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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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- GARY PIERCE

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IN THE MATTER OF THE  
APPLICATION OF ARIZONA PUBLIC  
SERVICE COMPANY FOR APPROVAL  
OF RENEWABLE ENERGY  
STANDARD IMPLEMENTATION  
PLAN, DISTRIBUTED ENERGY  
ADMINISTRATION PLAN,  
CUSTOMER SELF-DIRECT  
RENEWABLE RESOURCE TARIFF,  
AND RESET OF RENEWABLE  
ENERGY ADJUSTOR

DOCKET NO. E-01345A-07-0468

ARIZONA PUBLIC SERVICE  
COMPANY'S RESPONSE TO  
STAFF'S REPORT AND  
RECOMMENDED ORDER

Arizona Public Service Company ("APS" or "Company") filed its 2008 Renewable Energy Standard Implementation Plan ("Implementation Plan") for Arizona Corporation Commission ("Commission") approval on August 7, 2007, in compliance with the Renewable Energy Standard ("RES") Rules.<sup>1</sup> A revised Implementation Plan was filed for Commission approval on August 30, 2007. The Company is filing these Comments in response to the Commission Staff's Transmittal Memorandum and Proposed Order ("Staff Report"), which was filed in this docket on February 29, 2008.

The varied plans that have been proposed by parties in this docket reflect a number of approaches that could be taken to implement the recently adopted RES Rules. The Company's original Implementation Plan, the joint proposal that was developed by the Company and the Solar Advocates<sup>2</sup> ("Joint Proposal"), and Staff's proposals, Option A and Option B, are all viable plans, although each approach has distinct considerations and

<sup>1</sup> A.A.C. R-14-2-1801 through 1816.

<sup>2</sup> The Joint Plan was filed by APS and the Solar Advocates on December 17, 2007.

1 impacts. APS's Implementation Plan, the Joint Proposal and Staff's Option A offer  
2 opportunity for full compliance with the RES Rules, where Staff's Option B requires  
3 modification to the Distributed Renewable Energy Requirement for the first five years.  
4 While the Company supports both its Implementation Plan and the Joint Proposal, APS also  
5 believes that Staff's Option B is a reasonable approach, although further modification to  
6 allow flexibility in distributed program incentive allocations is requested.

7       The varied programs each seek to address alternatives for implementing the RES  
8 Distributed Energy ("DE") requirement and emphasize the need for flexibility during the  
9 early years. Customer participation in the DE program will depend on many factors and the  
10 immediate funding needs are difficult to predict. As Staff has noted, the cost assumptions  
11 for the DE portion of the Implementation Plan are dependent on the technologies that  
12 customers select and the level of customer participation. The bottom line is that the  
13 Company is prepared and eager to move forward with the implementation of renewable  
14 energy programs, in whatever form or manner the Commission finds most appropriate at this  
15 time. Furthermore, APS will be filing its 2009 Implementation Plan by July 1, 2008, which  
16 provides the opportunity to achieve several months of actual experience with the plan the  
17 Commission approves, and allows the Company to report on the preliminary effectiveness of  
18 that plan. The key points of the various proposed plans are discussed below.

#### 19 **APS's IMPLEMENTATION PLAN**

20       The Company's Implementation Plan is the first plan filed by APS pursuant to the  
21 RES Rules. It was designed to allow the Company the opportunity for full compliance,  
22 although APS has acknowledged that there is much uncertainty in the renewable energy  
23 markets, particularly how customers will respond to the DE program. The Implementation  
24 Plan included the Company's best estimate of technologies that may be available to the  
25 marketplace in the next five years, based on the information that was available at the time of  
26 the filing. In combination, the Implementation Plan and the Distributed Energy  
27 Administration Plan ("DEAP") described the Company's plan to fully implement the RES  
28 requirements, including the Company's approach for acquiring the renewable generation

1 resources, for development of a DE market, and an infrastructure development and  
2 implementation to support a substantially larger and further-reaching program. The  
3 Company's Implementation Plan proposed comprehensive customer outreach and marketing  
4 efforts, and requires significant resources to implement the considerable DE components.

5 The Implementation Plan proposed a 2008 budget of \$48.2 million, comprised of  
6 approximately \$10 million collected under the current adjustor, \$6 million collected in base  
7 rates, and an additional \$32.2 million through a reset of the adjustor. At the end of 2007,  
8 \$3.5 million that was allocated to customer incentives was unreserved, providing the  
9 opportunity to roll forward those funds into the 2008 budget and lower the additional funds  
10 needed. The Company believes that its Implementation Plan provides an opportunity to  
11 reach full compliance. Under any alternative, it must be recognized that ramping up the DE  
12 program is a challenge, even considering the RES Rules provisions to pro-rate the targets in  
13 the first year based on when the funding mechanism is approved.<sup>3</sup>

#### 14 **STAFF'S PROPOSALS**

15 Staff has proposed two different options for the Commission's consideration. Option  
16 A would reduce the total funds available for the 2008 implementation plan by pro-rating the  
17 required funding to recognize that the first quarter of the year is already completed and by  
18 reducing the Administration, Implementation, Marketing, Outreach, Commercialization and  
19 Integration or "non-project" budget. Option B proposed modifications to the distribution  
20 within the DE categories in the first five years, while holding the overall DE requirement to  
21 the RES-defined level. The proposed changes in Option B increase the role of wholesale DE  
22 and allow for more flexibility in the balance between the residential and non-residential  
23 requirements. Option B also reduced the non-project budget.

24 APS takes exception to Staff's characterization of the Company's Administration,  
25 Implementation, Marketing, Outreach, Commercialization and Integration budget as  
26 "excessive." The majority of this budget is associated with the significant increase in the DE  
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28 <sup>3</sup> See, A.A.C. R14-2-1804(B) and 1805(B).

1 program under the RES Rules. For example, APS's Solar Partners Incentive Program  
2 facilitated just over 500 installations in 2007. For full compliance with the RES Rules, APS  
3 projects that over 7,000 installations would be required in 2008, and even under Staff Option  
4 B, over 20,000 installations would be required by 2012. To determine the funding necessary,  
5 based on its several years of experience implementing the Solar Partners Incentive Program,  
6 APS's non-energy/incentive costs were carefully projected by studying the functions  
7 necessary to administer and implement the RES program on a scale necessary to achieve  
8 compliance. APS developed its models to calculate the costs of receiving, processing,  
9 reviewing, inspecting and paying incentives, and projected those costs based on an increasing  
10 level of incentives each year. APS also built in efficiencies it expects to gain over time, such  
11 as a reduced number of needed inspections by using a qualified installer program and reduced  
12 reservation coordinators through one-time information technology upgrades.

13 APS developed its marketing approach and placement strategy to educate customers  
14 on the values of renewable energy, increase awareness of the incentive program, and to  
15 encourage participation. The proposed marketing approach included development and  
16 support of programs to train and qualify installers, and an investment in cooperative  
17 marketing with installers. APS's proposed budget for Commercialization and Integration  
18 studies was designed for both APS and interested stakeholders to gain a greater understanding  
19 of renewable energy and methods of integration into standard business operations and  
20 processes. Additionally, APS has already begun the scoping effort for the Distributed Energy  
21 Cost/Benefit Study that it is obligated to complete pursuant to Decision No. 70130.<sup>4</sup>

22 Under the Company's proposal, material portions of these budgets are directly related  
23 to the number of installations driven by the incentive budget and technologies selected by  
24 customers. However, as proposed in its Implementation Plan, portions of the Company's first  
25 year implementation cost is directly related to maintaining and improving customer service  
26 systems and processes. Included in these costs are technology solutions, such as customer  
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28 <sup>4</sup> Issued January 23, 2008.

1 and installer interfaces, workflow management systems, and performance and reporting tools,  
2 which are essential to effectively and efficiently implement the programs. Many of the  
3 technology solutions proposed to increase the efficiency and responsiveness of the program  
4 will have to be delayed or abandoned under the Staff's reduced budgets. It is also important  
5 to note that only actual costs are charged to the RES program, and that the Company has  
6 proposed that unused funds be rolled over into subsequent years to reduce the funding  
7 requirements.

8       **Option B:** The Company supports Staff's Option B with certain modifications,  
9 because Option B recognizes and supports the current program, while allowing the DE  
10 market to grow. The increased role of wholesale-distributed generation proposed in Option  
11 B allows flexibility and scale to reduce the cost of compliance during the first five years of  
12 the program. This option is consistent with the spirit of the rules; it does not change overall  
13 compliance targets and provides the Company with a greater likelihood of achieving the  
14 proposed DE targets in the early years. However, should the Commission adopt Staff's  
15 Option B, the resources available for customer service, customer outreach and marketing will  
16 be significantly reduced from what was originally proposed in the Company's  
17 Implementation Plan. This, in turn, could negatively affect the level of customer  
18 participation in the renewable energy programs.

19       Flexible targets are an inherent part of Staff's proposal for Option B. For example, the  
20 residential and non-residential requirements are proposed to be a "minimum" of 25% of the  
21 total requirement, although each of them could vary from the minimum 25% up to 75%. APS  
22 believes that with this approach, it is necessary to also have the flexibility to reallocate  
23 incentive budgets to match customer demand, with the ultimate goal of reaching both the  
24 minimum targets for each category and the overall distributed energy requirement.

25       Therefore, if the Commission adopts Staff's Option B, the Company requests that the  
26 incentive budget allow for flexibility among the classes of incentives, to allow the program  
27 to adjust to the customers' choices and actual energy results. Customer incentives have been  
28 allocated between Up Front Incentives ("UFIs") for residential and non-residential

1 customers, Performance Based Incentives (“PBIs”) for non-residential customers, and  
2 incentives for wholesale-distributed generation. These classes of incentives may require  
3 more or less funding depending on the demand for each class and the energy needed to  
4 achieve compliance. The need for the requested flexibility within the incentive budget is  
5 presently illustrated by the current demand in the non-residential segment seeking UFI. To  
6 date, the total reservations from this class of customer seeking UFIs exceeds the \$1,550,000  
7 that Staff has allocated in its budget.<sup>5</sup>

8         Allowing the Company the flexibility to allocate the total incentive budget in response  
9 to customer demand would permit the renewable energy programs to grow naturally and  
10 provide insight regarding the needs of the current market. If such flexibility is not allowed,  
11 the Company would be required to file for changes under the standard Commission  
12 processes when funds are depleted for a certain class of incentive, even if uncommitted funds  
13 are available and unneeded for compliance for another class. The disadvantage to that  
14 approach is that the incentive program would be suspended and customer projects would be  
15 put on hold until Commission approval was received.

16         While recognizing the reduction in its non-project budgets may negatively impact  
17 customer participation, the Company nonetheless believes that it is possible to work within  
18 the budget parameters proposed in Option B. The reduction in the residential distributed  
19 energy requirement in the early years will, as Staff indicates, necessarily reduce a portion of  
20 the administration and implementation budgets.

21         **Option A:** The Company also acknowledges that Staff’s Option A, which pro-rates  
22 the funding and RES requirements for 2008, is a practical approach for this year. However,  
23 as the Company has previously discussed, Staff’s proposed budget reductions will reduce the  
24 resources available for customer service, outreach and marketing, which could impact the  
25 level of customer participation. The Company’s key concern with Option A is that this

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27 <sup>5</sup> The oversubscription results from the structure of the current program, as compared to the proposed DE  
28 incentive structure. The current program allows customers to choose between UFIs and PBIs. If approved as  
proposed, the DEAP would require all projects receiving incentives greater than \$75,000 to be PBIs.

1 proposal perpetuates the “catch-up” issues already inherent in the RES Rules’ delayed  
2 implementation. As Staff noted, the RES Rules allow for a “ramp-up” to allow utilities and  
3 the renewable energy industry to gradually expand their efforts to meet annual increases in  
4 the Renewable Energy Requirement and the Distributed Renewable Energy Requirement.  
5 Early in the rulemaking process it was anticipated that the RES rules would be in effect by  
6 2006. That was not the case; the RES Rules went into effect in August 2007, and funding for  
7 the APS programs has not yet been approved. The effect of the delay is that the Company  
8 must already catch-up for the 2006 and 2007 requirements; under Option A, it would also  
9 have to catch-up for the first quarter of 2008. The result is that the Company would be  
10 further challenged to comply with the 2009 RES Rules requirements, and the budget for  
11 compliance with the RES in 2009 would be significantly higher than that described by the  
12 Company under its Implementation Plan.

### 13 JOINT PROPOSAL

14 In response to comments filed by the Solar Advocates<sup>6</sup> (“Solar Advocates’  
15 Comments”) and a letter from Commissioner Mundell asking for parties to attempt to reach a  
16 reasonable compromise regarding the issues raised in the Solar Advocates’ Comments,<sup>7</sup> APS  
17 and the Solar Advocates had a series of meetings. They addressed incremental funding  
18 levels, trigger mechanisms, the Company’s methods for developing costs for administration,  
19 implementation, and marketing, as well as modifications to the proposed RES budget. The  
20 outcome of those meetings was the Joint Proposal,<sup>8</sup> an alternative proposal that recommends  
21 a budget and funding mechanisms that better synchronizes program funding with expected  
22 residential DE customer participation, rolls over the uncommitted DE funds from 2007, and  
23 reduces the marketing and outreach budget.

24  
25  
26 <sup>6</sup> The Solar Advocates are a group comprised of the Annan Group, Arizona Solar Energy Industries  
27 Association, Greater Tucson Coalition for Solar Energy, Solar Alliance and Vote Solar Initiative. The Solar  
28 Alliance is an industry association comprised of the largest photovoltaic companies in the United States.

<sup>7</sup> Commissioner Mundell’s letter was docketed on October 16, 2007.

<sup>8</sup> The Joint Proposal was filed with the Commission on December 17, 2007. APS filed exhibits that detailed  
the funding for the Joint Proposal on December 21, 2007.

1 The Joint Proposal recognized that missing the early years of the designed “ramp-up”  
2 period under the RES Rules results in a significant increase over current customer  
3 participation levels. The Joint Proposal recommended a two-step approach for funding the  
4 required \$43.7 million necessary to comply. The initial funding would be set at \$37 million,  
5 a level providing DE funding four times higher than that offered in 2007, and would increase  
6 automatically to an annualized level of \$43.7 million when customer requests reached certain  
7 defined levels.

8 While APS recognizes that Staff has concerns regarding the automatic reset of the  
9 adjustor, the Company believes that an adjustor that responds to the market is appropriate.  
10 Even Staff recognized that the level of customer commitment is uncertain. The Company  
11 also notes that without an automatic adjustment mechanism, the program would likely have  
12 to forego paying incentives pending Commission approval if the original funds are depleted.  
13 Nonetheless, APS believes the Joint Proposal is a valid and valuable option, and should be  
14 considered by the Commission, even if the automatic adjustment provision is removed.

#### 15 **OTHER CONSIDERATIONS**

- 16 • Green Power Rates. APS believes that its approach related to Green Power sales is  
17 correct, notwithstanding Staff’s disagreement. APS did not count its sales under its  
18 Green Power rate schedules<sup>9</sup> towards the RES requirements, because doing so would  
19 prohibit these rates from achieving Green-e certification. Green-e is an independent  
20 certification and verification program for renewable energy developed that is offered  
21 by the Center for Resource Solutions. A renewable facility is not eligible for this  
22 certification if it was mandated by a local, state or federal government agency, or if  
23 the energy offered under a program is applied towards regulatory requirements.<sup>10</sup>  
24 Energy that is Green-e eligible may count for LEED certification for new buildings –  
25 a certification that is important to a growing number of APS customers. The  
26

27 <sup>9</sup> APS Rate Schedules GPS-1 and GPS-2.

28 <sup>10</sup> THE GREEN-E CLIMATE PROTOCOL FOR RENEWABLE ENERGY, Version 1.0, adopted Oct. 18, 2007 at pg. 5;  
available at [http://www.green-e.org/docs/Climate/Green-e\\_Climate\\_protocol\\_forRE.pdf](http://www.green-e.org/docs/Climate/Green-e_Climate_protocol_forRE.pdf).

1 Company also believes that customer choice can drive its renewable energy program  
2 beyond the requirements established by the Commission. The renewable generation  
3 costs are a small portion of the overall budget proposed by Staff, and counting Green  
4 Power sales toward RES compliance will not have a significant budgetary impact.  
5 For these reasons, the Company urges the Commission to continue to separate the  
6 Green Power sales from the RES requirements.

- 7 • DEAP Review Panel. To address the potential changes in the renewable energy  
8 markets that will be significantly expanded to meet the requirements of the RES  
9 Rules, APS proposed the creation of a DEAP Review Panel for ongoing review and  
10 adjustment of certain DEAP elements. APS believes that a panel with authority to  
11 expeditiously adjust the DEAP and its program elements is critical to the DE  
12 program's ultimate success. Program elements may need to be adjusted to reflect new  
13 information, changing market conditions, incorrect initial assumptions or  
14 technological innovations. The proposed panel would have five members, including  
15 one representative from Commission Staff, three representatives from the distributed  
16 generation industry and one representative from APS. Any recommended  
17 modifications would require unanimous approval of the panel. Suggested  
18 modifications to the DEAP that did not receive a unanimous vote may be included in  
19 the following year's Implementation Plan filing.

20 Staff has taken the position that the issue of a review panel is more  
21 appropriately addressed in the Commission's Uniform Credit Purchase Program  
22 ("UCPP") working group. While the Company agrees with Staff generally, APS  
23 continues to believe that at this point in time the DEAP Review Panel is worthwhile  
24 and beneficial. It is generally understood that the DEAP may require some  
25 modifications as more is learned about market and customer needs. The DEAP  
26 Review Panel could provide timely review and adjustments should the markets  
27 change significantly. If a UCPP panel is established to address these issues, APS  
28 believes that the DEAP Review Panel could then be disbanded.

- 1 • Solar Energy Augmentation for Fossil Fuel Plants. Jasper Energy LLC filed  
2 comments requesting that the Commission permit the Company to include solar  
3 energy related power augmentation systems at the Company's fossil fuel power  
4 plants. APS does not believe that specific authorization from the Commission is  
5 necessary. APS has received similar proposals to utilize solar energy augmentation  
6 systems in previous renewable energy Requests for Proposals, and will continue to  
7 consider these types of resource proposals.
- 8 • Metering of Off-Grid Renewable Systems. Sunrise Energy Alternatives LLC  
9 ("Sunrise") had raised concerns regarding the complexity of the APS process. The  
10 Company had originally proposed metering off-grid residential systems in much the  
11 same way it had proposed to meter output from grid-tied systems. In doing so, the  
12 Company did not recognize the full breadth of complicating issues. Historically, the  
13 Company had reported the energy contribution from off-grid systems using estimated  
14 production. After a review of the benefits of system metering and evaluating those  
15 benefits against technical complications and inspection and metering costs, the  
16 Company now intends to use a production estimate for small off-grid systems. For  
17 larger, off-grid non-residential systems, the Company and customer will develop a  
18 metering arrangement through the use of an engineering and design output report  
19 provided by the customer or installer. The Company has conferred with Sunrise, and  
20 this approach alleviated the concerns raised.
- 21 • Disclosure of Financing Arrangements. On December 21, 2007, APS docketed a  
22 letter to the Utilities Division Director regarding an issue that had been raised by  
23 SunEdison. In the Company's DEAP, APS had proposed that total project costs  
24 would include acceptable financing charges for purposes of calculating caps on  
25 commercial distributed energy incentives. However, some stakeholders do not wish  
26 to disclose financing charges, even though it would result in a lower cap for the total  
27 incentive payment. Therefore, APS is requesting that the Commission affirm that  
28

1 Section 6.4 of the DEAP may be modified to change the word "must" disclose to  
2 "may" disclose financing charges.

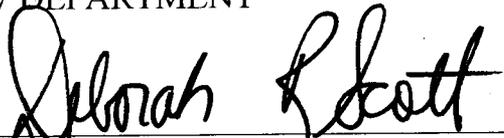
- 3 • Annual Budget Reconciliation. The Company notes that because of the nature of  
4 renewable energy, cost will vary with production output from generation facilities and  
5 customer distributed technology choices and demand for incentives. The RES  
6 budgets are actually an estimate of performance for generation technologies and for  
7 the DE program parameters. As a result, there may be variations to the budget from  
8 those described by the Implementation Plan. The Company will reconcile the budget  
9 at year-end, and take that reconciliation into account as part of its next  
10 Implementation Plan filing.

11 **CONCLUSION**

12 In this initial APS Implementation Plan docket, the Commission has been presented  
13 with a number of different approaches for implementation of the RES Rules. The Company  
14 initially filed its Implementation Plan that provides for full compliance with the 2008 RES  
15 requirements, and later jointly filed a modified approach to implementation with the Solar  
16 Advocates. Staff provided two different options in its Staff Report. It is clear that there are a  
17 number of ways to undertake this initial implementation. The Company believes that either  
18 of the proposals APS has filed, or Staff Option B, with some modification, will allow the  
19 Company to move forward with its renewable energy programs under the new RES Rules.

20 RESPECTFULLY SUBMITTED this 13<sup>th</sup> day of March, 2008.

21 PINNACLE WEST CAPITAL CORPORATION  
22 LAW DEPARTMENT

23  
24 By: 

25 Deborah R. Scott  
26 Attorneys for Arizona Public Service  
27 Company  
28

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8 March, 2008 to:

9 All Parties of Record

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