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Docket No.
RE-000000-00-0377

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Arizona Corporation Commission

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TO: THE COMMISSION

FROM: Legal and Utilities Divisions

JAN CORP COMMISSION
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NOV 21 2001

DATE: October 29, 2001

DOCKETED BY [Signature]

RE: IN THE MATTER OF THE APPROVAL OF A SETTLEMENT AGREEMENT BETWEEN RESIDENTIAL UTILITY CONSUMER OFFICE AND THIS COMMISSION OF LITIGATION OVER THE ENVIRONMENTAL PORTFOLIO STANDARD CV2001-005973 AND CV 2000-013045.

Earlier this year, the Commission enacted A.A.C. R14-2-1618, the environmental portfolio standard ("EPS"). The EPS is a rule that requires electric utilities to generate a set percentage of their portfolios from renewable resources, such as solar, wind, biomass, or landfill gas.

The Residential Utility Consumer Office ("RUCO") appealed the Commission's EPS Decisions to the Superior Court. This action has been pending since July of last year.

In September, representatives of the Commission's staff ("Staff") and RUCO began to explore possible ways to settle this litigation. RUCO and Staff reached an Agreement in principle ("the Agreement") subject to the Commission's approval. The Agreement contains the following four points:

1. The utilities' surcharge tariffs currently require either rate review filings or that the utilities file information regarding revenues, expenses, and assets related to compliance with the EPS. All such rate reviews/information filings will be docketed items in which RUCO will be permitted to intervene, as long as RUCO's intervention is not inconsistent with A.R.S. § 40-464.
2. RUCO will be permitted to request relief from the Commission based on its analysis of rate review/information filings.
3. EPS surcharges will remain interim until the Commission makes findings of fair value in proceedings in which RUCO has notice and an opportunity to be heard.
4. If RUCO is aggrieved by the results of rate review/information filing dockets, the Commission will not seek to bar RUCO from re-raising the objections that

are the subject of the current appeals, as long as RUCO's arguments are not inconsistent with A.R.S. § 40-252.

RUCO has stated that, if the Commission will approve the Agreement (a copy of which is attached), RUCO will withdraw its appeals.

Staff recommends that the Commission approve the Agreement and authorize the Legal Division to sign it on the Commission's behalf. These four items are all essentially procedural in nature. The benefits to the public of implementing the EPS are substantial, and RUCO's requests do not interfere with that implementation.

A detailed discussion of this matter follows.

EVOLUTION OF THE EPS – A FACTUAL HISTORY

Promoting renewable sources of energy, including solar, geothermal, hydro, and wind, is vital to ensure Arizona's energy future. The EPS requires electric utilities to broaden their portfolios, thereby decreasing their dependence on fossil fuel sources. This objective is vital given the growing tensions in the Middle East and the volatile fluctuations of natural gas prices in the past few years. The Commission found the EPS to be in the public interest.

On May 4, 2000, the Commission issued Decision No. 62506 approving the EPS and referring the EPS for rulemaking. On February 8, 2001, the Commission formally approved the EPS Rules in Decision No. 63364 (which was later modified in Decision No. 63486 issued on March 29, 2001). The EPS Rules require 0.2 percent of total retail energy sold by each Load-Serving Entity (LSE) to be generated from new solar resources or environmentally friendly renewable solar technologies. The portfolio percentage increases on January 1 of each year after 2001, so that by 2007 LSEs must derive 1.1 percent of their total retail sales from qualifying sources. The annual increase could be frozen before January 1, 2005 if the cost of environmental portfolio electricity has not declined to a Commission-approved cost/benefit point.

The Commission also developed a means for utilities to recover the costs of the EPS. The environmental portfolio surcharge (EPS surcharge) would be \$0.000875 per kWh on the customer's monthly bill. There is a surcharge cap of \$0.35 per month for residential customers, and \$13 per month per meter or per service for all non-residential customers, except for those non-residential customers using at least 3,000 kWh per month, who will be subject to a cap of \$39 per month. Under Decision No. 63364, affected LSEs are required to file tariffs to implement these surcharges.

The Commission approved several of these tariffs on February 8, 2001. These tariffs include Decision Nos. 63353 (TEP), 63354 (APS), 63355 (Trico Electric Cooperative), 63356 (Duncan Valley Electric Cooperative), 63357 (Graham County Electric Cooperative), 63358 (Navopache Electric Cooperative), 63359 (Mohave County

Electric Cooperative), 63360 (Citizens Communications Company) and 63361 (Sulphur Springs Valley Electric Cooperative). All of the tariff orders listed above establish the EPS surcharge as interim, pending a proceeding in which the Commission would make a fair value determination. Each LSE would either file an application for a rate review proceeding or would file sufficient information for a fair value determination. Such information would include the following:

1. Total revenue for the first twelve months after implementing the surcharge.
2. Total actual operating expenses for the first twelve months after implementing the surcharge.
3. The value of all assets, listed by major category, used for the first twelve months after implementation of the surcharge to provide electric service to customers. The applicant should specifically identify the assets and their value, acquired to comply with the EPS.

The tariff orders also provide for the Commission to determine how the EPS surcharge impacts rates and allow the Commission to make appropriate findings and rate determinations, including true-up, refund, or setting permanent rates.

CV2001-005973 and CV 2000-013045 – A PROCEDURAL HISTORY

RUCO filed its original and amended Complaints on July 13, 2000 and October 2, 2000 challenging the Commission's approval of the EPS in Decision No. 62506. The Commission timely filed its answers to the Complaint and the amended Complaint. RUCO filed a sister complaint in Superior Court on April 9, 2001, challenging the Commission's authority to promulgate the EPS Rules in Decision No. 63364. On June 8, 2001, the Commission filed an answer to RUCO's sister complaint. RUCO and Staff were subsequently able to work out an Agreement in principle, subject to the Commission's approval. Under the settlement, RUCO would agree to withdraw its pending appeals of the EPS upon the Commission approving the four proposed procedural conditions listed above.

RUCO's proposal arises out of RUCO's concern that the rate review filings will be handled informally, i.e., will not be docketed items. If a matter is not docketed, RUCO often has no way to know of its existence. RUCO would like to be assured that the rate reviews referred to in the EPS tariff orders will be docketed items, thereby providing RUCO with notice and an opportunity to present evidence and make recommendations to the Commission. RUCO believes that these clarifications are necessary to ensure that it will be able to effectively advocate on behalf of the residential customers of Arizona in proceedings where the Commission finds fair value.

By contrast, Staff believes that the procedural protections sought by RUCO are already embodied in either the EPS tariffs or existing law. However, to the extent that

RUCO's proposal serves to clarify the applicable procedures, all parties will benefit. Furthermore, Staff believes that none of the proposed conditions substantively changes the structure, implementation, or design of the EPS Rules, or the LSEs' associated tariff orders. For all of the above reasons, Staff believes that RUCO's proposed conditions are reasonable and recommends that the Commission approve the Agreement.

If the Commission accepts the Agreement, RUCO will withdraw its appeals and ask the court to dismiss them with prejudice. Each party would bear its own costs and attorneys' fees.

CONCLUSION

The EPS is beneficial, vital, and essential if we are to encourage the continued development of renewable sources of energy. The Agreement does not compromise the substance of the EPS, and clarifies the nature of RUCO's participation in future proceedings. Therefore, Staff recommends that the Commission approve the Agreement and authorize the Legal Division to sign it on the Commission's behalf.

JDG/jdg

SETTLEMENT AGREEMENT

The undersigned Parties stipulate and agree to the following settlement provisions in connection with the pending lawsuits CV2001-005973 and CV2000-013045 before the Superior Court entitled Residential Consumer Utility Office v. The Arizona Corporation Commission. Both actions were consolidated with CV1997-003748 (Tucson Electric Power Company v. The Arizona Corporation Commission). This Agreement is intended to settle issues relating to CV2001-005973 and CV2000-013045 only, and not other issues in the consolidated proceeding.

1. Parties to the Agreement.

Parties to this Agreement are the Residential Utility Consumer Office ("RUCO") and the Arizona Corporation Commission ("Commission").

2. Statement of Intentions and Admissions.

The purpose of this Agreement is to resolve contested matters in a manner consistent with the public interest. Nothing contained in this Agreement is an admission by any Party that any of the positions taken, or that might be taken by each in formal proceedings, is unreasonable. In addition, acceptance of the Agreement by any of the Parties is without prejudice to any position taken in these proceedings.

3. Terms of the Agreement.

Through a series of Decisions, the Commission approved an Environmental Portfolio Standard ("EPS") and enacted Rules to implement the EPS. The Rules established a surcharge to pay for the EPS, and required affected utilities to file tariffs to implement these surcharges. The Commission approved several of these tariffs on

February 8, 2001. RUCO appealed the Commission's Decisions approving the EPS and the Rules through a series of lawsuits, which were later consolidated as described above. The Parties have entered into settlement negotiations and agree to the following terms:

A. The utilities' surcharge tariffs currently require either rate review filings or that the utilities file information regarding revenues, expenses, and assets related to compliance with the EPS. All such rate reviews/information filings will be docketed items in which RUCO will be permitted to intervene, as long as RUCO's intervention is not inconsistent with A.R.S. § 40-464.

B. RUCO will be permitted to request relief from the Commission based on its analysis of rate review/information filings.

C. EPS surcharges will remain interim until the Commission makes findings of fair value in proceedings in which RUCO has notice and an opportunity to be heard.

D. If RUCO is aggrieved by the results of rate review/information filing dockets, the Commission will not seek to bar RUCO from re-raising the objections that are the subject of the current appeals, as long as RUCO's arguments are not inconsistent with A.R.S. § 40-252.

4. Limitations.

The terms of this Agreement apply solely to and are binding in the context of the provisions and results of this Agreement and none of the positions taken herein by any of the Parties may be referred to, cited or relied upon by any Party in any fashion as precedent or otherwise in any proceeding before this Commission or any other regulatory agency or before any court of law for any purpose except in furtherance of the purposes and results of this Agreement.

5. Dismissal of pending action.

Upon approval by the Commission, and execution of the Agreement by the Parties, RUCO will file a motion to dismiss its actions relating to CV2001-005973 and CV2000-013045 with prejudice.

6. Each party will bear its own costs and attorneys' fees.

DATED this _____ day of October, 2001.

ARIZONA CORPORATION COMMISSION

By: _____

RESIDENTIAL CONSUMER UTILITY OFFICE

By: _____