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Direct Line DOCKET CONTROL

May 15, 2009

Arizona Corporation Commission
DOCKETED

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Bob Stump
Commissioner
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007-2996

DOCKETED BY

Re: Your Letter Dated April 23, 2009; Docket No. E-01345A-08-0172

Dear Commissioner Stump:

In order to provide a clear response to the letters that have been received from you and other commissioners regarding the Arizona Public Service Company ("APS" or "Company") line extension policy ("Service Schedule 3"), we thought it would be helpful to provide some background regarding the purpose of line extension policies generally and the evolution of the APS policy specifically.

Line Extension Policies

Line extension policies in some form exist throughout the utility business world and are used by municipalities as well as regulated utilities to govern the extension of service to new customers or to existing customers who require increased levels of service. Quite simply, extension policies are an attempt to recognize that it generally costs more to serve new customers than existing customers.

Schedule 3 in effect prior to 2007

Prior to Decision No. 69663, dated June 28, 2007, APS's line extension policy, for the most part, contained the same provisions as when it was originally implemented in 1954. As you know, that policy provided free extensions for up to 1000 feet, but only for certain customers and under certain conditions. As it was, the 1000 foot allowance was among the most generous in the country (TEP for example, allowed only 500 feet). Importantly, the "1000 foot free" provision applied only to individuals or small groups of permanent residential customers who requested line extensions for service to homes. **The "1000 foot free" provision did not apply to residential subdivision developers or commercial customers.**

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For the single permanent residential (or similar) customer, the policy applied as follows:

- Free extensions were allowed for distances up to 1000 feet, provided the estimated extension cost was under \$25,000.
- For individual extensions that were over 1000 feet but under 2000 feet and under \$25,000, the customer advanced the cost of the extension for the distance over 1000 feet. The advance was potentially refundable, but only if additional customers connected to the original extension within 5 years.
- If the individual extension was over 2000 feet or over \$25,000, the “free footage” provision did not apply. Such extensions were subject to generally the same type of funding requirements that applied to commercial customers or real estate developers.

Decision No. 69663

In the rate case application that ultimately resulted in Decision No. 69663, dated June, 2007, APS proposed significant changes to Service Schedule 3. These revisions included moving away from the free footage and economic feasibility study models in an attempt to simplify the administration of the service schedule. In lieu of free footage allowances and economic feasibility studies, APS proposed that the extension policy be based on equipment allowances. When the cost of an extension exceeded the allowance, the customer was required to provide a refundable extension allowance. In Decision No. 69663, the Company’s proposals were adopted essentially on an interim basis (Revision 9 of Schedule 3). However, the Decision also ordered APS to refile Schedule 3 and remove **all** provisions regarding free footage, equipment allowances, economic feasibility studies, and refunds.

Decision No. 70185

Decision No. 70185, dated February 27, 2008, approved the revisions to Schedule 3 that Decision 69663 had required. The Decision also provided for a transition plan from the previously effective versions of Schedule 3 and “grandfathered” customers residing on tribal lands to the version of Schedule 3 that included the free footage allowance. This new revision to Schedule 3 (Revision 10) became effective February 27, 2008 and remains in effect today.

Questions from Commissioner Stump Letter

1. *What cost would consumers incur if the Commission were to re-instate the 1000 foot free-line extension?*

Over the last 5 year period, APS saw approximately 4,870 individual extension projects under 1000 feet with a total cost of approximately \$45 million. As explained in response to Commissioner Kennedy's letter on this subject, this approximately \$9 million per year of what would be treated as revenues under provisions of the proposed settlement would have to be made up by higher rates to APS customers.

2. *Should there be a cap on the amount a utility can charge the development for the extension?*

As noted above, the 1000 foot allowance never applied to residential developments -- it applied only to individual permanent customers. Under APS's currently approved Service Schedule 3, developers are charged the estimated cost of the facilities to serve the development. Because of the large number of factors that influence the construction cost in a development (e.g., development density, size of homes, size of development, terrain, and construction difficulty), it would not be pragmatic to cap the amount that can be charged. Moreover, the amount incurred by APS above the cap for the extension to that developer would have to be recovered from all customers in the form of higher rates.

3. *If a utility were to put in a line extension, is there a benefit to all users in that extension area, including the utility and its customers?*

When developing cost estimates in accordance with Service Schedule 3, APS recognizes that some extensions provide system improvements, which benefits both the utility and other customers. In such cases, the customer requesting the extension is not charged for the full cost of the extension. Rather, a "system planning" cost is calculated and deducted from the extension cost to determine the amount for which the customer should fairly be responsible.

4. *If a developer were to put in the extension, would the developer be subsidizing all development which occurs later?*

No. Please see the response to the previous question.

5. *What policies, if any, could be put into place to re-pay the initial developer for the 1000 foot free-line extension?*

As previously indicated, developers have never been eligible for a 1000 foot free extensions. In the case of individual residential applicants for service, the first customer connected could

Bob Stump
Commissioner
May 15, 2009
4

receive a partial refund under the previous versions of Schedule 3 if additional customers were connected using the same facilities during the first five years following that initial customer's advance.

6. *What is the average cost to a developer to put in the line extension?*

The average cost can vary significantly as noted above. For planning purposes, APS assumes a cost of \$2,300 per lot for high density single family residential developments. This planning estimate generally reflects the costs "inside the fence" of the subdivision and excludes system costs such as backbone feeders and substations. These latter costs are not covered by Schedule 3 and are borne by all APS customers.

7. *What is the average cost to an individual homeowner to put in the line extension?*

The cost can range from a few thousand dollars for short extension to tens of thousands for a lengthy extension in rugged territory. Over the last 5 years, APS has processed approximately 4,870 work orders for individual residential extensions. The average of cost of these extensions was approximately \$9,200.

I hope we have clarified several issues you have raised regarding APS's line extension policy.

Very truly yours,



Thomas L. Mumaw

TLM/na

cc: Chairman Kristin K. Mayes
Commissioner Gary Pierce
Commissioner Paul Newman
Commissioner Sandra D. Kennedy
Mike Kearns
Ernest Johnson
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Parties of Record

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