers will satisfy APS' obligation for this voltage class under the acts of deliberate destruction category and that this commitment can be made from the available spare inventory. It is noted that APS owns 100 percent of all 230/69 kV transformers on its system. The four transformers are booked as inventory and therefore do not carry a net book value. The transformers do carry an inventory value equal to their individual original cost. The two 55 MVA transformers identified as candidates for the Sharing Agreement have inventory values of \$114,654 and \$144,248. The two 188 MVA transformers identified as candidates for the Sharing Agreement have inventory values of \$1,565,450 and \$1,152,150.
- m) The Sharing Agreement indicates similar utility participation throughout the continental United States.
- n) Staff recognizes that the transformers identified at this time as candidates for the Sharing Agreement are subject to change over time due to usage by APS, sale to others, failure, retirement, and other possible factors. Participation in a particular voltage class requires commitment of a prescribed total capacity (MVA) of transformers, not specifically identified units. The determining factor for the transformers in the Sharing Agreement for each voltage class is the minimum MVA required by EEI in that voltage

class which is determined by the total EEI requirement divided by the number of participants. As participation in the Sharing Agreement increases, the MVA requirement for each utility to participate decreases.

- o) The sale of any transformers under this Sharing Agreement is not intended to produce a profit for the seller and, therefore, all sales are priced at either the seller's depreciated book cost or the market price for a replacement transformer, at the seller's option, plus expenses of the transaction.

Staff supports the concepts of the Sharing Agreement and APS' participation in the program. APS benefits in this program as do other participants by increasing their available stock of high voltage transformers to restore service following acts of deliberate destruction. Additionally, the risk of over committing APS system spare transformers in this Sharing Agreement program in lieu of its own emergency needs or unexpected contingencies has been adequately addressed through the "Permitted Disposition" provision of the Sharing Agreement.

Staff recommends that the Commission grant APS approval to enter into and participate in the EEI Spare Transformer Sharing Agreement in the 500/230 kV voltage category, the 345/230 kV voltage category, and the 230/69 kV voltage category. Participation will occur after the EEI requirement is decreased to 931 MVA in the 500/230 kV voltage category, 600 MVA in the 345/230 kV voltage category, and 486 MVA in the 230/69 kV voltage category.

Staff further recommends that APS be allowed to sell not more than two 500/345 kV transformers totaling a maximum of 931 MVA to meet its commitment in the 500/345 kV voltage category; not more than one 345/230 kV transformer totaling a maximum of 600 MVA to meet its commitment in the 345/230 kV voltage category; and not more than four 230/69 kV transformers totaling a maximum of 486 MVA to meet its commitment in the 230/69 kV voltage category; all subject to the following condition:

- The Company should file reports pursuant to this EEI Spare Transformer Sharing Agreement with Docket Control within sixty days of any transaction summarizing each transfer, sale, mortgage, lease, or assignment entered into pursuant to this order.

II. Sale of a Portion of Round Valley Substation

APS owns and operates the Round Valley Substation in Coconino County, Arizona and provides transmission services to Southwest Transmission Cooperative ("SWTC") utilizing electric facilities in this substation under APS' Open Access Transmission Tariff ("OATT"). SWTC serves Mohave Electric Cooperative ("MEC"), one of its distribution cooperatives, through APS' Round Valley Substation's electric facilities. SWTC desires to extricate itself from the cost of this APS transmission service through purchasing the requisite portion of the Round Valley Substation and assuming the associated future operations, maintenance and other obligations of the facility. The sale price of the agreed on 50 percent ownership interest in the facility is \$450,900, and the APS substation would become a joint-use facility with APS and

SWTC equally sharing in the ongoing cost of the facility. As a joint use facility, SWTC will no longer be subject to APS' OATT.

Staff has reviewed the particulars of the Application with regard to the Sale of a Portion of Round Valley Substation and makes the following observations:

- a) The Round Valley Substation presently contains the 230 kV facilities of APS and Western Area Power Administration ("WAPA") with an adjacent 230/69 kV facility owned by MEC. The WAPA and MEC facilities are both electrically connected to the APS equipment and operate together; however, the facilities of all three entities are identifiable and distinct except for some minor commonality in the control house which is shared by APS and WAPA.
- b) The APS portion of the Substation is comprised of one 230 kV 1,200 amp oil circuit breaker, three 230 kV air switches, rigid and strain bus, steel support structures, potential devices, control house with relay panels and communication interface, foundations, and various other ancillary devices to support the operation of the facility. The land for the Substation is leased. The APS Substation portion of the yard was placed in service in 1958.
- c) The sale price and percent ownership of a sufficient portion of the APS facility by SWTC to negate the APS OATT was derived through a negotiated settlement of offered and counter-offered sales prices and ongoing obligation costs.
- d) The sale price of 50 percent of the facility at \$450,900 and the division of future obligations, including the land lease (50 percent to APS and 50 percent to SWTC), were derived through the negotiation process between APS and SWTC.
- e) APS would apply the \$450,900 sale price to reduce total depreciation which will benefit APS customers by reducing the rate base correspondingly. Rate base is directly proportional to the utility's net asset value, where net asset value is the original cost of plant less depreciation. In this case, the \$450,900 sale price is credited to Federal Energy Regulatory Commission ("FERC") Account 108 (accumulated depreciation), thereby increasing the depreciation account and reducing the rate base.
- f) Also, the 50 percent obligation to SWTC for future operations, maintenance and land lease cost will benefit APS customers. These benefits to APS customers will be offset (more or less) by the reduction in transmission tariff cost no longer received by APS.
- g) SWTC will no longer be required to pay the APS OATT of approximately \$137,000 annually when the sale is completed. This amount would be allocated to wholesale (FERC) service for ratemaking purposes and would not impact retail rates. This annual payment loss was likely inevitable either through litigation or through SWTC

completely bypassing the Round Valley Substation, both options of which were under review by SWTC.

h) Staff has inspected the facility and determined that APS' representation of the facilities in function is accurate. Additionally, the facilities were in place with consideration for good engineering design and practice. Staff did point out two issues of concern to APS which subsequently were adequately addressed. They were:

- A spare steel structure approximately 10 feet tall was stored vertically against the active structure supporting the 230 kV bus and ancillary devices. APS reviewed the situation and advised it did not view this as a safety or reliability concern; however, the spare structure was moved away from the active structure and stored horizontally. Staff believes this was the proper action.
- Oil containment for the three oil filled breakers was lacking. Staff noted this appeared inconsistent with other APS installations and was questionable especially with the downward slope of the substation pad appearing to be well in excess of one percent (thereby exacerbating the flow of oil off the site). APS reviewed this facility and advised that the site was not subject to Spill Prevention, Control and Countermeasure ("SPCC") regulations as promulgated by the Environmental Protection Agency. APS' computer modeling determined there was no environmental impact for an oil leak at this location considering the oil volume available and topography of the area. Staff considers this response acceptable.

APS indicated to Staff that the approximate rate paid by SWTC under the original 1974 contract was \$30,408 annually. Under the current OATT rate, SWTC pays approximately \$137,000 annually. According to APS, SWTC has considered "building around" the Round Valley Substation to avoid the OATT tariff by installing its own facilities near Round Valley.

Staff believes such an alternative could be duplicative in nature and would be a higher cost solution to the high OATT rate problem. Staff further believes that SWTC's participation in the Round Valley Substation by purchasing 50 percent of the facility, paying 50 percent of the land lease payment, and paying 50 percent of the ongoing costs of the facility would be a lower cost alternative that could be beneficial to Arizona ratepayers.

Staff therefore supports the sale of 50 percent of the Round Valley Substation to SWTC and a sharing agreement with SWTC to evenly share the ongoing operations of the facility on a 50 percent APS 50 percent SWTC basis.

Staff recommends that the Commission grant APS approval to sell 50 percent of the Round Valley Substation to SWTC subject to the following conditions:

1. The sale price for 50 percent ownership of the substation would be \$450,900 and the full sale price would be credited to APS accumulated depreciation/salvage (FERC Account 108).
2. APS would enter an Operations and Maintenance Agreement with SWTC for an even cost sharing of future operations, ongoing land lease payments, maintenance, replacements, upgrades and other services in connection with the joint ownership of the substation.

III. Sale of the Waddell Substation

APS desires to sell the property it owns at Cotton Lane and Cactus Road in the County of Maricopa and the City of Surprise, Arizona and which presently contains an operational distribution substation known as Waddell Substation. The existing site is subject to reductions in size due to an upcoming road widening, and it is already inadequate to handle the future electric facilities needed in this growing area. It is to be replaced by a new substation at a larger nearby site. Once the new substation is built and energized, APS would then remove the electrical equipment at the Waddell Substation and complete the land transfer to the new owner, Suburban Land Reserve, Inc.

Staff has reviewed the particulars of the Application with regard to the Sale of Waddell Substation and makes the following observations:

- a) The Waddell Substation has a capacity of 30 MVA and is supplied by one incoming 69 kV feeder and has three outgoing 13 kV feeders. The electrical facilities and land are 100 percent owned by APS.
- b) The electrical equipment on the site is comprised of two 20 MVA transformers, three 13 kV breakers, various 13 kV and 69 kV air switches, rigid and strain bus, wood structures and steel structures on permanent foundations and temporary supports, equipment foundations, relay and communication interface, and various other ancillary devices to support the operation of the facility. The Substation and most of the active equipment are in excess of 30 years old with the exception of one 20 MVA transformer and associated equipment which are less than 30 years old. The equipment less than 30 years old is generally salvageable and suitable for use elsewhere on the APS system. The equipment older than 30 years, with the possible exception of the 20 MVA transformer, is not generally salvageable.
- c) The Waddell Substation has a relatively small footprint for a substation (107 feet by 183 feet), and the site size is being diminished by road widening which will reduce its dimensions to 107 feet by 118 feet. This reduced size of the site is not adequate for the present 30 MW capacity of the station and is not capable of supporting the capacity increases necessary with expected load growth. Staff believes it is appropriate to

incorporate the Waddell Substation capacity into a new and expandable nearby facility as APS plans.

- d) The new substation site replacing Waddell Substation is approximately one mile from the Waddell Substation and is well positioned to handle the increasing load of this developing area. It also has a significantly larger footprint (320 feet by 265 feet) to accommodate increased facilities for greater capacity. The new substation site referred to as the "Sarival Site" is being procured by APS from the buyer of the Waddell Substation Site, SLR, and both transactions are contained in the same agreement.
- e) Staff has inspected the facility and determined that APS' representation of the facilities in function is accurate. Additionally, the facilities with the consideration noted below were in place with consideration for good engineering design and practice.
- Various steel structures supporting insulators, bus, switches and other ancillary devices are mounted on temporary steel plates in lieu of standard concrete foundations. These structures are generally associated with the recent addition of the newer 20 MVA transformer and its associated 69 kV supply and 13 kV outgoing feeder. Considering the short-term nature of this installation, Staff does not object to this type of construction as long as all applicable standards and codes are met.
- f) The sale price for the Waddell Substation site is based on appraised value of similar sites and is approximately \$5.00 per square foot adjusted for this site. Staff has reviewed appraisals provided by APS and concurs with the \$5.00 per square foot determination. The resultant sale price of \$63,235 is commensurate with the reduced site size due to road widening (12,626 square feet). The purchase of the new "Sarival Site" from SLR is similarly based upon a purchase price of approximately \$5.00 per square foot.

Staff is in concurrence with APS' sale of the Waddell Substation site to SLR and the associated procurement of a new site and construction of a new replacement substation in the area.

Staff recommends that the Commission grant APS approval to sell to SLR the land containing the Waddell Substation, located at Cotton and Cactus Lane in the Phoenix West Valley, subject to the following conditions:

1. The sale price of the land for the site would be \$63,235.
2. The decommissioning of electrical service at Waddell Substation would be coordinated with the construction and commissioning of the new area substation such that no interruptions in customer electric service would occur.

3. The after tax loss of \$12,691 associated with this transaction would be credited against after tax gains. The net gain/loss on the sale of this asset would be equally shared between ratepayers and shareholders.

IV. Pre-Approval for Qualifying Transactions

APS requests pre-approval from the Commission to transfer, sell, mortgage, or lease used and useful property without first securing an order from the Commission authorizing each specific transaction. APS proposes that the pre-approval be subject to certain conditions and limitations:

- a) The transfer price or transaction price for individual transfers, sales, mortgages or leases would be limited to \$1,000,000.
- b) The Company would report information summarizing each transaction entered into under the pre-approval semi-annually.
- c) The net gain on such transfers, sales, or mortgages would be evenly split between APS shareholders and ratepayers with the ratepayer portion to be credited to an account accruing interest at the same rate as customer deposits for use to benefit ratepayers either by a direct refund or by expenditure of the funds for programs to directly benefit ratepayers.

The requested pre-approval would apply to transfers, sales, leases, or mortgages that are subject to A.R.S. §40-285(A), and not exempt under A.R.S. §40-285(C), and also meet APS' prescribed conditions and limitations; that is, transactions not exceeding \$1,000,000 involving used and useful plant and other property. Transactions that fall within the statutory requirements for Commission approval and exceed \$1,000,000 would continue to require specific Commission approval on a case-by-case basis. Sales or other transactions involving property not necessary for the performance of APS' duties to the public would continue to require no Commission approval.

APS states that the benefits and advantages of the proposed pre-approval include:

- a) Pre-approval will facilitate the Company's ability to respond to changing needs and to maximize efficient use of assets.
- b) Pre-approval will enable the Company to act rapidly to take advantage of opportunities that may not remain available for the time required to obtain specific Commission approval.
- c) Pre-approval should reduce the administrative burden on the Commission and the Company.

- d) Pre-approval should minimize the transaction costs involved in disposing of properties and facilitate the Company's ability to move forward in a timely manner.

Staff reviewed APS' proposal and investigated the legal, procedural, and economic ramifications of the requested pre-approval. Staff sought information to help it to determine whether Commission pre-approval would satisfy public service corporation obligations under A.R.S. §40-285(A). A.R.S. §40-285(A) requires a public service corporation wishing to sell, lease, assign, mortgage or otherwise dispose of or encumber plant or other property necessary or useful in the performance of its duties to the public, to first obtain an order from the Commission granting it authority to do so.

In its review, Staff determined that a similar case involving the granting of pre-approval had been ordered when the Commission granted APS pre-approval for qualifying transfers, sales, or mortgages under A.R.S. §40-285(A) in Decision No. 60481, November 25, 1997, as amended by Decision No. 61708, May 13, 1999. Pre-approval was granted under these decisions for certain individual transactions not exceeding \$500,000. Additional conditions on the pre-approval granted under these decisions set an annual cap for pre-approved transactions at \$5,000,000 per calendar year, after which all subsequent transactions that year exceeding \$100,000 require specific Commission approval. The pre-approval granted in these decisions is still in force, and it appears that it might have been used by APS to meet its statutory obligation to obtain Commission approval for the sales requested in Items II and III of this Application if those decisions had been interpreted broadly. However, interpretations have varied regarding whether the pre-approval granted in Decision No. 60481, as amended by Decision No. 61708, applies only to qualifying street lighting equipment or if it applies generally to all types of plant and other used and useful property.

In discussions with Staff, APS stated that it included Item IV in its Application to obtain an order from the Commission granting the Company pre-approval authority for all types of qualifying plant and other property, not just street lighting plant and equipment. APS is also proposing to increase the cap on individual qualifying transactions from \$500,000 to \$1,000,000.

It is not anticipated that a high volume of sales or other transactions would take place under APS' proposed pre-approval, if granted. Indeed, only 12 transactions were completed under the pre-approval granted in Decision No. 60481 from November 1997 to date, and all but two of those transactions were for the sale of streetlighting systems. Other than the items in the instant Application, APS has made only one other individual request for approval for sale of used and useful property in the past five years. Transactions that may qualify for the requested pre-approval often involve the sale of smaller outgrown facilities to move to larger facilities and may include the following, for example:

- Sale of a service center building and land parcel
- Sale of substation land that has been outgrown (such as Waddell Substation)
- Sale of a communications site
- Sale of a small portion of a transmission line

- Sale of a pole yard or other work or storage site

The Company is proposing to utilize some of the same procedures and accounts that were used to implement Decision No. 60481 and its amendments in Decision No. 61708 (Application p. 6, items b and c). After reviewing APS' pre-approval request, Staff views it as a request to gain pre-approval for transactions involving all types of qualifying used and useful plant and equipment and to raise the individual transaction cap to \$1,000,000.

Staff agrees that it could be advantageous to grant APS pre-approval for certain smaller qualifying transactions. Indeed, in a rapidly growing service territory, APS must be able to respond to changing needs and to take advantage of opportunities quickly, efficiently, and economically. The Item III Waddell Substation scenario, for example, is likely to recur in the future. This is a situation where a small rural substation is no longer of adequate capacity to serve an area that has transformed from farm land into a developed residential/commercial area. Staff recognizes that pre-approval could help to minimize transaction costs involved in disposing of some smaller properties and facilities and could therefore save ratepayers money. Staff also believes that pre-approval could reduce administrative burden on the Commission and allow the Commission to expend its time on more substantive issues. Staff is currently not aware of any disadvantages to allowing some form of pre-approval for many smaller transactions.

Staff examined the terms and conditions of the pre-approval granted in Decision No. 60481, as amended by Decision No. 61708, and found them to contain some appropriate safeguards and procedures to ensure that implementation of the pre-approval was reasonable, fair, and efficient. Staff examined the \$500,000 individual transaction limitation for pre-approval imposed in 1997 and considers that it was reasonable at that time. Staff applied various inflation indices to the \$500,000 individual transaction cap in 1997 and found that a limit in the range of \$600,000 - \$800,000 would be the equivalent level today. Staff similarly reviewed the inflation effect on the \$5,000,000 existing annual cap and the lower \$100,000 individual transaction cap that becomes effective after the annual maximum is reached in a calendar year. Staff believes that additional benefits would accrue to ratepayers, the Commission, and the Company if pre-approval were allowed to apply to qualifying transactions involving other types of used and useful plant and property in addition to street lighting.² However, because the pre-approval would apply to a broader array of used and useful assets, Staff believes that additional conditions on such pre-approval would be appropriate.

Staff recommends that the Commission grant APS pre-approval to transfer, sell, mortgage, lease, assign, or otherwise dispose of or encumber, in whole or in part, tangible or intangible property otherwise subject to A.R.S. §40-285(A) (used and useful property), and not exempt under A.R.S. §40-285(C) (property other than used and useful), subject to the following conditions and limitations:

² The present benefits are derived from APS and customer shared transactions and held in account generally with a balance less than \$100,000 until a Commission approved disbursement.

1. Individual transfers, sales, mortgages, leases, or assignments shall not exceed a per transaction cap of \$750,000.
2. Logical transactions shall not be disaggregated into separate component transactions for the purpose of allowing them to fall under the \$750,000 cap.
3. The cumulative amount of such transfers, sales, mortgages, leases, or assignments shall not exceed \$7,500,000 in any single year except as provided for in condition/limitation (4.) immediately following.
4. Once the \$7,500,000 accumulation threshold is reached in any calendar year, all subsequent qualifying transactions exceeding \$150,000 during the remainder of the year would require specific Commission approval.
5. Fifty percent of the net gain on pre-approved transfers, sales, mortgages, leases, or assignments shall be credited to APS ratepayers by placing the ratepayers' portion of the gain in a separate account that accrues interest at the same rate as customer deposits. The account to be utilized in compliance with this order shall be the same account currently utilized for compliance with Decision No. 60481 as amended by Decision No. 61708. This account has generally maintained balances less than \$100,000 over the last four years. No less often than once each two years on April 30 of even numbered years, the entire amount in the account, if \$100,000 or greater, will be either refunded to customers or utilized by APS to fund programs that will directly benefit customers as directed and approved by the Commission. However, should the amount in the account reach \$1.5 million earlier than six months prior to an April 30 disbursement date, disbursement of the entire amount in the account, in the manner described above, shall be undertaken as soon as is practicable. Customers receiving service under special contracts will not be eligible to receive such refunds. Any funds currently in the account as a result of Decision No. 60481, as amended by Decision No. 61708, shall be carried over, added to any future funds placed into the account, and subject to the same disposition procedure as described herein.
6. Any transfers, sales, mortgages, leases, or assignments that may directly or indirectly exert a negative impact on the safety, quality, reliability, or economy of an APS customer's electric service are ineligible for pre-approval and will require specific applications for Commission approval on a case-by-case basis.
7. The Company shall file semi-annual reports summarizing each transfer, sale, mortgage, lease, or assignment entered into pursuant to this order and further shall state how each transaction complies with condition/limitation (6.) immediately above. This reporting requirement shall be met by continuing the reporting currently being submitted by APS in compliance with Decision No. 60481, as amended by Decision No. 61708, replacing and superseding that requirement. The semi-annual report shall also summarize APS' use of any funds expended for programs to directly benefit customers pursuant to the

condition/limitation (5.) above. These semi-annual reports, "Calculation of Gains on Utility Property," shall be filed with Docket Control on or before March 1 and September 1 of each year.

Transfers, sales, mortgages, leases, or assignments subject to A.R.S. §40-285(A), but not within the above criteria (e.g. over \$750,000 or over \$150,000 after the \$7,500,000 annual accumulation threshold is reached), will continue to require specific applications for approval by the Commission on a case-by-case basis.

Staff recommends that the Commission reserve the option to impute revenues to APS in its next rate case to the extent of any annual net revenue loss resulting from plant or other property sales or other transactions under the pre-approval granted herein.



Ernest G. Johnson
Director
Utilities Division

EGJ:ST:JDA:lhm\JMA

ORIGINATORS: Steve Taylor and Jerry D. Anderson

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BEFORE THE ARIZONA CORPORATION COMMISSION

- MIKE GLEASON
Chairman
- WILLIAM A. MUNDELL
Commissioner
- JEFF HATCH-MILLER
Commissioner
- KRISTIN K. MAYES
Commissioner
- GARY PIERCE
Commissioner

IN THE MATTER OF THE ARIZONA
PUBLIC SERVICE COMPANY'S
APPLICATION FOR AUTHORIZATION TO
(1) ENTER INTO A TRANSFORMER
SHARING AGREEMENT, (2) TRANSFER A
PORTION OF THE ROUND VALLEY
SUBSTATION, (3) TRANSFER THE
WADDELL SUBSTATION, AND (4) FOR
PRE-APPROVAL OF CERTAIN FUTURE
TRANSACTIONS UNDER A.R.S. §40-
285(A).

DOCKET NO. E-01345A-06-0770
DECISION NO. _____
ORDER

Open Meeting
June 26 – June 27, 2007
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Arizona Public Service Company (“APS”) is certificated to provide electric service as a public service corporation in the State of Arizona.
2. On December 8, 2006, APS submitted an application to the Arizona Corporation Commission (“Commission”) for authorization to:
 - I. Enter into an Edison Electric Institute (“EEI”) Spare Transformer Sharing Agreement (“Sharing Agreement”) with other utilities for high voltage and extra high voltage transformers in the event of an act of deliberate destruction.
 - II. Sell a portion of its Round Valley Substation to Southwest Transmission Cooperative.
 - III. Sell its Waddell Substation property to Suburban Land Reserve, Inc. (“SLR”).

1 IV. Pre-approve certain transactions up to \$1 million.

2 I. Transformer Sharing Agreement

3 3. APS desires to enter into a Transformer Sharing Agreement with approximately 50
4 other utilities in the United States and Canada to ensure that critical high voltage (230 kV) and
5 extra high voltage (345 kV and 500 kV) transformers will be available to APS or other affected
6 utilities in the event of an act of deliberate destruction. The benefit to APS and its customers is
7 that transformers would be available to APS to rebuild damaged portions of its transmission
8 system due to an act of deliberate destruction, and the inventory of spares available to APS would
9 be greater in number and lower in cost than APS could obtain as an isolated utility preparing for a
10 similar event. The Sharing Agreement will also require APS to possibly sell or otherwise dispose
11 of or encumber these assets in this program on short notice to other participants, and it is this
12 "selling of these assets" as described in A.R.S. §40-285(A) for which APS is specifically
13 requesting approval.

14 4. APS states that it desires to participate specifically in the 500/230 kV class of
15 transformers utilizing two units it now has available at its Westwing Substation. Also, it is
16 anticipated that APS will join the 345/230 kV class (as soon as a sufficient number of other
17 companies commit to this class) utilizing one unit it now has available at Pinnacle Peak Substation.
18 Additionally, APS expects its participation would soon thereafter extend to the 230/69 kV class
19 based on further review with other utilities and a determination of requirements to participate in
20 this class. The review in the 230/69 kV class is ongoing; however, APS expects its participation
21 would be four 230/69 kV transformers (as updated in APS' March 9, 2007 data response) for
22 which it does have candidate spares and, therefore, it requests the approval to also include these
23 transformers in the Sharing Agreement.

24 5. In total, the Application requests commitment for two 500/230 kV transformers,
25 one 345/230 kV transformer and four 230/69 kV transformers to be included in the Sharing
26 Agreement, and as a condition of that Sharing Agreement, these transformers could then be sold
27 (as defined in A.R.S. §40-285(A)) to other participants in the Sharing Agreement on the required
28

1 short notice. This transaction would then proceed without further Commission approval of the sale
2 of these assets.

3 6. Utilities Division Staff ("Staff") has reviewed the particulars of the Application
4 with regard to the Sharing Agreement and has made the following observations:

- 5 a) APS owns and operates 500 kV, 345 kV and 230 kV stations in Arizona and
6 New Mexico and has an obligation to ensure timely restoration of service in
7 the event of an act of deliberate destruction. The Sharing Agreement
8 addresses acts of deliberate destruction.
- 9 b) The longest manufacturing lead time of transmission components for electric
10 utilities is for 230 kV high voltage and 345 kV and 500 kV extra high voltage
11 transformers (approximately 18 months), and it is therefore necessary for
12 utilities to plan for access to readily available transformers if certain
13 unforeseen events occur.
- 14 c) APS owns or is a participant owner in a sufficient number of spare high
15 voltage and extra high voltage transformers to participate in the Sharing
16 Agreement depending on the level of participation of other utilities in each
17 voltage class. A minimum MVA (million volt-amp, closely equivalent to
18 MW) requirement for each voltage class is set by EEI, and as members
19 commit to that class, the MVA requirement is then divided among the
20 members. As the number of utilities participating in any voltage class
21 increases, the MVA requirement for each participant in that overall class
22 decreases accordingly.
- 23 d) APS has 11 in-service 500/230 kV transformers and four 500/230 kV single
24 phase transformers (two of which are "in service" spares). The capacity of
25 the two spare transformers APS is prepared to commit to this program totals
26 931 MVA. This is insufficient to meet the requirement for joining this class
27 at this time which is 1,029 MVA for the next member (11th) to join. APS
28 would wait until the 13th membership is open as its 931 MVA commitment
would meet the then reduced requirement of 848 MVA.
- e) APS has three in-service 345/230 kV transformers and one 345/230 kV spare
plus one jointly owned spare at Four Corners that could be utilized for local
needs. The capacity of APS' single spare transformer is 600 MVA which is
insufficient to meet the requirement for joining this class at this time. APS
would wait until sufficient membership is achieved such that a 600 MVA
commitment in this voltage class would allow membership.
- f) APS has 48 in-service 230/69 kV transformers and four 230/69 kV spares.
The capacity of these four spare transformers is 486 MVA which is
insufficient to meet the requirement for joining this class at this time. APS
would wait until sufficient membership is achieved such that a 486 MVA
commitment in this voltage class would allow membership.

- 1 g) Acts of deliberate destruction are appropriate events for utilities to prepare
2 for, and the Sharing Agreement provides the necessary inventory to be
3 prepared for this class of event. Additionally, other localized emergencies
4 and/or failures require similar planning and are addressed by individual
5 utilities through maintaining a suitable number of spares on its system and
6 some reliance on other utilities. Both programs, the acts of deliberate
7 destruction and the localized emergency/failure events, may complement each
8 other; i.e., the same transformer may be used in both categories as long as due
9 consideration is given to depletion of the spares inventory for localized use.
- 10 h) Utilities may use their spare units under the acts of deliberate destruction
11 category for any other purpose (for their own routine failed unit needs for
12 example) as long as it or a replacement is restored to the acts of deliberate
13 destruction inventory within 18 months.¹ Additionally, APS has protected its
14 own local emergency needs for all transformers that are or will be included in
15 the Sharing Agreement through a "Permitted Disposition" provision in the
16 Sharing Agreement. This provision provides APS with the discretion to
17 assess their own imminent reliability or other pertinent considerations before
18 proceeding with a transformer sale, and if APS conditions so warrant, APS
19 will maintain that transformer for its own use.
- 20 i) This Sharing Agreement will allow APS to transfer or sell the transformer
21 equipment included in this Application on the very short notice required in
22 emergencies associated with acts of deliberate destruction.
- 23 j) Staff has inspected the two 500/230 kV single phase transformers at
24 Westwing Substation and finds them both to be acceptable inventory for use
25 as may be needed under the acts of deliberate destruction program or other
26 emergency or failure incidents. Staff also finds that the quantity of two
27 500/230 kV single phase transformers requested for the acts of deliberate
28 destruction program is appropriate considering the possible exposure of this
class of transformer on the APS system. It is also noted that APS shares
ownership of these 500/230 kV transformers with Western Area Power
Administration and Salt River Project. These co-owners are in agreement
with the use of these transformers as spares under the acts of deliberate
destruction program. The APS net book values for the respective
transformers are \$201,656 and \$740,004. Both units are presently stored on
site as spares ready for future use as required.
- k) Staff has inspected the single 345/230 kV three-phase transformer at Pinnacle
Peak Substation and finds it to be acceptable inventory for use as may be
needed under the acts of deliberate destruction program or other localized
emergency or failure incidents. Staff also finds that the quantity of one
345/230 kV transformer requested for the acts of deliberate destruction
program is appropriate considering the reduced exposure in number of this

¹ Pg. 23 of July 18, 2006 EEI Spare Transformer Sharing Agreement.

1 class of transformer on the APS system as compared to the 500/230 kV class.
2 It is also noted that APS owns 100 percent of this 345/230 kV transformer and
3 it has a net book value of \$253,536. The unit is presently on site and in
4 service; however, it is to be replaced by June 1, 2007, at which time it would
5 become available as a spare ready for future use as required.

6 l) Staff has not inspected the four 230/69 kV transformers requested in this
7 Application as the study for this requirement is ongoing. The use of 230/69
8 kV transformers on the APS system is widespread and there are multiple
9 available spares to handle previously expected contingencies. It is expected
10 that a requirement of four 230/69 kV transformers will satisfy APS'
11 obligation for this voltage class under the acts of deliberate destruction
12 category and that this commitment can be made from the available spare
13 inventory. It is noted that APS owns 100 percent of all 230/69 kV
14 transformers on its system. The four transformers are booked as inventory
15 and therefore do not carry a net book value. The transformers do carry an
16 inventory value equal to their individual original cost. The two 55 MVA
17 transformers identified as candidates for the Sharing Agreement have
18 inventory values of \$114,654 and \$144,248. The two 188 MVA transformers
19 identified as candidates for the Sharing Agreement have inventory values of
20 \$1,565,450 and \$1,152,150.

21 m) The Sharing Agreement indicates similar utility participation throughout the
22 continental United States.

23 n) Staff recognizes that the transformers identified at this time as candidates for
24 the Sharing Agreement are subject to change over time due to usage by APS,
25 sale to others, failure, retirement, and other possible factors. Participation in a
26 particular voltage class requires commitment of a prescribed total capacity
27 (MVA) of transformers, not specifically identified units. The determining
28 factor for the transformers in the Sharing Agreement for each voltage class is
the minimum MVA required by EEI in that voltage class which is determined
by the total EEI requirement divided by the number of participants. As
participation in the Sharing Agreement increases, the MVA requirement for
each utility to participate decreases.

o) The sale of any transformers under this Sharing Agreement is not intended to
produce a profit for the seller and, therefore, all sales are priced at either the
seller's depreciated book cost or the market price for a replacement
transformer, at the seller's option, plus expenses of the transaction.

7. Staff supports the concepts of the Sharing Agreement and APS' participation in the
program. APS benefits in this program as do other participants by increasing their available stock
of high voltage transformers to restore service following acts of deliberate destruction.
Additionally, the risk of over committing APS system spare transformers in this Sharing

1 Agreement program in lieu of its own emergency needs or unexpected contingencies has been
2 adequately addressed through the "Permitted Disposition" provision of the Sharing Agreement.

3 8. Staff has recommended that the Commission grant APS approval to enter into and
4 participate in the EEI Spare Transformer Sharing Agreement in the 500/230 kV voltage category,
5 the 345/230 kV voltage category, and the 230/69 kV voltage category. Participation will occur
6 after the EEI requirement is decreased to 931 MVA in the 500/230 kV voltage category, 600 MVA
7 in the 345/230 kV voltage category, and 486 MVA in the 230/69 kV voltage category.

8 9. Staff has further recommended that APS be allowed to sell not more than two
9 500/345 kV transformers totaling a maximum of 931 MVA to meet its commitment in the 500/345
10 kV voltage category; not more than one 345/230 kV transformer totaling a maximum of 600 MVA
11 to meet its commitment in the 345/230 kV voltage category; and not more than four 230/69 kV
12 transformers totaling a maximum of 486 MVA to meet its commitment in the 230/69 kV voltage
13 category; all subject to the following condition:

- 14 • The Company should file reports pursuant to this EEI Spare Transformer Sharing
15 Agreement with Docket Control within sixty days of any transaction summarizing
16 each transfer, sale, mortgage, lease, or assignment entered into pursuant to this
17 order.

18

19 **II. Sale of a Portion of Round Valley**

20 10. APS owns and operates the Round Valley Substation in Coconino County, Arizona
21 and provides transmission services to Southwest Transmission Cooperative ("SWTC") utilizing
22 electric facilities in this substation under APS' Open Access Transmission Tariff ("OATT").
23 SWTC serves Mohave Electric Cooperative ("MEC"), one of its distribution cooperatives, through
24 APS' Round Valley Substation's electric facilities. SWTC desires to extricate itself from the cost
25 of this APS transmission service through purchasing the requisite portion of the Round Valley
26 Substation and assuming the associated future operations, maintenance and other obligations of the
27 facility. The sale price of the agreed on 50 percent ownership interest in the facility is \$450,900,
28 and the APS substation would become a joint-use facility with APS and SWTC equally sharing in

1 the ongoing cost of the facility. As a joint use facility, SWTC will no longer be subject to APS'
2 OATT.

3 11. Staff has reviewed the particulars of the Application with regard to the Sale of a
4 Portion of Round Valley Substation and has made the following observations:

- 5 a) The Round Valley Substation presently contains the 230 kV facilities of APS
6 and Western Area Power Administration ("WAPA") with an adjacent 230/69
7 kV facility owned by MEC. The WAPA and MEC facilities are both
8 electrically connected to the APS equipment and operate together; however,
9 the facilities of all three entities are identifiable and distinct except for some
10 minor commonality in the control house which is shared by APS and WAPA.
- 11 b) The APS portion of the Substation is comprised of one 230 kV 1,200 amp oil
12 circuit breaker, three 230 kV air switches, rigid and strain bus, steel support
13 structures, potential devices, control house with relay panels and
14 communication interface, foundations, and various other ancillary devices to
15 support the operation of the facility. The land for the Substation is leased.
16 The APS Substation portion of the yard was placed in service in 1958.
- 17 c) The sale price and percent ownership of a sufficient portion of the APS
18 facility by SWTC to negate the APS OATT was derived through a negotiated
19 settlement of offered and counter-offered sales prices and ongoing obligation
20 costs.
- 21 d) The sale price of 50 percent of the facility at \$450,900 and the division of
22 future obligations, including the land lease (50 percent to APS and 50 percent
23 to SWTC), were derived through the negotiation process between APS and
24 SWTC.
- 25 e) APS would apply the \$450,900 sale price to reduce total depreciation which
26 will benefit APS customers by reducing the rate base correspondingly. Rate
27 base is directly proportional to the utility's net asset value, where net asset
28 value is the original cost of plant less depreciation. In this case, the \$450,900
sale price is credited to Federal Energy Regulatory Commission ("FERC")
Account 108 (accumulated depreciation), thereby increasing the depreciation
account and reducing the rate base.
- f) Also, the 50 percent obligation to SWTC for future operations, maintenance
and land lease cost will benefit APS customers. These benefits to APS
customers will be offset (more or less) by the reduction in transmission tariff
cost no longer received by APS.
- g) SWTC will no longer be required to pay the APS OATT of approximately
\$137,000 annually when the sale is completed. This amount would be
allocated to wholesale (FERC) service for ratemaking purposes and would not
impact retail rates. This annual payment loss was likely inevitable either

1 through litigation or through SWTC completely bypassing the Round Valley
2 Substation, both options of which were under review by SWTC.

3 h) Staff has inspected the facility and determined that APS' representation of the
4 facilities in function is accurate. Additionally, the facilities were in place with
5 consideration for good engineering design and practice. Staff did point out
6 two issues of concern to APS which subsequently were adequately addressed.
7 They were:

- 8 • A spare steel structure approximately 10 feet tall was stored vertically
9 against the active structure supporting the 230 kV bus and ancillary
10 devices. APS reviewed the situation and advised it did not view this as a
11 safety or reliability concern; however, the spare structure was moved away
12 from the active structure and stored horizontally. Staff believes this was
13 the proper action.
- 14 • Oil containment for the three oil filled breakers was lacking. Staff noted
15 this appeared inconsistent with other APS installations and was
16 questionable especially with the downward slope of the substation pad
17 appearing to be well in excess of one percent (thereby exacerbating the
18 flow of oil off the site). APS reviewed this facility and advised that the
19 site was not subject to Spill Prevention, Control and Countermeasure
20 ("SPCC") regulations as promulgated by the Environmental Protection
21 Agency. APS' computer modeling determined there was no environmental
22 impact for an oil leak at this location considering the oil volume available
23 and topography of the area. Staff considers this response acceptable.

12. APS indicated to Staff that the approximate rate paid by SWTC under the original
17 1974 contract was \$30,408 annually. Under the current OATT rate, SWTC pays approximately
18 \$137,000 annually. According to APS, SWTC has considered "building around" the Round
19 Valley Substation to avoid the OATT tariff by installing its own facilities near Round Valley.

21 13. Staff believes such an alternative could be duplicative in nature and would be a
22 higher cost solution to the high OATT rate problem. Staff further believes that SWTC's
23 participation in the Round Valley Substation by purchasing 50 percent of the facility, paying 50
24 percent of the land lease payment, and paying 50 percent of the ongoing costs of the facility would
25 be a lower cost alternative that could be beneficial to Arizona ratepayers.

26 14. Staff therefore supports the sale of 50 percent of the Round Valley Substation to
27 SWTC and a sharing agreement with SWTC to evenly share the ongoing operations of the facility
28 on a 50 percent APS 50 percent SWTC basis.

1 15. Staff has recommended that the Commission grant APS approval to sell 50 percent
2 of the Round Valley Substation to SWTC subject to the following conditions:

- 3 a) The sale price for 50 percent ownership of the substation would be \$450,900
4 and the full sale price would be credited to APS accumulated
5 depreciation/salvage (FERC Account 108).
6 b) APS would enter an Operations and Maintenance Agreement with SWTC for
7 an even cost sharing of future operations, ongoing land lease payments,
8 maintenance, replacements, upgrades and other services in connection with
9 the joint ownership of the substation.

10 **III. Sale of the Waddell Substation**

11 16. APS desires to sell the property it owns at Cotton Lane and Cactus Road in the
12 County of Maricopa and the City of Surprise, Arizona and which presently contains an operational
13 distribution substation known as Waddell Substation. The existing site is subject to reductions in
14 size due to an upcoming road widening, and it is already inadequate to handle the future electric
15 facilities needed in this growing area. It is to be replaced by a new substation at a larger nearby
16 site. Once the new substation is built and energized, APS would then remove the electrical
17 equipment at the Waddell Substation and complete the land transfer to the new owner, Suburban
18 Land Reserve, Inc.

19 17. Staff has reviewed the particulars of the Application with regard to the Sale of
20 Waddell Substation and has made the following observations:

- 21 a) The Waddell Substation has a capacity of 30 MVA and is supplied by one
22 incoming 69 kV feeder and has three outgoing 13 kV feeders. The electrical
23 facilities and land are 100 percent owned by APS.
24 b) The electrical equipment on the site is comprised of two 20 MVA
25 transformers, three 13 kV breakers, various 13 kV and 69 kV air switches,
26 rigid and strain bus, wood structures and steel structures on permanent
27 foundations and temporary supports, equipment foundations, relay and
28 communication interface, and various other ancillary devices to support the
 operation of the facility. The Substation and most of the active equipment are
 in excess of 30 years old with the exception of one 20 MVA transformer and
 associated equipment which are less than 30 years old. The equipment less
 than 30 years old is generally salvageable and suitable for use elsewhere on
 the APS system. The equipment older than 30 years, with the possible
 exception of the 20 MVA transformer, is not generally salvageable.

- 1 c) The Waddell Substation has a relatively small footprint for a substation (107
2 feet by 183 feet), and the site size is being diminished by road widening
3 which will reduce its dimensions to 107 feet by 118 feet. This reduced size of
4 the site is not adequate for the present 30 MW capacity of the station and is
5 not capable of supporting the capacity increases necessary with expected load
6 growth. Staff believes it is appropriate to incorporate the Waddell Substation
7 capacity into a new and expandable nearby facility as APS plans.
- 8 d) The new substation site replacing Waddell Substation is approximately one
9 mile from the Waddell Substation and is well positioned to handle the
10 increasing load of this developing area. It also has a significantly larger
11 footprint (320 feet by 265 feet) to accommodate increased facilities for
12 greater capacity. The new substation site referred to as the "Sarival Site" is
13 being procured by APS from the buyer of the Waddell Substation Site, SLR,
14 and both transactions are contained in the same agreement.
- 15 e) Staff has inspected the facility and determined that APS' representation of the
16 facilities in function is accurate. Additionally, the facilities with the
17 consideration noted below were in place with consideration for good
18 engineering design and practice.
- 19 • Various steel structures supporting insulators, bus, switches and other
20 ancillary devices are mounted on temporary steel plates in lieu of standard
21 concrete foundations. These structures are generally associated with the
22 recent addition of the newer 20 MVA transformer and its associated 69 kV
23 supply and 13 kV outgoing feeder. Considering the short-term nature of
24 this installation, Staff does not object to this type of construction as long as
25 all applicable standards and codes are met.
- 26 f) The sale price for the Waddell Substation site is based on appraised value of
27 similar sites and is approximately \$5.00 per square foot adjusted for this site.
28 Staff has reviewed appraisals provided by APS and concurs with the \$5.00
29 per square foot determination. The resultant sale price of \$63,235 is
30 commensurate with the reduced site size due to road widening (12,626 square
31 feet). The purchase of the new "Sarival Site" from SLR is similarly based
32 upon a purchase price of approximately \$5.00 per square foot.

33 18. Staff is in concurrence with APS' sale of the Waddell Substation site to SLR and
34 the associated procurement of a new site and construction of a new replacement substation in the
35 area.

36 19. Staff has recommended that the Commission grant APS approval to sell to SLR the
37 land containing the Waddell Substation, located at Cotton and Cactus Lane in the Phoenix West
38 Valley, subject to the following conditions:

- 39 a) The sale price of the land for the site would be \$63,235.

- 1 b) The decommissioning of electrical service at Waddell Substation would be
2 coordinated with the construction and commissioning of the new area
3 substation such that no interruptions in customer electric service would occur.
- 4 c) The after tax loss of \$12,691 associated with this transaction would be credited
5 against after tax gains. The net gain/loss on the sale of this asset would be
6 equally shared between ratepayers and shareholders.

7 **IV. Pre-Approval for Qualifying Transactions**

8 20. APS requests pre-approval from the Commission to transfer, sell, mortgage, or
9 lease used and useful property without first securing an order from the Commission authorizing
10 each specific transaction. APS proposes that the pre-approval be subject to certain conditions and
11 limitations:

- 12 a) The transfer price or transaction price for individual transfers, sales,
13 mortgages or leases would be limited to \$1,000,000.
- 14 b) The Company would report information summarizing each transaction
15 entered into under the pre-approval semi-annually.
- 16 c) The net gain on such transfers, sales, or mortgages would be evenly split
17 between APS shareholders and ratepayers with the ratepayer portion to be
18 credited to an account accruing interest at the same rate as customer deposits
19 for use to benefit ratepayers either by a direct refund or by expenditure of the
20 funds for programs to directly benefit ratepayers.

21 21. The requested pre-approval would apply to transfers, sales, leases, or mortgages
22 that are subject to A.R.S. §40-285(A), and not exempt under A.R.S. §40-285(C), and also meet
23 APS' prescribed conditions and limitations; that is, transactions not exceeding \$1,000,000
24 involving used and useful plant and other property. Transactions that fall within the statutory
25 requirements for Commission approval and exceed \$1,000,000 would continue to require specific
26 Commission approval on a case-by-case basis. Sales or other transactions involving property not
27 necessary for the performance of APS' duties to the public would continue to require no
28 Commission approval.

29 22. APS states that the benefits and advantages of the proposed pre-approval include:

- 30 a) Pre-approval will facilitate the Company's ability to respond to changing
31 needs and to maximize efficient use of assets.

- 1 b) Pre-approval will enable the Company to act rapidly to take advantage of
2 opportunities that may not remain available for the time required to obtain
3 specific Commission approval.
- 4 c) Pre-approval should reduce the administrative burden on the Commission and
5 the Company.
- 6 d) Pre-approval should minimize the transaction costs involved in disposing of
7 properties and facilitate the Company's ability to move forward in a timely
8 manner.

9 23. Staff reviewed APS' proposal and investigated the legal, procedural, and economic
10 ramifications of the requested pre-approval. Staff sought information to help it to determine
11 whether Commission pre-approval would satisfy public service corporation obligations under
12 A.R.S. §40-285(A). A.R.S. §40-285(A) requires a public service corporation wishing to sell,
13 lease, assign, mortgage or otherwise dispose of or encumber plant or other property necessary or
14 useful in the performance of its duties to the public, to first obtain an order from the Commission
15 granting it authority to do so.

16 24. In its review, Staff determined that a similar case involving the granting of pre-
17 approval had been ordered when the Commission granted APS pre-approval for qualifying
18 transfers, sales, or mortgages under A.R.S. §40-285(A) in Decision No. 60481, November 25,
19 1997, as amended by Decision No. 61708, May 13, 1999. Pre-approval was granted under these
20 decisions for certain individual transactions not exceeding \$500,000. Additional conditions on the
21 pre-approval granted under these decisions set an annual cap for pre-approved transactions at
22 \$5,000,000 per calendar year, after which all subsequent transactions that year exceeding \$100,000
23 require specific Commission approval. The pre-approval granted in these decisions is still in force,
24 and it appears that it might have been used by APS to meet its statutory obligation to obtain
25 Commission approval for the sales requested in Items II and III of this Application if those
26 decisions had been interpreted broadly. However, interpretations have varied regarding whether
27 the pre-approval granted in Decision No. 60481, as amended by Decision No. 61708, applies only
28 to qualifying street lighting equipment or if it applies generally to all types of plant and other used
29 and useful property.

1 25. In discussions with Staff, APS stated that it included Item IV in its Application to
2 obtain an order from the Commission granting the Company pre-approval authority for all types of
3 qualifying plant and other property, not just street lighting plant and equipment. APS is also
4 proposing to increase the cap on individual qualifying transactions from \$500,000 to \$1,000,000.

5 26. It is not anticipated that a high volume of sales or other transactions would take
6 place under APS' proposed pre-approval, if granted. Indeed, only 12 transactions were completed
7 under the pre-approval granted in Decision No. 60481 from November 1997 to date, and all but
8 two of those transactions were for the sale of streetlighting systems. Other than the items in the
9 instant Application, APS has made only one other individual request for approval for sale of used
10 and useful property in the past five years. Transactions that may qualify for the requested pre-
11 approval often involve the sale of smaller outgrown facilities to move to larger facilities and may
12 include the following, for example:

- 13 • Sale of a service center building and land parcel
- 14 • Sale of a communications site
- 15 • Sale of a small portion of a transmission line
- Sale of a pole yard or other work or storage site

16 27. The Company is proposing to utilize *some of the same procedures and accounts* that
17 were used to implement Decision No. 60481 and its amendments in Decision No. 61708
18 (Application p. 6, items b and c). After reviewing APS' pre-approval request, Staff views it as a
19 request to gain pre-approval for transactions involving all types of qualifying used and useful plant
20 and equipment and to raise the individual transaction cap to \$1,000,000.

21 28. Staff agrees that it could be advantageous to grant APS pre-approval for certain
22 smaller qualifying transactions. Indeed, in a rapidly growing service territory, APS must be able to
23 respond to changing needs and to take advantage of opportunities quickly, efficiently, and
24 economically. The Item III Waddell Substation scenario, for example, is likely to recur in the
25 future. This is a situation where a small rural substation is no longer of adequate capacity to serve
26 an area that has transformed from farm land into a developed residential/commercial area. Staff
27 recognizes that pre-approval could help to minimize transaction costs involved in disposing of
28 some smaller properties and facilities and could therefore save ratepayers money. Staff also

1 believes that pre-approval could reduce administrative burden on the Commission and allow the
2 Commission to expend its time on more substantive issues. Staff is currently not aware of any
3 disadvantages to allowing some form of pre-approval for many smaller transactions.

4 29. Staff examined the terms and conditions of the pre-approval granted in Decision
5 No. 60481, as amended by Decision No. 61708, and found them to contain some appropriate
6 safeguards and procedures to ensure that implementation of the pre-approval was reasonable, fair,
7 and efficient. Staff examined the \$500,000 individual transaction limitation for pre-approval
8 imposed in 1997 and considers that it was reasonable at that time. Staff applied various inflation
9 indices to the \$500,000 individual transaction cap in 1997 and found that a limit in the range of
10 \$600,000 - \$800,000 would be the equivalent level today. Staff similarly reviewed the inflation
11 effect on the \$5,000,000 existing annual cap and the lower \$100,000 individual transaction cap
12 that becomes effective after the annual maximum is reached in a calendar year. Staff believes that
13 additional benefits would accrue to ratepayers, the Commission, and the Company if pre-approval
14 were allowed to apply to qualifying transactions involving other types of used and useful plant and
15 property in addition to street lighting.² However, because the pre-approval would apply to a
16 broader array of used and useful assets, Staff believes that additional conditions on such pre-
17 approval would be appropriate.

18 30. Staff has recommended that the Commission grant APS pre-approval to transfer,
19 sell, mortgage, lease, assign, or otherwise dispose of or encumber, in whole or in part, tangible or
20 intangible property otherwise subject to A.R.S. §40-285(A) (used and useful property), and not
21 exempt under A.R.S. §40-285(C) (property other than used and useful), subject to the following
22 conditions and limitations:

- 23 a) Individual transfers, sales, mortgages, leases, or assignments shall not exceed
24 a per transaction cap of \$750,000.
- 25 b) Logical transactions shall not be disaggregated into separate component
26 transactions for the purpose of allowing them to fall under the \$750,000 cap.

27 _____
28 ² The present benefits are derived from APS and customer shared transactions and held in account generally with a
balance less than \$100,000 until a Commission approved disbursement.

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- c) The cumulative amount of such transfers, sales, mortgages, leases, or assignments shall not exceed \$7,500,000 in any single year except as provided for in condition/limitation (4.) immediately following.

- d) Once the \$7,500,000 accumulation threshold is reached in any calendar year, all subsequent qualifying transactions exceeding \$150,000 during the remainder of the year would require specific Commission approval.

- e) Fifty percent of the net gain on pre-approved transfers, sales, mortgages, leases, or assignments shall be credited to APS ratepayers by placing the ratepayers' portion of the gain in a separate account that accrues interest at the same rate as customer deposits. The account to be utilized in compliance with this order shall be the same account currently utilized for compliance with Decision No. 60481 as amended by Decision No. 61708. This account has generally maintained balances less than \$100,000 over the last four years. No less often than once each two years on April 30 of even numbered years, the entire amount in the account, if \$100,000 or greater, will be either refunded to customers or utilized by APS to fund programs that will directly benefit customers as directed and approved by the Commission. However, should the amount in the account reach \$1.5 million earlier than six months prior to an April 30 disbursement date, disbursement of the entire amount in the account, in the manner described above, shall be undertaken as soon as is practicable. Customers receiving service under special contracts will not be eligible to receive such refunds. Any funds currently in the account as a result of Decision No. 60481, as amended by Decision No. 61708, shall be carried over, added to any future funds placed into the account, and subject to the same disposition procedure as described herein.

- f) Any transfers, sales, mortgages, leases, or assignments that may directly or indirectly exert a negative impact on the safety, quality, reliability, or economy of an APS customer's electric service are ineligible for pre-approval and will require specific applications for Commission approval on a case-by-case basis.

- g) The Company shall file semi-annual reports summarizing each transfer, sale, mortgage, lease, or assignment entered into pursuant to this order and further shall state how each transaction complies with condition/limitation (6.) immediately above. This reporting requirement shall be met by continuing the reporting currently being submitted by APS in compliance with Decision No. 60481, as amended by Decision No. 61708, replacing and superseding that requirement. The semi-annual report shall also summarize APS' use of any funds expended for programs to directly benefit customers pursuant to the condition/limitation (5.) above. These semi-annual reports, "Calculation of Gains on Utility Property," shall be filed with Docket Control on or before March 1 and September 1 of each year.

1 than four 230/69 kV transformers totaling a maximum of 486 MVA to meet its commitment in the
2 230/69 kV voltage category; all subject to the following condition:

3 Arizona Public Service Company shall file reports pursuant to this EEI Spare
4 Transformer Sharing Agreement with Docket Control within sixty days of any
5 transaction summarizing each transfer, sale, mortgage, lease, or assignment entered
6 into pursuant to this order.

7 IT IS FURTHER ORDERED that approval to sell 50 percent of the Round Valley
8 Substation to SWTC is hereby granted, subject to the following conditions:

- 9 a) The sale price for 50 percent ownership of the substation shall be \$450,900
10 and the full sale price shall be credited to Arizona Public Service Company
11 accumulated depreciation/salvage (FERC Account 108).
12 b) Arizona Public Service Company shall enter an Operations and Maintenance
13 Agreement with SWTC for an even cost sharing of future operations, ongoing
14 land lease payments, maintenance, replacements, upgrades and other services
15 in connection with the joint ownership of the substation.

16 IT IS FURTHER ORDERED that approval for Arizona Public Service Company to sell to
17 SLR the land containing the Waddell Substation, located at Cotton and Cactus Lane in the Phoenix
18 West Valley, is hereby granted, subject to the following conditions:

- 19 a) The sale price of the land for the site shall be \$63,235.
20 b) The decommissioning of electrical service at Waddell Substation shall be
21 coordinated with the construction and commissioning of the new area
22 substation such that no unreasonable interruptions in customer electric service
23 will occur.
24 c) The after tax loss of \$12,691 associated with this transaction shall be credited
25 against after tax gains. The net gain/loss on the sale of this asset shall be
26 equally shared between ratepayers and shareholders.

27 IT IS FURTHER ORDERED that pre-approval for Arizona Public Service Company to
28 transfer, sell, mortgage, lease, assign, or otherwise dispose of or encumber, in whole or in part,
tangible or intangible property otherwise subject to A.R.S. §40-285(A) (used and useful property),
and not exempt under A.R.S. §40-285(C) (property other than used and useful), is hereby granted,
subject to the following conditions and limitations:

- 1 a) Individual transfers, sales, mortgages, leases, or assignments shall not exceed
2 a per transaction cap of \$750,000.
- 3 b) Logical transactions shall not be disaggregated into separate component
4 transactions for the purpose of allowing them to fall under the \$750,000 cap.
- 5 c) The cumulative amount of such transfers, sales, mortgages, leases, or
6 assignments shall not exceed \$7,500,000 in any single year except as
7 provided for in condition/limitation (d.) immediately following.
- 8 d) Once the \$7,500,000 accumulation threshold is reached in any calendar year,
9 all subsequent qualifying transactions exceeding \$150,000 during the
10 remainder of the year would require specific Commission approval.
- 11 e) Fifty percent of the net gain on pre-approved transfers, sales, mortgages,
12 leases, or assignments shall be credited to APS ratepayers by placing the
13 ratepayers' portion of the gain in a separate account that accrues interest at the
14 same rate as customer deposits. The account to be utilized in compliance with
15 this order shall be the same account currently utilized for compliance with
16 Decision No. 60481 as amended by Decision No. 61708. No less often than
17 once each two years on April 30 of even numbered years, the entire amount in
18 the account, if \$100,000 or greater, will be either refunded to customers or
19 utilized by APS to fund programs that will directly benefit customers as
20 directed and approved by the Commission. However, should the amount in
21 the account reach \$1.5 million earlier than six months prior to an April 30
22 disbursement date, disbursement of the entire amount in the account, in the
23 manner described above, shall be undertaken as soon as is practicable.
24 Customers receiving service under special contracts will not be eligible to
25 receive such refunds. Any funds currently in the account as a result of
26 Decision No. 60481, as amended by Decision No. 61708, shall be carried
27 over, added to any future funds placed into the account, and subject to the
28 same disposition procedure as described herein.
- f) Any transfers, sales, mortgages, leases, or assignments that may directly or
indirectly exert a negative impact on the safety, quality, reliability, or
economy of an APS customer's electric service are ineligible for pre-approval
and will require specific applications for Commission approval on a case-by-
case basis.
- g) The Company shall file semi-annual reports summarizing each transfer, sale,
mortgage, lease, or assignment entered into pursuant to this order and further
shall state how each transaction complies with condition/limitation (f.)
immediately above. This reporting requirement shall be met by continuing
the reporting currently being submitted by APS in compliance with Decision
No. 60481, as amended by Decision No. 61708, replacing and superseding
that requirement. The semi-annual report shall also summarize APS' use of
any funds expended for programs to directly benefit customers pursuant to the
condition/limitation (5.) above. These semi-annual reports, "Calculation of

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Gains on Utility Property,” shall be filed with Docket Control on or before March 1 and September 1 of each year.

IT IS FURTHER ORDERED that the Commission shall reserve the option to impute revenues to Arizona Public Service Company in its next rate case to the extent of any annual net revenue loss resulting from plant or other property sales or other transactions under the pre-approval granted herein.

IT IS FURTHER ORDERED that this Order shall not bind the Commission to any particular rate making treatment of a transaction that qualifies for pre-approval.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive Director of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this _____ day of _____, 2007.

BRIAN C. McNEIL
Executive Director

DISSENT: _____

DISSENT: _____

EGJ:ST:JDA:lhm\JMA

1 SERVICE LIST FOR: Arizona Public Service Company
DOCKET NO. E-01345A-06-0770

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4 Snell & Wilmer
5 One Arizona Center
6 400 East Van Buren
7 Phoenix, AZ 85004-2202

8 Mr. Thomas L. Mumaw
9 Pinnacle West Capital Corporation
10 Post Office Box 53999, MS 8695
11 Phoenix, Arizona 85072-3999

12 Mr. Ernest G. Johnson
13 Director, Utilities Division
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15 1200 West Washington
16 Phoenix, Arizona 85007

17 Mr. Christopher C. Kempley
18 Chief Counsel
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