

ORIGINAL

THIS AMENDMENT:  
 Passed \_\_\_\_\_ Passed as amended by \_\_\_\_\_  
 Failed \_\_\_\_\_ Not Offered \_\_\_\_\_  
 \_\_\_\_\_ Withdrawn \_\_\_\_\_



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Arizona Corporation Commission

DOCKETED

2008 DEC 16 A 8:46

MAYES PROPOSED AMENDMENT 1

AZ CORP COMMISSION  
DOCKET CONTROL

DEC 16 2008

TIME/DATE PREPARED: December 15, 2008

DOCKETED BY

COMPANY: Arizona Public Service Company

AGENDA ITEM NO. U-20

DOCKET NO. E-01345A-08-0172

OPEN MEETING DATE: Dec. 16-19, 2008

Page 31: DELETE line 9 following "doubt" through line 27

AND INSERT:

"Based upon the testimony and evidence presented at the hearing combined with the current economic climate and the Commission's broad authority to determine what constitutes an emergency or whether one is imminent, we find that an emergency exists in this case.

Arizona Attorney General Opinion 71-17 expresses clear guidelines for determining when an "emergency" declaration is appropriate. According to the criteria described in the Opinion, an emergency exists when "sudden change brings hardship to a company, when a company is insolvent or when the condition of the company is such that its ability to maintain service pending a formal rate determination is in serious doubt." See also *RUCO*, in which the court stated that "interim rate making requires... an emergency situation, the posting of a bond, and a subsequent full rate case-in order to comport with the constitutional mandate that rates be just and reasonable."<sup>1</sup>

It is clear that recent sudden changes have dramatically affected global credit markets, impacting the operation of companies nationwide. Events unfolding even as the hearing in this case began illustrate the magnitude of the ongoing economic crisis. On the first day of the hearing, September 15, 2008, Lehman Brothers declared bankruptcy.<sup>2</sup> At the hearing, APS stated that they would be unable to issue a planned \$400 million equity issuance because the stock offering would have been below the book value of the Company.<sup>3</sup> Elsewhere, the record reflects news accounts describing the impending financial crunch, including one article entitled, "Ripple spreading in the financial crisis"<sup>4</sup> In sum, the record in this case reflects the extraordinary and uncertain economic times faced by consumers and businesses in Arizona and across the country.

<sup>1</sup> Residential Utility Consumer Office v. Ariz. Corp. Comm'n, 199 Ariz. 588, at 599, 20 P.3d 1169 at 1173 (Ariz. Ct. App. 2001).

<sup>2</sup> Tr Vol I, Page 130, lines 10-12.

<sup>3</sup> Tr. Vol. I, Page 66, lines 13-18.

<sup>4</sup> Tr Vol II, Page 416, line 17.

Given the recent state of the economy, and absent near-term rate relief, APS' bonds could be downgraded from investment to non-investment grade, which could bar the Company from accessing the credit markets, or make the procurement of credit prohibitively expensive.<sup>5</sup> In response to a letter from a Commissioner requesting information regarding the cost impact associated with a bond downgrade, APS filed exhibits demonstrating that such a downgrade to "junk bond" territory would result in higher financing costs across all categories of Company debt, totaling \$1 billion of additional costs over the next 10 years.<sup>6</sup> Almost as troubling as the financial impact to APS and its customers associated with a credit downgrade or inability to access credit markets, is the likelihood that such a status could seriously impair APS's ability to continue to build critical electric infrastructure and to deploy the next generation of renewable energy projects in Arizona. APS has assured the Commission that if interim rates are implemented, the earnings generated "would be reinvested in infrastructure and technology necessary to serve APS customers and reduce the need for external debt financing."<sup>7</sup>

This Commission expects the Company to be a major participant in renewable energy and transmission projects throughout its service territory, most of which will only come to fruition if the Company remains a credit-worthy counterparty to the developers of these projects. APS will also be required to invest significantly in traditional forms of energy generation to meet its expected load growth, as APS requires 5,000 megawatts of new resources by 2020. Despite these energy needs, APS has indicated that it will cut or postpone \$500 million of spending from its capital expenditure budget over the next four years and has cut its operations and maintenance budget by \$50 million. Therefore, in light of the requirement that APS continue to build new infrastructure and be a leader nationally in the production of renewable energy, we believe that the Company's ability to maintain the quality of service mandated by the Commission is in serious doubt under the imminent threat of a credit downgrade.

While we find that APS is experiencing an emergency, we wish to make it clear that we strongly disagree with APS that emergency or interim rate increases can be routinely implemented. We believe emergency rate increases should be sparingly utilized, and reserved for the most perilous situations.

Page 35:  
DELETE lines 1 to 5

Lines 12-13  
DELETE: "Although we do not believe that APS has demonstrated that an emergency exists currently, we"

AND INSERT: "We"

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<sup>5</sup> See October 17, 2008 APS Response to an October 8, 2008 letter from Commissioner Mayes.

<sup>6</sup> See pages 4 and 13, APS Exhibit 1, as noted in response to an October 3, 2008 letter from Commissioner Gleason.

<sup>7</sup> See APS' June 6, 2008 Motion, p. 6.

Page 35, After line 21, INSERT:

“Based on the above we find that Staffs alternative determination of an increase of \$65.2 million is reasonable and appropriate. This will result in a surcharge of \$0.00226 per kWh. This will increase the average APS residential customer’s bill by \$1.99 per month in the summer and \$1.46 per month in the winter. The emergency interim surcharge will be subject to refund pending a decision in APS’ permanent rate case.

Page 35, line 23 INSERT: “additional” after “believe”

Page 39, DELETE lines 1-2

Page 39, line 8, After “recession” INSERT:

“we find that an emergency exists, therefore,”

Page 39, line 8, After the first “reasonable” INSERT:

“to adopt the level of Staff’s alternative emergency interim rate increase and”

Page 40, line 20, INSERT NEW FINDINGS OF FACT:

“While APS has stated that it has responded to its current fiscal condition by postponing \$500 million in capital expenditures over the next four years, and has cut \$50 million from its operations budget, the Company has resisted additional cost savings measures, as outlined in a response to an inquiry from a Commissioner asking APS to detail its cost savings activities.<sup>8</sup>

In light of the fact that APS is experiencing an emergency for the second time since 2006, and is requesting that its customers pay additional rates prior to a complete investigation by this Commission of the prudence of the investments underlying its proposed permanent rate increase, we believe that it is in the public interest to require the Company to more closely scrutinize its operations and expenses and make additional cuts to these areas of its budget. We believe that the amount of budget cuts APS should target is at least \$20 million (annualized pre-tax), or 2.6 percent below its 2007 test year operating and maintenance expense. Adopting these measures provides an additional avenue for APS to improve its finances. Specifically, we believe APS should make use of several easily identifiable short term measures, to further buttress its finances and protect ratepayers until its pendant full rate case is completed. We decline to declare precisely how those cuts should be made, but find that the Company should consider cutting back its lobbying and advertising expenditures, paring back management compensation for 2009, imposing a temporary hiring freeze for all non-essential personnel, examining payroll overhead and implementing a freeze on increases to its dividend, among other measures. Such steps would be similar to those taken by corporations throughout the United States facing emergencies

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<sup>8</sup> These figures were provided to the Commission in this docket in response to a November 19, 2008 letter from Commissioner Mayes.

during these difficult economic times. Given its request for an emergency rate increase, we find that APS should be prepared to adjust its practices from business as usual to appropriately reflect the severity of the emergency it has identified. Further, the Company should file a report detailing the cost saving measures taken and associated savings achieved in this Docket no later than March 18, 2009, for Commission review.

In this proceeding, APS has consistently pointed to its financial metrics as demonstrative of the Company's deteriorating condition. Because APS' finances have been made a central issue in this proceeding, we believe it is necessary that APS better inform this Commission of its interactions with credit ratings agencies. Accordingly, APS should be required to file all communications between APS/Pinnacle West personnel/representatives and the representatives of credit ratings agencies, including notes, emails, phone messages, presentations (inclusive of memos and PowerPoint), and meeting notes, and that APS should memorialize the substance of any meetings and phone calls between APS and ratings agency representatives, effective the date the Commission votes on this Order. APS shall file all such communications as a compliance item in this docket, until the conclusion of its general rate case, and thereafter, with Docket control every six months, beginning January 1, 2010."

Page 40, line 26, DELETE: "No emergency exists to warrant the implementation of interim"  
AND INSERT: "An emergency exists which warrants the implementation of emergency"

Page 40, line 28, DELETE: "denied without prejudice" AND INSERT: "approved as discussed herein"

Page 41, lines 2 & 3, DELETE: "Company's Motion for an Interim Base Rate Surcharge is hereby denied without prejudice." AND INSERT: "Company is hereby granted an emergency interim base rate surcharge of \$0.00226 per kwh that shall become effective with all bills issued after December 31, 2008."

Page 41, line 4, INSERT NEW ORDERING PARAGRAPHS:

"IT IS FURTHER ORDERED that this surcharge shall not apply to E-3 and E-4 low income customers, E-36 customers, and the solar rate schedules Solar-2 and SP-1.

IT IS FURTHER ORDERED that Arizona Public Service Company shall notice all its customers, in a form acceptable to Staff, of this surcharge by December 31, 2008.

IT IS FURTHER ORDERED that Arizona Public Service Company shall post a \$10 million bond or sight draft letter of credit and provide the original to the Commission's Business Office and file copies in Docket Control as a compliance item in this Docket, prior to December 31, 2008, and such bond or sight draft letter of credit shall remain in effect until a final order is issued by the Commission in Arizona Public Service Company's pending permanent rate case."

Page 42, line 4, INSERT NEW ORDERING PARAGRAPHS:

“IT IS FURTHER ORDERED that Arizona Public Service Company shall examine its operations and expenses and employ short term measures to further buttress its financial position. Arizona Public Service Company shall target additional cuts to its operations and expenses of at least \$20 million, or 2.6 percent below its 2007 test year operations and maintenance expense. Arizona Public Service Company shall consider items such as cutting back its lobbying and advertising expenditures, paring back management compensation for 2009, imposing a temporary hiring freeze for all non-essential personnel, examining payroll overhead and implementing a freeze on any increases to its dividend in 2009, among other possible measures.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file a report with the Commission’s Docket Control as a compliance item in this docket, detailing the cost cutting measures taken and associated savings, no later than March 18, 2009 for Commission review.

IT IS FURTHER ORDERED that APS shall reinvest the earnings resulting from the additional interim base rate surcharge and any monies achieved from cost savings measures taken pursuant to this Order, in infrastructure and technology necessary to serve APS customers and reduce the need for external debt financing.

IT IS FURTHER ORDERED that APS shall file all communications between Arizona Public Service Company/Pinnacle West Capital Corporation personnel/representatives and the representatives of credit ratings agencies, including notes, emails, phone messages, presentations (inclusive of memos and PowerPoint), and meeting notes.

IT IS FURTHER ORDERED that Arizona Public Service Company shall memorialize the substance of any meetings and phone calls between Arizona Public Service Company/Pinnacle West Capital Corporation personnel/representatives and ratings agency representatives, for past communications and on an ongoing basis, effective the date the Commission votes on this Order.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file all such communications as a compliance item in this Docket. APS shall file all currently existing communications within 10 days of the effective date of this Decision and shall file future communications on a monthly basis until the conclusion of its general rate case. Thereafter, APS shall make such filings on a six month basis, with the first filing due on January 1, 2010.”

Make all conforming changes.