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BEFORE THE ARIZONA CORPORATION COMMISSION

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

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AZ CORP COMMISSION  
DOCKET CONTROL

IN THE MATTER OF THE FILING BY TUCSON )  
ELECTRIC POWER COMPANY TO AMEND )  
DECISION NO. 62103. )

DOCKET NO. E-01933A-05-0650

IN THE MATTER OF THE APPLICATION OF )  
TUCSON ELECTRIC POWER COMPANY FOR )  
THE ESTABLISHMENT OF JUST AND )  
REASONABLE RATES AND CHARGES )  
DESIGNED TO REALIZE A REASONABLE )  
RATE OF RETURN ON THE FAIR VALUE OF )  
ITS OPERATIONS THROUGHOUT THE STATE )  
OF ARIZONA. )

DOCKET NO. E-01933A-07-0402

Arizona Corporation Commission

DOCKETED

OCT 05 2007

DOCKETED BY

**NOTICE OF FILING SUPPLEMENTAL EXHIBIT  
TO THE DIRECT TESTIMONY OF MICHAEL J. DECONCINI**

Tucson Electric Power Company, through undersigned counsel, hereby submits the attached Exhibit MJD-4 as a supplemental exhibit to the Direct Testimony of Michael J. DeConcini. Exhibit MJD-4 is a Coordination of Operations Report and is submitted in this docket pursuant to Decision No. 66028 (July 3, 2003).

RESPECTFULLY SUBMITTED this 5<sup>th</sup> day of October 2007.

ROSKA DEWULF & PATTEN, PLC

By

Michael W. Patten  
J. Matthew Derstine  
One Arizona Center  
400 East Van Buren Street, Suite 800  
Phoenix, Arizona 85004

ROSHKA DeWULF & PATTEN, PLC  
ONE ARIZONA CENTER  
400 EAST VAN BUREN STREET - SUITE 800  
PHOENIX, ARIZONA 85004  
TELEPHONE NO 602-256-6100  
FACSIMILE 602-256-6800

1  
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and  
  
Raymond S. Heyman  
Michelle Livengood  
Tucson Electric Power Company  
One South Church Avenue, Ste 200  
Tucson, Arizona 85701

Original and 15 copies of the foregoing  
filed this 5<sup>th</sup> day of October 2007 with:

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

Copy of the foregoing hand-delivered/mailed  
this 5<sup>th</sup> day of October 2007 to:

Chairman Mike Gleason  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Commissioner William A. Mundell  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Commissioner Jeff Hatch-Miller  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Commissioner Kristin K. Mayes  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Commissioner Gary Pierce  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Lyn A. Farmer, Esq.  
Chief Administrative Law Judge  
Hearing Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

**ROSHKA DEWULF & PATTEN, PLC**

ONE ARIZONA CENTER  
400 EAST VAN BUREN STREET - SUITE 800  
PHOENIX, ARIZONA 85004  
TELEPHONE NO 602-256-6100  
FACSIMILE 602-256-6800

- 1 Jane Rodda, Esq.
- 2 Administrative Law Judge
- 3 Hearing Division
- 4 Arizona Corporation Commission
- 5 400 W. Congress
- 6 Tucson, Arizona 85701
  
- 7 Christopher C. Kempley, Esq.
- 8 Chief Counsel, Legal Division
- 9 Arizona Corporation Commission
- 10 1200 West Washington Street
- 11 Phoenix, Arizona 85007
  
- 12 Ernest G. Johnson
- 13 Director, Utilities Division
- 14 Arizona Corporation Commission
- 15 1200 West Washington Street
- 16 Phoenix, Arizona 85007
  
- 17 C. Webb Crockett
- 18 Patrick J. Black
- 19 FENNEMORE CRAIG, PC
- 20 3003 North Central Avenue, Suite 2600
- 21 Phoenix, Arizona 85012-2913
  
- 22 Scott S. Wakefield, Chief Counsel
- 23 Residential Utility Consumer Office
- 24 1100 West Washington, Suite 220
- 25 Phoenix, Arizona 85007
  
- 26 Timothy Hogan
- 27 Arizona Center for Law
- in the Public Interest
- 202 East McDowell Road, Suite 153
- Phoenix, Arizona 85004
  
- Jeff Schlegel
- SWEEP Arizona Representative
- 1167 West Samalayuca Dr
- Tucson, Arizona 85704
  
- Michael Grant, Esq.
- Gallagher & Kennedy
- 2575 East Camelback Road
- Phoenix, Arizona 85016
  
- Gary M. Yaquinto
- Arizona Investment Council
- 2100 North Central Avenue, Suite 210
- Phoenix, Arizona 85004

**ROSHKA DeWULF & PATTEN, PLC**

ONE ARIZONA CENTER  
400 EAST VAN BUREN STREET - SUITE 800  
PHOENIX, ARIZONA 85004  
TELEPHONE NO 602-256-6100  
FACSIMILE 602-256-6800

- 1 Nicolas J. Enoch  
Lubin & Enoch, PC
- 2 349 North Fourth Avenue  
Phoenix, Arizona 85003
- 3
- 4 Peter Q. Nyce, Jr  
General Attorney-Regulatory Office  
Department of the Army
- 5 901 North Stuart Street  
Arlington, Virginia 22203
- 6
- 7 Dan Neidlinger  
Neidlinger & Associates  
3020 North 17<sup>th</sup> Drive
- 8 Phoenix, Arizona 85015
- 9 Daniel D. Haws  
OSJA, Attn: ATZS-JAD
- 10 USA Intelligence Center  
Ft Huachuca, Arizona 85613
- 11
- 12 Lawrence Robertson  
P. O. Box 1448  
Tubac, AZ 85646
- 13
- 14 David Berry  
Western Resource Advocates  
P. O. Box 1064
- 15 Scottsdale, Arizona 85252
- 16 Eric Guidry  
Western Resource Advocates  
2260 Baseline Road, Suite 200
- 17 Boulder, Colorado 80302
- 18
- 19 Robert J. Metli  
Snell & Wilmer LLP  
One Arizona Center
- 20 400 East Van Buren  
Phoenix, AZ 85004
- 21
- 22 Thomas Mumaw  
Barbara A. Klemstine  
Brian Brumfield
- 23 Arizona Public Service Company  
P. O. Box 53999, Station 9708
- 24 Phoenix, Arizona 85072
- 25 Greg Patterson  
Arizona Competitive Power Alliance
- 26 916 West Adams, Suite 3  
Phoenix, Arizona 85007
- 27

**ROSHKA DEWULF & PATTEN, PLC**  
ONE ARIZONA CENTER  
400 EAST VAN BUREN STREET - SUITE 800  
PHOENIX, ARIZONA 85004  
TELEPHONE NO 602-256-6100  
FACSIMILE 602-256-6800

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24  
25  
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27

S. David Childers, P.C.  
Low & Childers, P.C.  
2999 North 44<sup>th</sup> Street, Suite 250  
Phoenix, Arizona 85018

Christopher Hitchcock  
Law Offices of Christopher Hitchcock  
P. O. Box AT  
Bisbee, Arizona 85603

Michael L. Kurtz, Esq.  
Kurt J. Boehm, Esq  
Boehm, Kurtz & Lowry  
36 East Seventh Street, Suite 1510  
Cincinnati, Ohio 45202

By Mary Appolito

**EXHIBIT**

**MJD-4**

**Coordination of Operations Report  
Docket No. E-01933A-07-0402**

**Tucson Electric Power Company  
and  
UNS Electric, Inc. - Santa Cruz Operations**

**October 5, 2007**

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## **I. Purpose of Report**

On July 3, 2003, the Arizona Corporation Commission (“Commission”) issued Decision No. 66028, which approved, among other things, the transfer of Citizens Communications Company’s (“Citizens”) Arizona electric assets to UniSource Energy Corporation (“UniSource Energy”). The new entity, UNS Electric, Inc. (“UNS Electric”) serves customers in Santa Cruz County and in Mohave County. In that Decision, the Commission ordered Tucson Electric Power Company (“TEP”) to submit a feasibility study and consolidation plan or, in the alternative, a plan for the coordination of operations of TEP with UNS Electric’s operations in Santa Cruz County.

Consolidation of the Santa Cruz County operations with the TEP operations is not economically feasible due to TEP’s two-county bond financing. A primary requirement of the two-county bond financing is that the utility utilizing this financing mechanism can serve customers in no more than two counties (for TEP, those counties are Pima and Cochise). To extend service beyond two counties would invalidate that financing and add a significant amount of alternative financing costs for TEP. Therefore, TEP and UNS Electric (collectively referred to as the “Companies”) have identified and analyzed areas where the operations of the Companies could be coordinated. This report identifies the implementation and integration that has occurred to-date, and future anticipated efforts. This effort is an on-going process that will continue into the foreseeable future.

## **II. Overview**

### **A. Coordination Effort**

Even before the acquisition of the Citizens’ Arizona gas and electric properties was finalized, TEP had begun to analyze how to integrate the Companies and to identify the priorities. Because of its proximity to TEP’s service territory, attention was focused on the synergies that could be developed to benefit the customers in the Santa Cruz service territory.

In performing the analysis, the Companies focused on potential improvements in two major areas: (1) increased reliability, and (2) improved customer service for the Santa Cruz service area. Because the Companies have an obligation to their customers to provide reliable electric service, this was a priority. All of the changes that have been implemented were made to improve business efficiency and provide either a direct or indirect benefit to customers.

The Companies have combined efforts to identify opportunities for increased business efficiencies by maximizing human and material resources. The goals for integration of operations include:

- Increasing reliability for UNS Electric’s system in Santa Cruz County;
- Implementing consistent processes, policies, regulatory filings and performance standards;
- Centralizing communication, contract coordination and invoicing;
- Merging projects and project management;
- Utilizing construction “best practices”;

- **Creating economies of scale in purchasing, consulting and contracting;**
- Expanding technologies and systems;
- Consolidating control operations and system planning and design;
- Combining work force functions;
- Improving budget planning; and
- Planning for generation additions and operational improvements.

**B. Consolidation v. Coordination -  
Impact of Two-County Bond Refinancing**

TEP has \$359 million of two-county (local furnishing) tax-exempt bonds outstanding, as well as \$31 million of two-county debt remaining under the long-term lease for Sundt Unit 4. The weighted average cost of these debt obligations at September 30, 2007 was approximately 5.0%. Additionally, TEP repurchased \$221 million of local furnishing bonds in 2005 which may be reissued or refinanced at a later date. If these bonds were to lose their tax-exempt status, TEP would be forced to redeem all of the two-county debt obligations currently outstanding and TEP would lose its ability to reissue \$221 million of two-county bonds on a tax-exempt basis.

A refinancing of the entire \$390 million principal amount of two-county debt obligations would require TEP to issue a like amount of taxable corporate bonds. Assuming TEP would be able to market and sell taxable bonds in this amount, the one-time issuance costs would be approximately \$6 million (estimated at 1.5% of par value). The increase in annual interest expense would depend on the interest rate spread between the newly issued taxable bonds and the existing tax-exempt bonds. If new taxable bonds are issued at an estimated interest rate of 6% to 7%, the estimated interest rate spread would be approximately 1% to 2% on the entire \$390 million principal amount. Such a refinancing would increase TEP's interest expense by \$4 million to \$8 million per year. Additionally, since TEP would be forced to retire the \$221 million of two-county bonds repurchased in 2005, TEP would incur higher financing costs in the future estimated at \$2 million to \$4 million per year.

Clearly, there are substantial one-time costs and annually recurring costs that would be incurred by TEP if TEP's two-county bonds were to lose their tax-exempt status. For this reason, the Companies determined that the coordination of operations, rather than the consolidation of the Companies, was the most prudent approach.

**III. Implementation and Planned Integration**

**A. Reliability**

In analyzing the Santa Cruz County electric operations, it was clear that reliability was an important concern. The customers in Santa Cruz County had experienced an extraordinary number of outages during the late 1990s, under the predecessor company. The Companies identified a number of improvements that could be made to ensure greater reliability for Santa Cruz customers.

~~TEP designed and implemented several enhancements to the Santa Cruz transmission and distribution system.~~ These improvements are aimed at improving reliability, and in those circumstances where there is a power outage, reducing the time necessary to restore service to customers. In addition, TEP transferred the operational control of the Santa Cruz system to its system control room in Tucson to further enhance the value of these improvements. In conjunction with this transfer, the Companies incorporated remote start capability for the turbines in the TEP system control room.

UNS Electric had three turbines located at the Valencia Substation upon the transfer to UniSource Energy. In 2006, a fourth turbine was placed into service at this site. These turbines are used to meet the majority of the load requirements during times when the 115 kV transmission line is unavailable, during low voltage conditions and when the 115 kV transmission is unable to support the total Santa Cruz load requirement. Historically, these turbines have been started manually by Santa Cruz operating personnel in Nogales. TEP implemented remote-start capability from TEP's system control center in Tucson, which significantly shortened the time needed to restore power to Nogales in the event of the loss of the 115 kV transmission line.

In addition, TEP incorporated the Santa Cruz system into its Energy Management System ("EMS") so TEP can operate the transmission and distribution system. TEP also became the interface with the Western Area Power Administration ("Western") for the Santa Cruz service area. These changes have provided an improved level of power restoration, which has improved reliability and benefited customers.

To correct low voltage problems, 25 shunt capacitors were installed in the 2004 time frame and additional capacitors have subsequently been installed on the Santa Cruz distribution system. The improvement in voltage reduced the need to run the Valencia turbines during high load periods.

TEP's Canoa Substation is located approximately five miles from the UNS Electric Kantor Substation. If UNS Electric loses the 115 kV transmission system, there is sufficient capacity at Canoa to interconnect and carry some of the load on the Kantor and Canez Substations. However, the use of this alternative is limited because TEP is restricted by its two-county financing to only provide service in the two counties it serves, absent emergency circumstances. Therefore, this interconnection can only be used during emergency conditions. Despite this limitation, the Companies determined that such an interconnection is important for reliability purposes. The Companies constructed a 46 kV tie line between TEP's Canoa Substation and UNS Electric's Kantor Substation in 2004 to provide support to UNS Electric in the event of an emergency.

TEP purchased a mobile transformer in 2006 which was designed and constructed to accommodate the differing transmission voltages of the Santa Cruz and Tucson area systems. This transformer was used at the Valencia Substation in 2007 in conjunction with construction activities related to modifications to that Substation. UNS Electric pays a cost based service fee to TEP when the TEP mobile transformer is required in its service territory.

TEP has provided extensive planning and engineering support to UNS Electric at both the distribution and transmission level. For Santa Cruz, TEP planning and engineering has been

~~working on needed transmission import capability into the area. This includes planning for the conversion of the existing line to Nogales from 115 kV to 138 kV as well as altering its source feed from the Western 115 kV system to TEP's 138 kV/345 kV system. This conversion will increase the capability of the line to serve load into the future. Additional efforts with Western have resulted in the conversion from point-to-point transmission service in the Mohave area to network service. This change has eliminated a contract limitation for serving additional load in the Mohave region and reduced transmission costs for UNS Electric.~~

The Companies previously provided the Commission with detailed information regarding the integration of operations for purposes of reliability in Santa Cruz County. See "Supplemental Information to Response to Commission Questions and Updated Outage Response Plan for Santa Cruz County," (filed with the Commission on April 30, 2004 and an errata filed on May 3, 2004) in Docket No. E-01032A-99-0401.

## **B. Software**

In today's business climate, software plays a major role in daily business operational efficiency. A new customer information system, Cordaptics, was implemented for storing and retrieving both TEP and UNS Electric customer information. TEP's MP2 maintenance software, which is used for substations, proactively addresses system maintenance needs and has been integrated into the Santa Cruz County operating system. This enables a continuous monitoring of system maintenance needs, heading off potential problems by keeping system maintenance up to date and alerting personnel of system maintenance requirements in advance.

TEP's Outage Management System ("OMS") has the capability to detect for the Santa Cruz service area the cause of customer outages based on customer calls and its ability to trace back to a common point of failure from those calls. This system has helped TEP personnel to manage distribution outages efficiently through better outage tracking, prioritization and improved dispatch time. The Companies converted the Santa Cruz distribution maps to TEP's Geographic Information System ("GIS") and installed the OMS for the Santa Cruz service area. This has resulted in improvements in restoration time due to enhanced detection capability of the OMS and the ability to manage outages from TEP's control room. Similar conversions are being studied for the Mohave area.

TEP's Load Forecasting group is now developing the UNS Electric retail load forecast for UNS Electric operations. This function was previously outsourced to a third-party. Further work is being performed by TEP's Financial Planning group for short- and long-term forecasting and budgeting. TEP's Supply-Side Planning group has developed system models in PROMOD and Strategist for UNS Electric's operations. These models have been utilized when UNS Electric issued Requests for Proposals for purchased power in anticipation of the expiration of UNS Electric's current all-requirements contract. Both TEP's Supply-Side Planning and Transmission Planning groups are coordinating their efforts to evaluate UNS Electric's long-term system needs for both transmission and generation. TEP Distribution Control is currently performing the planned switching at the Santa Cruz substations. Previously, the switching was performed by UNS Electric personnel in the Kingman dispatch office.

### **C. Communications**

A continuous flow of current information is critical for all business endeavors. For that reason, telephone communications have been upgraded using fiber optics to enhance direct communications between TEP and Santa Cruz operations. Video conferencing at multiple locations has been implemented to improve communications between TEP and UNS Electric's operations, which eliminates or reduces travel time needed for "face-to-face" meetings.

Another aspect of communication is the interconnected infrastructure for Control Area Operations including providing adequate bandwidth for Supervisory Control and Data Acquisition ("SCADA"), data retrieval, including radio, telephone and information technology applications. A new radio system has been implemented in the Santa Cruz area and the Gold Hill radio repeater site was constructed. This radio system is compatible with TEP's system and has improved radio coverage in the Santa Cruz area. TEP also purchased two radio repeater sites and has upgraded its microwave system to provide high speed communications between Nogales, Tucson and Kingman. The operating and information technology groups have benefited from this upgrade.

### **D. Customer Service**

Since January 5, 2004, the TEP Customer Care Center has been handling all inbound phone activity for the Santa Cruz electric operations. By routing all calls through the centralized call center, the Companies have improved the call volume capacity, increased customer service representative availability, extended hours of availability to customers to 12 hours per business day and provided a more consistent application of customer service policies. An effort has been made to improve communications with the Santa Cruz customers. Bill messages and bill inserts have been substantially improved through the support of the Corporate Communications group. TEP began making outbound courtesy calls to Santa Cruz customers in February 2004. Outbound calls are placed to delinquent customers to advise them of the status of their delinquent account, remind customers to make payments, inform customers of payment locations and provide payment option information. The goal is to avoid situations that might result in customers being disconnected.

In March 2004, the Companies established procedures consistent with TEP's procedure for after-hours reconnect requests in the Santa Cruz service territory. Since April 1, 2004, a work tracking mechanism has been implemented in the Nogales office. Its purpose is to track work units for inclusion in customer service reporting.

The TEP Commercial Customer Care group has incorporated Santa Cruz service customer care responsibilities for UNS Electric's large customers located in Santa Cruz into their current job responsibilities, without additional staff. The team is endeavoring to increase the level of personalized service to individual customers and commercial associations, identify and standardize policies to create consistency across UniSource Energy subsidiaries, and reduce cost.

To date, assumed duties have included assisting large customers with operational issues and rate analysis; meeting with government and commercial organizations to explain the

~~acquisition, rate impacts and future UNS Electric goals (including facility and reliability improvements); and actively participating on the Santa Cruz Economic Development Foundation.~~

Low-Income, Demand-Side Management and Renewable Energy program planning and administration have been centralized and improved for the benefit of UNS Electric customers.

#### **E. Land Management**

The TEP Public Improvement group is coordinating all Santa Cruz County public improvement projects. This includes centralizing all communication, contract coordination and invoicing. This reallocation of workload decreases the need for overtime by Santa Cruz operations personnel. This provides an opportunity for Santa Cruz personnel to focus more on the design and construction of public improvements, system reinforcement and new business. This effort also provides for increased opportunities to work with governmental agencies involved in these projects, reducing conflicts during the design phase.

In addition, TEP's Land Department provides administrative oversight for line extension agreements, assists with land acquisitions, permitting, re-zonings and other right-of-way related efforts for the UNS Electric Santa Cruz operations. TEP will also perform the necessary environmental permitting to comply with the National Environmental Policy Act and state and local laws. The technical expertise and work effort provided by TEP reduces or eliminates the need for additional staff or consultants in Santa Cruz County.

#### **F. Fleet Management**

TEP is coordinating the purchase of new equipment for the Santa Cruz operations. This includes writing specifications, bidding the equipment to vendors and placing the equipment in service. In addition, TEP Fleet Services is handling all vehicle registration renewals and any associated functions. The Santa Cruz fleet is utilizing the Wright Express Fuel system for all off-site fueling. TEP coordinates the Wright Express fueling cards and invoices, and tracks fuel usage in the TEP fuel system.

A new asset management system was installed and is used to track information for TEP and UNS Electric. Major equipment repairs are done at the TEP automotive shop and service calls to field crews are dispatched from Tucson as needed.

#### **G. Environmental Issue Administration**

Since the acquisition of Citizens by UniSource Energy, TEP has coordinated all environmental compliance obligations for UNS Electric. TEP applies for and negotiates all environmental permits required by UNS Electric, including the permits required for the turbine additions at the Valencia Power Plant and the Black Mountain Generating Station. TEP also planned for and managed the upgrade of emission monitoring equipment for the UNS Electric Valencia turbines. TEP prepares and submits reports to local, state and federal environmental agencies required by regulation or permit, and develops practices to ensure environmental compliance. TEP arranges for disposal of all regulated waste generated by UNS Electric and

~~oversees the soil and groundwater remediation initiated by Citizens at Valencia, which is currently being conducted under the Arizona Department of Environmental Quality's ("ADEQ's") Voluntary Remediation Program.~~

#### **H. Standardization Efforts**

The Companies recognize that standardization of processes and cross-training of personnel will result in a more effective work force that can address outages and emergencies in an efficient manner. Therefore, these issues are being addressed in a number of ways.

A plan for cross-training of TEP and the UNS Electric Santa Cruz County personnel has been implemented for the Control Area Operations and Support Technology areas. Cross-training of TEP and UNS Electric personnel on electric metering processes and a comparison of wiring standards and other processes has been completed.

High priority operating procedures, materials and metering have been standardized. For example, UNS Electric has adopted TEP's Outage Notification Procedure. In addition, the Companies are in the process of developing uniform construction standards and design criteria. Regularly scheduled meetings are held with representatives from the Companies to discuss "best practices" and develop standards that will provide for consistent work, construction and safety practices. In addition, uniform construction standards and design criteria provide an opportunity for cost savings.

The Companies are also in the initial stages of developing uniform procedures and standards to comply with corporate standards, Federal Communications Commission requirements and the 1996 Telecommunications Act for third-party attachments to electric poles. The goal is to provide centralization for standardization and review of contracts and application procedures, development of attachment rates, consistency in notification of procedural changes and the coordination of facilities audits.

#### **IV. Cost Savings/Economies of Scale**

Some improvements that should provide savings include reducing the purchase of non-standard materials, reducing purchasing activity from multiple vendors and increasing purchasing volume. For example, the Materials Management Department has streamlined purchasing by optimizing purchase order processes. By consolidating orders and purchasing meters and transformers from a single vendor, cost savings should be recognized. The Companies are holding on-going ad-hoc meetings to review common materials to determine where further cost savings might be realized.

It is also anticipated that the sharing of personnel resources should provide cost savings. TEP engineers will review relay coordination studies and project orders that had previously been outsourced to engineering firms which will provide cost savings for UNS Electric. The use of TEP personnel, instead of outside contractors, to provide substation landscaping is another opportunity to cut costs. In addition, the utilization of TEP's information technology ("IT") computer support center reduces IT costs for Santa Cruz County.

**V. Conclusion**

As this Report indicates, TEP and UNS Electric have made substantial efforts to coordinate the operations of the Companies to improve the reliability of the system and to implement business efficiencies. Each of these improvements will benefit customers either directly or indirectly. The Companies will continue to identify, analyze and implement processes that will facilitate efficiencies and good business practices. The effort to coordinate the operations is an on-going effort that will continue into the foreseeable future.