



Grand Canyon State Electric
Cooperative Association, Inc. ORIGINAL



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Your Touchstone Energy Cooperatives

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

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Re: *AEPCO Exception to the Final Staff Report and Recommended Opinion and Order (November 6, 2007) for Competitive Procurement Issues; Docket No. E-00000E-05-0431*

Dear Sir/Madam:

Arizona Electric Power Cooperative, Inc. ("AEPCO"), as a generation cooperative, submits this Exception to the Final Commission Staff Report and Recommended Opinion and Order ("ROO") for Competitive Procurement Issues, dated November 6, 2007. AEPCO focuses its Exception on the requirement that an independent monitor should be used in certain requests for proposal ("RFP") processes for procurement of new resources. The Commission should modify this language so that this requirement does not apply to cooperatives that are subject to Rural Utilities Service (RUS) regulations under 7 CFR Section 1710.

AEPCO agrees with the Staff recommendations that: (1) a rulemaking on the resource acquisition process should not be instituted and (2) an RFP solicitation process should be the primary resource acquisition tool. As Staff notes, "Arizona's electric utilities have very different characteristics and a "one size fits all" set of procurement rules might not allow for flexibility that each of the utilities needs to fulfill its individual growth requirements."

In that spirit, one of the things which is different about AEPCO is that, as an RUS borrower, AEPCO is already subject to extensive federal RFP requirements as to how the process is conducted. RUS oversees the entire RFP process, and no loan approval or loan funds are provided to AEPCO until the RUS Requirements are met.

The principal criterion under 7 C.F.R. § 1710, *et seq.* requires that any self-build generation plan has to be justified through a competitive solicitation for purchased power which is RUS-monitored and a highly transparent procedure. RUS is involved in a cooperative's process to self-build or purchase power from the beginning to the end of the process. For example, the investigations of alternative sources of power must be coordinated in advance with RUS. AEPCO must submit in advance studies including the comprehensive economic present-value analyses of the costs and revenues of the available self-generation, load management, energy conservation and purchased power options to the RUS. AEPCO is required to keep RUS fully informed on evaluations of RFP responses and provide supporting information as requested by RUS. Such evaluations of all the purchase power alternatives to generating unit construction must demonstrate that any decision results in the most economical and effective way to meet the power requirement.

RUS will determine, based on this information provided by the borrower or based on its own assessment whether RUS will require further information or other methods of determining how to supply needed generation capacity.

Finally, the RUS requires borrowers to solicit proposals from all potential sources of power, including municipals, investor-owned utilities, independent power producers and co-generators. To assure the broadest possible range of RFP participation, AEPCO must also

publish the solicitations for proposals in at least three national publications. The RUS requires copies of these publications..

RUS regulations under 7 CFR Section 1710.253 and 254 have been attached as Exhibit B.

AEPCO has cited for the Staff three examples of AEPCO's implementation of the RUS process that resulted in a multi-year purchase power agreements ("PPA") being executed with Arizona merchant power plants, one in 2003 and two in 2006.

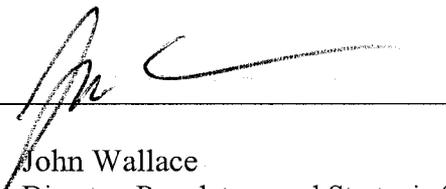
In conclusion, an additional monitor should not be required for AEPCO or other cooperatives that are RUS borrowers for their procurements. An additional monitor would be duplicative of safeguards already in place, increase the required lead-time for project approval and increase costs without providing additional benefit for such cooperatives, their members or the entities likely to participate in the process.

AEPCO requests that the Commission modify the ROO such that the independent monitor requirement does not apply to cooperatives that are RUS borrowers. Suggested amendment language is attached as Exhibit A.

Very truly yours,

GRAND CANYON STATE ELECTRIC
COOPERATIVE ASSOCIATION

By _____


John Wallace
Director, Regulatory and Strategic Services

Docket Control
November 19, 2007
Page 4

Original and 13 copies filed with Docket
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Docket Control
November 19, 2007
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Docket Control
November 19, 2007
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Docket Control
November 19, 2007
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Docket Control
November 19, 2007
Page 8

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EXHIBIT A

**AEPCO's Requested Amendments to Competitive Procurement
Recommended Opinion and Order**

In the ROO at p. 3, line 21, after the end of the sentence, insert the language: "Rural Utilities Service ("RUS") borrowers are exempt from this requirement because the RUS performs similar functions as an independent monitor."

EXHIBIT B

RUS Regulations Under 7 CFR Section 1710.253

§ 1710.253

§ 1710.253 Engineering and cost studies—addition of generation capacity.

(a) The construction or purchase of additional generation capacity and associated transmission facilities by a power supply or distribution borrower, including the replacement of existing capacity, shall be supported by comprehensive project-specific engineering and cost studies as specified by RUS. The studies shall cover a period from the beginning of the project to at least 10 years after the start of commercial operation of the facilities.

(b) The studies must include comprehensive economic present-value analyses of the costs and revenues of the available self-generation, load management, energy conservation, and purchased-power options, including assessments of service reliability and financing requirements and risks. Requirements for analyzing purchased-power options are set forth in § 1710.254.

(c) Generally, studies of self-generation, load management, and energy conservation options shall include, as appropriate, analyses of:

- (1) Capital and operating costs;
- (2) Financing requirements and risks;
- (3) System reliability;
- (4) Alternative unit sizes;
- (5) Alternative types of generation;
- (6) Fuel alternatives;
- (7) System stability;
- (8) Load flows; and
- (9) System dispatching.

(d) At the request of a borrower, RUS, in its sole discretion, may waive specific requirements of this section if such requirements imposed a substantial burden on the borrower and if such waiver will not significantly affect the accomplishment of the objectives of this subpart.

§ 1710.254 Alternative sources of power.

(a) *General.* (1) RUS will make loans to finance the construction of generation facilities by distribution or power supply borrowers and transmission facilities by power supply borrowers only under the following conditions if said borrowers do not already own and operate such types of facilities:

7 CFR Ch. XVII (1-1-07 Edition)

(i) Where no adequate and dependable source of power is available to meet the consumers' needs; or

(ii) Where the rates offered by other power sources would result in a higher cost of power to the consumers than the cost from facilities financed by RUS, and the amount of the power cost savings that would result from the RUS-financed facilities bears a significant relationship to the amount of the proposed loan.

(2) If a borrower already owns and operates the types of facilities included in a loan request, then a loan for the purposes contained in paragraph (a)(1) of this section, as well as for the construction of transmission facilities by a distribution borrower, will be considered and evaluated by RUS in terms of whether the proposed facilities constitute an effective and economical means of meeting the power requirements of the consumers. A borrower shall contact RUS as soon as practicable in order for RUS to review information submitted by the borrower and advise the borrower, in writing, whether there is a need for the borrower to investigate and seek alternative sources of power. RUS will determine, based on information provided by the borrower or otherwise available, whether there is a need to investigate alternative sources of power or whether RUS will require information or other methods of determining the need for the generation capacity. RUS will base its determination on whether RUS is able to conclude that the project is needed, the borrower would incur delays and costs in pursuing an RFP, or that an RFP is not likely to produce new alternatives to the project.

(b) Loan requests for the addition of generation capacity, including replacement of existing capacity, will be accepted by RUS when the applicant has completed the requirements established by RUS, in a manner satisfactory to RUS. The investigations of alternative sources of power must be coordinated in advance with RUS. This section applies to RUS financed generation capacity whether owned solely by the borrower, owned on an undivided ownership basis with other utilities or substantially controlled by the borrower.

Rural Utilities Service, USDA

§ 1710.300

(c) The applicant may be required to seek and utilize capacity available from RUS borrowers and other organizations before developing plans for additional generation capacity. RUS may require, on a case by case basis, that the applicant, among other things:

(1) Solicit power and energy purchase proposals from all reasonable potential sources of power, such as other electric cooperatives, investor-owned utilities, municipal utility organizations, and Federal and state power authorities.

(2) Solicit proposals from independent power producers, including co-generators, to determine the terms and conditions under which these producers can supply the additional power and energy needs of the applicant, without RUS financial assistance. Such solicitations should be placed in at least three national newspapers or trade publications, and they meet all planning, coordination or other requirements imposed by state authorities, as well as the environmental requirements of RUS.

(d) When solicitations are received in accordance with paragraph (c) of this section, the applicant will evaluate all alternative proposals on an economic, present-value basis, giving consideration to cost-effectiveness, reliability of service, the short-term and long-term financial viability of the supplier, and the financial risk to the borrower and its creditors. The applicant will keep RUS fully informed on these evaluations and provide supporting information and analysis as requested by RUS.

(e) After evaluation of all proposals received in accordance with paragraph (c) of this section, and having informed RUS of the results, the applicant may be required to negotiate final proposals with the entities submitting the best acceptable offers. Contracts requiring RUS approval will either be approved in advance by the Administrator or contain a provision that the contract is not valid until approved, in writing, by the Administrator. The Administrator will approve the contracts in a timely manner provided that the borrower has met all applicable requirements, including, among other matters, evidence that the alternative source of power se-

lected is an economical and effective alternative.

(f) RUS may make independent inquiries with potential power suppliers as to the availability of power to meet borrowers' needs. Information developed by RUS will be shared with borrowers at their request.

(g) Further details of RUS requirements for financing of generation and bulk transmission facilities are set forth in 7 CFR part 1712.

(h) At the request of a borrower, RUS, in its sole discretion, may waive specific requirements of paragraphs (b) through (e) of this section if such waiver is required to prevent unreasonable delays in obtaining generation capacity that could result in system reliability problems.

(Approved by the Office of Management and Budget under control number 0572-0032)

(57 FR 1053, Jan. 9, 1992, as amended at 65 FR 31247, May 17, 2000)

§§ 1710.255-1710.299 [Reserved]

Subpart G—Long-Range Financial Forecasts

§ 1710.300 General.

(a) RUS encourages borrowers to maintain a current long-range financial forecast. The forecast should be used by the board of directors and the manager to guide the system towards its financial goals.

(b) A borrower must prepare, for RUS review and approval, a long-range financial forecast, approved by its board of directors, in support of its loan application. The forecast must demonstrate that the borrower's system is economically viable and that the proposed loan is financially feasible. Loan feasibility will be assessed based on the criteria set forth in § 1710.112.

(c) The financial forecast and related projections submitted in support of a loan application shall include:

(1) The projected results of future actions planned by the borrower's board of directors;

(2) The financial goals established for margins, TIER, DSC, equity, and levels of general funds to be invested in plant;

(3) A pro forma balance sheet, statement of operations, and general funds