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Arizona Corporation Commission  
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Docket Control  
Arizona Corporation Commission  
1200 W. Washington  
Phoenix, AZ 85007

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Re: *Electric Cooperative Comments on Competitive Procurement Issues;*  
*Docket No. E-00000E-05-0431*

Dear Sir/Madam:

Enclosed are the original and 13 copies of Comments of the Arizona Electric Power Cooperative and Southwest Transmission Cooperative concerning Competitive Procurement Issues in this docket. Your assistance is appreciated.

Very truly yours,

GALLAGHER & KENNEDY, P.A.

By:

Michael M. Grant

MMG/plp  
10421-42/1558954  
Enclosures

cc (w/enclosures): Barbara Keene, Utilities Division (delivered)  
Bing Young, Utilities Division (delivered)

**Original and 13 copies** filed with Docket  
Control this 17<sup>th</sup> day of May, 2007.

**ELECTRIC COOPERATIVE COMMENTS  
IN THE MATTER OF THE GENERIC INVESTIGATION INTO ELECTRIC  
RESOURCE PLANNING  
(DOCKET NO. E-00000E-05-0431)  
DATED MAY 17, 2007**

**Introduction**

On April 25, 2007, the Arizona Corporation Commission ("Commission") Staff held the first Resource Planning Workshop on Competitive Procurement Issues only. The Staff and participants attending this Workshop developed a list of issues to be addressed in future Workshops. The participants agreed to file written comments on these issues in the Generic Resource Planning docket (Docket No. E-00000E-05-0431).

The following comments on these issues are provided by Arizona Electric Power Cooperative, Inc. ("AEPSCO") and Southwest Transmission Cooperative ("SWTC") (collectively, "Cooperatives") which provide power and energy and transmission service, respectively, to AEPSCO's member distribution cooperatives.

The Cooperatives, as well as Duncan Valley Electric Cooperative, Inc. ("Duncan"), Graham County Electric Cooperative, Inc. ("Graham"), Mohave Electric Cooperative, Inc. ("Mohave"), Navopache Electric Cooperative, Inc. ("Navopache"), Trico Electric Cooperative, Inc. ("Trico") and Sulphur Springs Valley Electric Cooperative, Inc. ("Sulphur") (collectively, "Distribution Cooperatives"), reserve the right, individually and collectively, to provide additional or different comments and positions on any of these and other issues as becomes necessary in the future. The Cooperatives, individually and collectively, also reserve the right to change the opinions expressed as new information becomes available.

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1. **Whether the Commission should go through a formal Rulemaking to formalize procurement procedures**

*Cooperatives' Response: Most Arizona cooperatives, including AEPCO, are Rural Utilities Services ("RUS") borrowers and are already subject to detailed RUS procedures on this subject as specified in the Code of Federal Regulations ("CFR") (generally, 7 CFR § 1710, et seq.). RUS requires that any self-build generation plan be justified against a competitive procurement of purchased power through a RUS-monitored process. These procedures assure a high level of transparency when procuring power. For example, loan applicants are required, by RUS regulation, to solicit proposals from all reasonable potential sources of power, including other Cooperatives, investor-owned utilities, municipal utility organizations, federal and state power authorities, independent power producers and co-generators. Solicitations for proposals are required to be published in at least three national publications in addition to direct contact. The applicant is also required to inform RUS of progress in the solicitation as negotiations progress. Final plans must include sufficient detail to show that present-value analyses of alternatives and their effects on total power costs over the forecast period result in the most economical and effective means of meeting the cooperative's power requirements.*

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*The Cooperatives do not believe that any additional rules are necessary on this subject because the Cooperatives are already subject to these RUS procurement and oversight procedures. See also the responses to Issue Nos. 16 and 17.*

- 2. What types of generation, purchase power, or fuel resources should be subject to formalized procurement procedures**

*Cooperatives' Response: AEPCO follows the procurement processes mandated by the CFRs and summarized in the response to Issue No. 1 for evaluation of all potential resource alternatives in every resource expansion cycle.*

- 3. Whether or not an Independent Evaluator should be required as part of the process, and if so, the Independent Evaluator's role in the process**

*Cooperatives' Response: An independent evaluator should not be required. As mentioned in the response to Issue No. 1, RUS not only acts as an independent evaluator but also specifies open and transparent processes for competitive procurement. An additional independent evaluator would be duplicative of safeguards already in place, would increase the required lead-time for project approval and would increase costs without providing additional benefit for the Cooperatives. Finally, in the event of a conflict between an independent evaluator and RUS, the Cooperatives' mortgage documents and CFRs require the Cooperative to award bids consistent with RUS' evaluation.*

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**4. Any required protocols for the utility self-build or affiliate bid and build options**

*Cooperatives' Response:* The protocols specified by RUS are described in the response to Issue No. 1 and are set forth in 7 CFR § 1710, et seq.

**5. Involvement of ACC**

*Cooperatives' Response:* Given the extensive procurement procedures required by federal regulations, the Cooperatives feel that direct ACC involvement is not necessary. However, information concerning any particular procurement could be supplied upon request.

**6. The design, mechanics, and timing of the RFP, including evaluation criteria to be used**

*Cooperatives' Response:* The Cooperatives follow all of the CFR procurement procedures, including evaluation criteria described in prior responses.

**7. The interaction of a formalized procurement process with a utility which is presently subject to a building moratorium**

*Cooperatives' Response:* The Cooperatives do not have an opinion on this subject at the present time.

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**8. Protocols for the process of evaluating RFPs that insure integrity of the process**

*Cooperatives' Response:* As described in the response to Issue No. 1, the CFRs specify that final plans over the forecast period must demonstrate that present-value analyses result in the most economical and effective means of meeting the Cooperatives' power requirements. This and other measures are applied in the formulation, bidding and evaluation stages to assure process integrity.

**9. How confidential and trade secret information provided by bidders should be handled**

*Cooperatives' Response:* Confidentiality of certain information received in the process will be necessary and should be allowed, i.e., price and unique terms and conditions of bidders.

**10. Whether and to what extent there should be bid fees, or other prequalification requirements for bidders**

*Cooperatives' Response:* Bid fees may be appropriate in certain contexts, but are not currently used by AEPCO. 7 CFR § 1710.254(d) states that reliability or service, the short-term and long-term financial viability of a supplier and the financial risk to the cooperative and its creditors should be considered in the evaluation process.

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**11. The treatment of “non-conforming” proposals**

*Cooperatives’ Response:* The Cooperatives’ practice has been to ask specific questions of suppliers who provide “non-conforming” proposals during the solicitation bidding and evaluation period in an attempt to bring any non-conforming proposals into conformance. If the Cooperatives are not able to bring non-conforming proposals into conformance through this process, they are rejected.

**12. What to do about bids received outside the RFP process**

*Cooperatives’ Response:* The Cooperatives’ practice has been to consider any valid offers, even those submitted after a deadline, provided that there is time to analyze, model, clarify and negotiate the proposal. The Cooperatives, however, reserve the right to reject any bids that are non-conforming or that are non-responsive.

**13. How to handle demand-side management and renewables proposals and the evaluation criteria for each to insure that the value of each is fairly reflected**

*Cooperatives’ Response:* AEPCO recently completed an RFP for renewable resources in relation to amendments to its Environmental Portfolio Standard (“EPS”) Plan and proposed REST Plan. Loans for Demand-Side Management and Renewable Energy facilities, both on- and off-grid, are required to be supported by a RUS-approved integrated resource plan that includes benefits and costs of all supply and demand-side options. (7 CFR §§ 351 and 353.) Necessary features for system operation such as

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*diversity, reliability, dispatchability and other risk factors must also be addressed. The ability to verify energy and cost savings achieved through DSM, energy conservation and renewable energy systems must be included and the durability of such savings measured over time must be evaluated in the process. Finally, RUS requires that renewable energy and DSM systems must utilize technologies that are proven and commercially available. The Cooperatives believe that the DSM programs should be designed, implemented and reported at the distribution cooperative level. Consistent with that position, 7 CFR § 1710.353(c) provides that DSM is a distribution loan purpose.*

- 14. Relationship to the IRP process whether the procurement process should be tailored to interact with a utility's integrated resource plan, should the Commission begin to require the filing of such plans**

*Cooperatives' Response: The Cooperatives believe that the competitive procurement process is a portion of the overall IRP process and should be tailored to interact with a utility's IRP. As previously stated in comments filed in this docket, the Cooperatives do not believe the Commission should reinstitute the filing of such IRP plans.*

- 15. The adoption of "Codes of Conduct" and "Best Practices" procedures by the utility**

*Cooperatives' Response: AEPCO, Southwest Transmission Cooperative and Sierra Southwest Cooperative Services currently have a Commission-approved Code of*

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*Conduct. The Cooperatives believe the processes they have outlined here and follow as required by RUS and the CFRs are a rigorous and comprehensive set of best practices.*

**16. What waivers or exceptions to this process should be adopted**

*Cooperatives' Response: Cooperatives are non-profit entities whose mission is to provide electric service at the lowest cost to their member/owners. Because the customers of the cooperative are also its owners and there is no profit incentive, conflict of interest concerns associated with the Cooperatives' competitive procurement are greatly reduced. As described in prior responses, RUS/CFR-mandated planning and competitive procurement procedures must be followed. Finally, as discussed in the response to Issue No. 17, the Cooperatives are facing a variety of challenges unique to smaller entities in the competitive procurement market.*

*For these reasons, the Cooperatives do not believe additional guidelines or rules are necessary or appropriate.*

*To summarize, for each application for loan funds AEPCO makes to RUS to support construction of new generating facilities, AEPCO must conduct a thorough Power Cost Study. This study must include comprehensive economic present-value analyses of the costs and revenues of available self-generation, load management, energy conservation, availability of competitively priced purchased power, financial viability of the purchased*

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*power supplier(s), assessments of service reliability and financing requirements and risks. These studies must also consider alternative unit types and sizes, fuel alternatives, system stability, impacts on the interconnected transmission system and system dispatch.*

*Loan applicants are required, by RUS regulation, to solicit proposals from all reasonable potential sources of power. The applicant is also required to inform RUS of progress in the solicitation as negotiations progress. Final plans must show that present-value analyses of alternatives and their effects on total power costs over the forecast period result in the most economical and effective means of meeting the Cooperatives' power requirements.*

**17. Other issues related to competitive procurement**

*Cooperatives' Response: AEPCO has recently joined with other cooperatives, electric irrigation and power districts, municipalities and tribal utilities to form the Southwest Public Power Resources ("SPPR") Group. SPPR Group has been formed as a result of the lessons learned in the past and in reaction to the current procurement market. The lessons learned in the past include:*

- *Deregulation occurred in the wholesale market but not the retail market*
- *The Energy Policy Act, FERC jurisdiction, marketers and other forces have had major impacts on the electric utility industry*

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- *Diversified resources are important for continued existence and financial health*
- *Joint planning efforts spread the risk of variable load growth*

*The goals of a Joint Project that will be undertaken by SPPR are as follows:*

- *Size resources to serve the combined load of the SPPR Group participants to gain economies of scale*
- *Spread risk among multiple participants*
- *Include purchased power agreements and unit ownership in the resource mix*

*SPPR Group has recently issued an RFP for purchased power on the open market, is in the process of evaluating proposals and has the following comments on this process.*

*SPPR Group members are facing several key challenges in the competitive procurement process. Traditional vertically integrated utilities are now in the minority when it comes to selling power into the deregulated wholesale market. Wall Street bankers and investment firms (“WSBs”) are the predominant parties in the wholesale power markets and smaller utilities are forced to entertain agreements with terms and conditions “typical” of standard commodity contracts.*

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*In order to purchase power on the open market, WSBs are requiring commodity contracts that have troublesome provisions for electric utilities, including the Cooperatives. Electricity is not a "typical" commodity; it needs to be available immediately when demanded and is not easily stored. WSB commodity contracts, however, treat electricity as if it were a commodity, and WSB commodity "firm" contracts have provisions that state if the power is not delivered they will pay liquidated damages. This is inherently problematic for utilities who are accustomed to dealing with truly firm contracts, contracts which become a cornerstone of the reliability. Commodity contracts with liquidated damages result in a utility having to seek a back-up supplier or plan other arrangements in case a WSB is unable to deliver.*

*WSB commodity contracts also require collateral to be provided when the price included in the contract exceeds the current market price. Providing this collateral can be a very large financial obligation and presents risks that are difficult to manage and which could undercut the reliability of the electric grid. In addition, as the market price decreases below the contract price, WSB contracts define this event as a default which has negative financial and legal consequences.*

*Further, WSBs are not interested in small power contracts. The minimum contract size is 25 MW blocks which is very high when considering the loads and demands of the*

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*Cooperatives and many of the SPPR Group members. SPPR Group was created in part to address this large minimum contract provision that would have precluded smaller utilities from buying power in the wholesale market.*

*Finally, WSBs are used to dealing with rated companies. Most electric cooperatives and the vast majority of the SPPR Group membership are not rated and do not want nor generally need to spend the significant amount of personnel resources and funds necessary to be rated. Rating requires an increase in accounting and bookkeeping requirements, along with quarterly financials.*

*In conclusion, SPPR Group was formed to address some of these issues. The effects of the current marketplace on electric cooperatives and smaller utilities may lead to further aggregation of electric cooperatives and smaller utilities to overcome these competitive procurement challenges. The Cooperatives should continue to have the opportunity to solicit or act in concert with other jurisdictional or non-jurisdictional utilities in joint plant or transmission projects subject to the RUS rules and requirements.*