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May 29, 2007

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

RE: Arizona Public Service Company's Initial Comments
Integrated Resource Planning Workshop
DOCKET NO. E00000E-05-0431

Dear Madam or Sir:

Arizona Public Service Company ("APS" or "Company") is providing the attached document in response to a request for written comments contained in the Arizona Corporation Commission ("Commission") Staff's April 26, 2007 Meeting Notice pertaining to the Commission's Resource Planning Workshops.

Staff's request for comments posed numerous questions about specific, detailed issues that might arise during a utility's resource planning process. APS looks forward to discussing these topics with parties'. However, the company believes, at this stage, the parties' discussions will be most productive if they focus on the conceptual framework for what that process should entail, rather than addressing detailed technical issues. For that reason, the attached Response provides APS's initial comments on the broad, conceptual issues identified by Staff. Additional input on the more specific items will be provided throughout the workshops as the issues are developed.

APS appreciates the opportunity to work with Staff and the interested parties to address both resource planning and competitive procurement issues, and looks forward to on-going participation in these workshops.

If you or your staff have any questions regarding the enclosed information please call me.

Sincerely,

Barbara Klemstine

BAK/scc

Attachments

Arizona Corporation Commission
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**Arizona Public Service Company
Initial Comments Regarding
Integrated Resource Planning Approval Process
Docket No. E-0000E-05-0431**

Introduction

On April 26, 2007, the Utilities Director of the Arizona Corporation Commission (“Commission”) issued a Request for Meeting Notice (“Request”) that scheduled workshops to address issues related to resource planning (other than competitive procurement issues). The Request also set forth a considerable number of questions that address various aspects of utility resource planning and the Integrated Resource Planning approval process (“IRP Approval Process”), and requested written comments from interested parties related to those issues.

Because the Commission’s examination of an IRP Approval Process is in its initial stages, Arizona Public Service Company (“APS” or “Company”) believes that, at this point in the process, the parties will be best served by focusing on the high level objectives and goals of resource planning, generating a framework and process that provides for open discussion and that facilitates the utility’s ability to move forward with critical resource decisions, rather than focusing on the detailed technical issues associated with IRP analysis. Once that general process is in place, the parties will be better situated to discuss the specific detailed elements involved. For these reasons, the Company’s response is a global overview of resource planning and a proposed approach to an IRP Approval Process. However, the Company believes that all interested parties should be able to provide additional written comments regarding specific issues as the workshop process progresses.

Overview of the Company’s Position

APS believes that the fundamental goal of resource planning should be to provide reliable service to our customers at the lowest cost, while balancing the overall risks of the resource portfolio and complying with applicable federal and state requirements. The purpose of the Commission’s workshops should be to facilitate the achievement of this overall goal by developing a resource planning process that assures regulatory certainty by: 1) providing a clear standard for evaluating a company’s resource plan; and 2) providing a forum to review and approve a company’s action plans in a timely manner that would assure full and timely cost recovery.

A review of resource planning and procurement in other states provides some perspective. Nevada has established a robust resource planning process that

provides for open discussion on resource options, clarity on resource preferences, and a defined action plan¹. The Nevada approach emphasizes risk management and portfolio management. Due to its rapid growth, nature of its load and desert climate conditions, Nevada is perhaps the state most similar to Arizona. The Company believes that the Nevada plan could serve as a pertinent and relevant reference in developing a regulatory resource planning process for Arizona.

The Company believes that the Commission's existing IRP rules are outdated and that new rules should be promulgated. The Commission's current Resource Planning rules² are obsolete in today's competitive electric market, which was the reason many of those regulations have been suspended by the Commission for almost a decade³. A fundamental deficiency of the current rules is that the outcome of the proceedings under those rules is a vague "consistency determination" – a finding that provides neither the utility, market participants, nor the financial community with any assurance that a procurement made pursuant to that IRP will be found "prudent" such that the utility will recover its related costs. In addition, the current rules do not include any timelines for Commission review of resource plans, which further contributes to the resulting regulatory uncertainty. Accordingly, the current rules entail a significant risk that the utility will not be able to meet the resource needs of its customers in a timely manner and secure the capital needed to acquire the additional resources necessary to meet its customer needs and to provide an adequate and reliable power supply.

Responses to Staff's Specific Questions

As previously stated, APS believes that at this stage, discussions regarding the IRP Approval Process will be most productive if they focus on the conceptual framework of the process, rather than honing in on discrete technical issues. APS is providing initial comments on issues related to the framework as identified by Staff.

- Q. What should be the primary objectives of a resource planning process?
- A. The primary objective of the resource plan is to identify the preferred resources that will be needed to meet anticipated customer needs in a reliable and cost effective manner. The resource planning process must consider risks and uncertainties. It must also include effective communications with the Commission and other key

¹ See, Nevada Revised Statutes, NRS 704.741, 704.746, and 704.751.

² A.A.C. R14-2-701 *et. seq.*

³ See, *In the Matter of the A.A.C. R14-2-704 Hearing for Resource Planning*, Docket No. E-00000A-95-0506, 1999.

stakeholders in order to develop agreement on appropriate actions. Agreement with the Commission should provide regulatory support and certainty related to the discretion utilities have in their implementation, timing for specific approvals, and ultimately full and timely cost recovery.

Q. To what extent, if any, should a Commission decision "accepting" or "approving" a plan (or part of a plan) be regarded as a finding of "prudence" in subsequent rate cases?

A. The Commission's approval of a utility's resource plan should be a determination that a resource decision made pursuant to the action plan (including a decision to expend funds to preserve the resource options described in the action plan) is prudent. A prudence determination of this kind is vital to achieving regulatory support and certainty for full and timely recovery, a principle which is itself critical to a utility's ability to meet its customers' needs.

Q. What time limits, if any, should apply to the Commission's processing of a resource plan?

A. It is extremely important to the effective functioning of a utility's resource planning that the IRP approval process be expeditious, with precise time limits established so that the utility may proceed with all that is entailed in assessing and acquiring resources pursuant to that Plan with confidence (and be able to instill that level of confidence in others in the market and the financial community). For those reasons, APS believes that a resource plan should be reviewed and approved within 180 days.

Q. How frequently should a utility be required to file a resource plan?

A. The frequency of the resource plan filing depends upon the details of the filing and most importantly the associated action plan. However, APS believes it would be reasonable to file a resource plan every three years.

Q. How can a resource planning process be developed that takes into account changes that occur between filings?

A. Along with its resource plan, each utility should file and receive Commission approval for an action plan that identifies steps it will take to develop or procure the necessary resources over the next

several years. Rather than identifying only discrete projects or resources, the action plan should provide the utility with a defined amount of latitude to pursue specified resources within a certain range (e.g., 100 MW of renewable generation, 10 MW of DSM, and 200 MW of peaking generation). This approach provides sufficient clarity to ensure that portfolio resource strategies are pursued and enables the utility to manage the risks associated with procurement in an efficient manner.

Q. Should resource plans include a short term "action plan" (such as the time between filings of resource plans) in which utilities could obtain more direct Commission direction and/or approval for certain critical items that must be decided in the short term?

A. Generally, yes, with some clarification. A utility's IRP sets forth a conceptual framework, outlining the variety of resource options available to the utility over the long term and identifying and evaluating the risks and uncertainties involved in exercising one option over another in the years ahead. The Company anticipates that an "action plan" should be approved by the Commission as part of the IRP process. The action plan would cover steps the utility would need to take in subsequent years in order to effectuate the desired outcome. The action plan should identify targeted types of resources (e.g., a certain amount of renewable generation, DSM, or peaking capacity), and provide definition regarding the discretion available to the utility in pursuing the acquisition of the desired resources. The action plan may also include larger discrete projects. Expenditures and decisions made pursuant to an approved action plan would be determined to be prudent. This determination would be used in subsequent rate proceedings.

Q. What role should DSM play in the resource planning process?

A. Demand Side Management activities include energy efficiency measures, as well as demand response programs, which each have different characteristics, benefits, risks, and costs. With that in mind, APS believes that DSM should be considered in the IRP process and evaluated by the utility in the same manner as other resource alternatives (with specific consideration of unique resource characteristics, as well as risk reduction benefits). In general, the IRP process should evaluate the full range of available resource options and develop a comprehensive action plan that includes all resource acquisition.

- Q. How should risk management be factored into the decision making process?
- A. Risk management is a key part of a utility's resource planning process. An understanding of the potential risks associated with a decision, an evaluation of the possible future outcomes, and an analysis of how to manage the risks inherent in the utility's resource portfolio (which can include, among others, commodity, technology, financing, or legislative risks), should be factors the utility considers when developing its IRP. The approved action plan must consider the anticipated risks, and should include a definition of the latitude available to the utility so that parties understand how utilities will move forward and manage the risk.

Conclusion

Resource planning is fundamental to managing the risks associated with providing reliable electric service at reasonable costs to customers. The Company appreciates the opportunity to participate in the Commission's workshops and discussions on these important issues and is prepared to fully address specific detailed elements as these discrete issues are taken up. APS believes that this process should result in a clear standard for evaluation of a resource plan, support the establishment of effective action plans, and provide a timely review and approval process that assures cost recovery.