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BEFORE THE ARIZONA CORPORATION COMMISSION

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IN THE MATTER OF THE APPLICATION OF THE SOLAR ALLIANCE FOR A DECLARATORY ORDER THAT PROVIDERS OF CERTAIN SOLAR SERVICE AGREEMENTS WOULD NOT BE PUBLIC SERVICE CORPORATIONS	DOCKET NO. E-20633A-08-0513 **SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT'S RESPONSE TO STAFF'S REPORT**

Salt River Project Agricultural Improvement and Power District ("SRP") files this Response to the Staff Report pursuant to the Procedural Order dated March 6, 2009.

Preliminary Statement

As a prefatory matter, SRP agrees with the Staff conclusion that a hearing is necessary and appropriate in this docket. Through the hearing process, the parties can explore the facts, determine who the underlying parties to this application are, determine issues of law and policy, and work on recommendations for the right approach.

In this response SRP expands a little on the law of what is a public service corporation. This application brings to mind the saying "hard cases make bad law". Encouraging solar energy development and the receipt of all available tax incentives is an important objective. Yet, it should not be reason to abandon the system of citizen protection that has been developed over the past 100 years in Arizona. While SRP manages its own solar program, it must rely on the Commission to provide appropriate oversight to generation providers who might seek to serve in the SRP

distribution area.

As referenced in the Staff Report, the answer is to devise an approach that complies with Arizona law, protects electric consumers, and yet still provides encouragement to the development of solar energy. While SRP is committed to working with the Solar Alliance members, we question whether the SSA model is necessary to achieve the benefits that they offer (new capital for renewable projects, the ability to monetize tax credits, a commitment to a renewable technology). To date, over 2000 SRP customers have participated in SRP's solar incentive program, but none have received an incentive for a system which utilizes the SSA model.

Solar Alliance Members Are Public Service Corporations

As pointed out in the Staff Report, we do not have a full record upon which to make definitive determinations. We have none of the actual businesses seeking an exemption before the Commission. We only have a general description of the business plans, and then with a proviso that all members may not meet all of the elements.

But, from the information that we do have, it appears clearly that the Solar Alliance members are public service corporations. Their business model is to own and operate generating facilities, and to sell the output to their customers. These companies hold themselves out generally to those who meet their customer criteria. True, the output is from scattered generating facilities, but this is a distinction without a difference.

The Arizona courts have established a two-part test for determining whether an entity is a public service corporation. *See Southwest Transmission Coop., Inc. v. Arizona Corp. Comm'n*, 213 Ariz. 427, 431, 142 P.3d 1240, 1244 (Ariz. Ct. App. 2006). First, the courts will consider whether the entity falls within the definition of "public service corporation" set forth in Article 15, Section 2 of the Arizona Constitution. *Id.* (citing *Southwest Gas Corp. v. Ariz. Corp. Comm'n*, 169 Ariz. 279,

285, 818 P.2d 714, 720 (Ariz. Ct. App. 1991)). Next, the courts will "evaluate whether the entity's business and activity are such 'as to make its rates, charges, and methods of operations as a matter of public concern,' by considering the eight factors articulated in *Natural Gas Serv. Co. v. Serv-Yu Coop....*" *Id.* (quoting *Natural Gas Serv. Co. v. Serv-Yu Coop*, 70 Ariz. 235, 237-8, 219 P.2d 324, 325-26 (Ariz. 1950)). The Solar Alliance members appear to meet both parts of the test.

1. Solar Alliance Members Fit The Constitutional Definition Of Public Service Corporation.

The Arizona Constitution defines "public service corporations" as "[a]ll corporations other than municipal engaged in furnishing gas, oil, or electricity for light, fuel, or power...." Ariz. Const., Art. 15, § 2.

In its application Solar Alliance states that "electricity is furnished to the customer as a result of the SSA ["Solar Services Agreements"]...." Application at 9. The Application further explains that customers "purchase the full output generated by the facility at agreed upon prices" and are charged "based on the power actually produced by the solar facility...." Application at 7.

This sale of electricity, which is purportedly part of a "package of services" provided under the SSA,[1] allows the customer to "purchase less electricity from the electric grid." Application at 9. In other words, customers are buying electricity under SSAs in order to reduce their purchase of the same product from other utilities. Solar Alliance recognizes this very point in its application:

> an SSA is generally not meant to supply all of the customer's power, or at all times of the day. Therefore, the customer remains connected to the public utility grid, and can *receive power from its regulated electric utility* at any time.

Application at 12 (emphasis added).

[1] For a complete discussion of this "package of services," see Part II.A.2.a, *infra*.

Despite its attempt to distinguish its members from those regulated by the Commission, Solar Alliance admits they each provide the same service. Solar Alliance members are in the business of furnishing electricity to customers, displacing, at least in part, the services provided by other utilities, and therefore constitute a "public service corporation" under the Arizona Constitution.

2. Electricity Sales Made By Solar Alliance Members Are "Clothed With A Public Interest."

Arizona courts have determined that, in addition to the constitutional requirement, an entity must also be engaged in business activities that are a matter of public concern in order to qualify as a public service corporation. *See, e.g. Southwest Transmission Coop., Inc. v. Arizona Corp. Comm'n*, 213 Ariz. 427, 431, 142 P.3d 1240, 1244 (Ariz. Ct. App. 1991); *General Alarm v. Underdown,* 76 Ariz. 235, 238, 262 P.2d 671, 672-73 (Ariz. 1953); *Natural Gas Serv. Co. v. Serv-Yu Coop.*, 70 Ariz. at 237-8, 219 P.2d at 325-26. The theory behind this requirement is that:

> To be a public service corporation, its business and activity must be such as to make its rates, charges, and methods of operations a matter of public concern. It must be, as the courts express it, clothed with a public interest to the extent clearly contemplated by the law which subjects it to government control. Free enterprise and competition is the general rule. Governmental control and legalized monopolies are the exception and are authorized under our constitution only for that class of business that might be characterized as a public service enterprise. The theory is that the right to public regulation and protection outweighs the customary right of competition.

Arizona Corp. Comm'n, 108 Ariz. at 321, 497 P.2d at 819 (quoting *General Alarm,* 76 Ariz. at 238, 262 P.2d at 672-73; *see also Southwest Gas Corp. v. Arizona Corp. Comm'n*, 169 Ariz. at 286, 818 P.2d at 721.

In making this public interest determination, courts have been guided by eight factors first articulated in *Serv-Yu*:

> (1) What the corporation actually does; (2) A dedication to public use; (3) Articles of incorporation, authorization, and purposes; (4) Dealing with the service of a commodity in which the public has been generally held to have an interest; (5) Monopolizing or intending to monopolize the territory with a public service commodity; (6) Acceptance of substantially all requests for service; (7) Service under contracts and reserving the right to discriminate is not always controlling; (8) Actual or potential competition with other corporations whose business is clothed with public interest.

Serv-Yu, 70 Ariz. At 237-38, 219 P.2d at 325-26. An entity need not satisfy each of the eight factors in order to qualify as a public service corporation. *See Southwest Transmission Coop., Inc.*, 213 Ariz. at 432, 142 P.2d at 1245; *Southwest Gas Corp.* 169 Ariz. at 287, 818 P.2d at 722.

In attempting to distance itself from the application of the *Serv-Yu* criteria, Solar Alliance first argues that the sale of energy is only incidental to the package of services provided under the SSA. But, the Application is devoid of facts from which this conclusion could be drawn. Second, Solar Alliance argues that serving a single customer does not trigger a public interest concern, ignoring the fact that the business of a Solar Alliance member (presumably) will be to provide service to multiple customers, producing a significant footprint on the electric industry

a. Electric Service is not incidental to a "package of services"

Solar Alliance does not dispute the fact that its members are furnishing electricity to retail customers. *See* Application at 7, 9 ("electricity is furnished to the customer as a result of the SSA...."). Nor does Solar Alliance deny a general public interest in the sale of electricity. Application at 12 ("electricity has been considered a service in which the public has an interest"). Yet, in its discussion of two *Serv-Yu* factors ("what the corporation actually does" and "dealing with the service of a commodity in which the public has been generally held to have an interest"), Solar

Alliance relies heavily on the position that its members are primarily furnishing not electricity, but rather a "package of services," of which electricity sales are merely "incidental." Application at 2, 7, 9-15.

The argument is but an attempt to conform SSA services to a line cases holding that the public does not have an interest in a public service commodity, if the provision of the commodity is only incidental to an entity's primary business activities. *See* Application at 12 (citing *Southwest Transmission Coop.,* 213 Ariz. at 432; *Nicholson,* 108 Ariz. at 321). In *Nicholson*, the court declined to characterize the owner of a mobile home park as a public service corporation because of its provision of water to the park's individual tenants. The court found the plaintiffs were "in the business of renting trailer spaces" and that furnishing water was "in support and incidental" to that business. *Nicholson,* 108 Ariz. at 321, 497 P.2d at 818. For that reason, the court determined that the park owner did not devote its private property to public service to a degree sufficient enough to summon the public interest.

The same "incidental" argument cannot be applied to Solar Alliance members. The so-called "package of services" that Solar Alliance members provide under the SSAs include:

> Analysis of the customer's load characteristics, sizing and placement of the solar facility on the customer's premises, financing the costs of acquiring the solar facility, monetizing tax credits related to the solar facility, ongoing maintenance of solar facility[sic], and electric output of the solar facility.

Application at 7. However, none of the foregoing services would be necessary but for the fact that Solar Alliance members are furnishing electricity to retail customers. These services are specifically designed to support the sale of electricity by SSA providers. Would their customers have any interest in solar facility placement or maintenance if they did not have some interest in the output of the facilities?

Significantly, the rest of the package is not priced independently from the sale of energy, but rather depends on the amount of energy sold. Application at 7 ("customer charges are computed based on power actually produced by the solar facility."). In fact, charges for all of these services are bundled with the charge for energy, are priced at a single kW-hour rate, and may be influenced by the price paid for electricity from the local utility. Application at 7-8. In this way, Solar Alliance members are no different than other electric service providers. The owner of a gas-fired generator, for example, must engage in siting, financing, maintenance, and operation functions, the costs of which services are included in price of power and energy generated by the plant.

Solar Alliance attempts to distinguish itself from other generators by arguing that an SSA "is largely a *financial* instrument that enables customers to finance a solar facility to serve a portion of its electric need." Application at 12 (emphasis in the original). Yet, it is not clear what customers are financing according to Solar Alliance's description of services provided under the SSA. Solar Alliance explains that the SSA providers themselves finance, install, own, maintain and operate the facilities located on the customer's premise. Application at 7.

The so-called "package of services" is designed to make electricity sales possible, and is included in the cost of the energy sold. It is therefore inaccurate for Solar Alliance to argue that the sale of energy is but an incidental element in the package of services offered under the SSAs. SSA members are actually selling electricity to retail customers. As discussed more fully below, the resulting impact of these sales on other utility customers is significant enough to raise public concern.

b. Solar Alliance ignores the true public interest in its members' business activities

Under the *Serv-Yu* factors, an entity must deal in a commodity in which the public generally has an interest, and must dedicate its property to public use in order

to qualify as a public service corporation. *Serv-Yu*, 70 Ariz. at 237-38, 219 P.2d at 325-26. Service to the public at large, and the acceptance of all service requests, are indicia of, but not a requirement to qualify as, a public service corporation. *Nicholson*, 108 Ariz. at 319, 497 P.2d at 818. Courts have also looked to whether the entity in question would compete with other public service corporations in a manner that would unfairly burden the public with stranded costs. *Eastern Shore Natural Gas Co. v. Delaware Public Serv. Comm'n.*, 635 A.2d 1273 (Dela. 1993); *In the Matter of Eastern Shore Natural Gas Co.*, 561 A.2d 561 (N.J. 1989); *PW Ventures, Inc. v. Nichols*, 533 So.2d 281 (Fla. 1988).

As stated above, Solar Alliance recognizes a general public interest in electricity as a public service commodity. In this case, the public has a particularized interest in the electricity generated and sold under the SSAs. The electricity sales made under SSAs displace those purchases that customers would normally make from their host utility. SSA customers would not be contributing to the utility's fixed costs during those periods when energy sales under SSAs take place, but would remain reliant on the host utility any time the solar facilities could not cover the costumer's load. Application at 14. The local utility must therefore plan and build its system taking into account the SSA customers' total load, regardless of how "intermittently" they are served under SSAs. Application at 17. As a result the burden of paying the utility's fixed costs during the SSA sales could fall disproportionately to the utility's other customers.

Additionally, when solar output exceeds a customer's load, the excess is made available to the public through the host utility. Application at 7, n.4. The host utility is forced to absorb this additional energy, whether or not it might be needed, potentially creating additional operational and reliability costs, which again become the responsibility of the other utility customers as a whole.

Solar Alliance's view of the "property" at issue in this case is too narrow. When arguing that SSA providers do not dedicate private property to public use, Solar Alliance focuses on the solar "facilities" themselves, Application at 9, and a "select and restricted group of customers." Application at 10. It argues that "Unlike a public service corporation that dedicates property to serve the public at large, the property through which an SSA provider provides service is only dedicated to the individual customer on whose site the solar facility resides." *Id.*

However, the fact that energy will be generated by SSA providers on private property is not unique. The same could be said for many generation plants, the owners of which do not escape regulation. Moreover, an entity need not actually offer services to the public at large in order to qualify as a public service corporation.

In *Nicholson*, the Arizona Supreme Court recognized that an entity need not be a public utility required to serve the public at large in order to qualify as a public service corporation:

> Clearly plaintiffs cannot be classified as a public utility since they only serve members of their own mobile trailer park. Members of the neighboring community would have no right to demand water service. The question here, though, is the status of plaintiffs as a public service corporation. In Trico, we distinguished this from a utility and held that such a classification was "something less than a fullfledged 'public utility.'" That "something less" was the requirement to serve the public at large with a commodity having a public interest. Thus where a corporation, association, etc. otherwise meets the definition of a public service corporation, the fact that the general public has no right to demand such service is not material.

Nicholson, 108 Ariz. at 319, 497 P.2d at 818. As explained above, the *Nicholson* court found the park owner's provision of water service to its own tenants did not place its private property in the realm of public interest because that service was incidental to the park's primary business purpose. Here, the sale of solar energy *is* the purpose of the SSAs.

Courts have found a public interest in the regulation of "private" sales of a public service commodity if, as a result of such sales, other customers of the utility will pay higher rates to cover stranded costs. *Eastern Shore Natural Gas Co. v. Delaware Public Serv. Comm'n.*, 635 A.2d 1273 (Dela. 1993); *In the Matter of Eastern Shore Natural Gas Co.*, 561 A.2d 561 (N.J. 1989); *PW Ventures, Inc. v. Nichols*, 533 So.2d 281 (Fla. 1988). There, the court recognized a future "potential for adverse competition which may affect the public interest." *Id.* The Florida Supreme Court recognized this problem in *PW Ventures, Inc. v. Nichols*:

> The effect of this practice would be that revenue that otherwise would have gone to the regulated utilities which serve the affected areas would be diverted to unregulated producers. This revenue would have to be made up by the remaining customers of the regulated utilities since the fixed costs of the regulated systems would not have been reduced.

PW Ventures, Inc. v. Nichols, 533 So.2d 281 (Fla. 1988).

These courts have found that an entity cannot escape regulation merely by claiming they do not serve the general public or accept substantially all claims for service.

> It is impossible for the Public Service Commission to monitor and effectively control the extent of competition in the provision of traditionally regulated commodities if an unregulated firm with no obligation to serve all similarly situated customers and without general obligation to provide service to all who require it in a specific territory can essentially enter the public utility business and "cherry pick" or "cream skim" away the existing utility's highest volume customers.

Eastern Shore Natural Gas Co. v. Delaware Public Serv. Comm'n., 635 A.2d 1273 (Dela. 1993); *see also In the Matter of Eastern Shore Natural Gas Co.*, 561 A.2d 561 (N.J. 1989).[2]

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[2] Arizona Courts have not addressed this issue directly. In *Southwest Gas Corporation*, the court declined to consider this issue because of a lack of evidence in the record. *Southwest Gas Corp.*, 169 Ariz. at 287, 818 P.2d at 722.

Solar Alliance's focus on SSA providers' service to individual customers is misguided. Its Application does not ask the Commission to disclaim jurisdiction over a single SSA provider. Rather, Solar Alliance asks for a preemptive exemption from regulation for a whole class of energy sales. It claims utilities will not lose a single customer as a result of the SSA providers entry into the electricity market. However, it does not look at the aggregate effect that its blanket, and open-ended exemption, would have on other utility customers across the state.

SRP does not deny the importance of developing sources of renewable energy. It has and will continue to actively support the growth of solar power in the State of Arizona. However, a blanket exemption for SSA providers could have far-reaching implications not addressed by the Application. Solar Alliance provides no information regarding the number of members it anticipates doing business in Arizona, nor the number of customers those members expect to serve. In light of the stated purpose of the Application, *i.e.,* to encourage the growth of distributed solar power, Application at 3, such information is critical in assessing the effect of SSA sales throughout the state. The unique blanket exemption from regulation that Solar Alliance requests cannot be based on speculative assertions, but rather must be grounded in substantial evidence.

Conclusion

SRP recognizes that the members of the Solar Alliance bring value to Arizona. They bring a source of capital and the ability to monetize tax credits. And most importantly, they are advocates of a non-carbon technology. To date, however, SRP has not seen a reason to change existing law. No SRP customer has received an incentive for a solar system which utilizes the SSA model. Rather, a number of providers have located in the SRP area utilizing lease agreements with customers.

SRP agrees with Staff. The record needs to be more fully developed in a hearing so that we can better understand the need for the exemption and discuss potential options to resolve the issues in accordance with the law. Moreover, it would be helpful to have an actual business applicant become a part of this proceeding. This would allow the ACC to receive evidence and testimony regarding a tangible set of facts to facilitate the appropriate legal analysis. During the hearing process, SRP is hopeful that the parties can develop options to bring to Arizona the benefits that these businesses offer, within the bounds of the law, consistent with the goals of consumer protection.

DATED this 17th day of April, 2009.

JENNINGS, STROUSS & SALMON, P.L.C.

By [signature], for

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