ORIGINAL

0000099146

BEFORE THE ARIZONA CORPORATION COMMISSION

RECEIVED

2009 JUN -9 P 2:57

AZ CORP COMMISSION
DOCKET CONTROL

COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE APPLICATION OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC. FOR A HEARING TO DETERMINE THE FAIR VALUE OF ITS PROPERTY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RETURN THEREON, TO APPROVE RATES DESIGNED TO DEVELOP SUCH RETURN AND FOR RELATED APPROVALS.

DOCKET NO. E-01575A-08-0328

NOTICE OF FILING REPLY BRIEF OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

Sulphur Springs Valley Electric Cooperative, Inc., through counsel undersigned, hereby files its Reply to Staff's May 22, 2009, Closing Brief in the above-captioned matter.

RESPECTFULLY SUBMITTED this 9th day of June, 2009.

SNELL & WILMER L.L.P.

By [signature]
Bradley S. Carroll
One Arizona Center
400 East Van Buren
Phoenix, Arizona 85004-2202
Attorneys for Sulphur Springs Valley Electric Cooperative, Inc.

Arizona Corporation Commission
DOCKETED
JUN - 9 2009
DOCKETED BY [initials]

Snell & Wilmer L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

ORIGINAL and 13 copies foregoing
filed this 9th day of June, 2009, with:

Docket Control
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

COPIES of the foregoing hand-delivered
this 9th day of June, 2009, to:

Ernest Johnson, Director
Utilities Division
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, Arizona 85007

Wesley C. Van Cleve, Attorney
Kevin Torrey, Attorney
Legal Division
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, Arizona 85007

COPY of the foregoing sent via E-Mail and U.S. Mail
this 9th day of June, 2009, to:

Jane Rodda, Administrative Law Judge
Hearing Division
ARIZONA CORPORATION COMMISSION
400 West Congress
Tucson, AZ 85701-1347

By

10114726.1

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES–Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE APPLICATION OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC. FOR A HEARING TO DETERMINE THE FAIR VALUE OF ITS PROPERTY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RETURN THEREON, TO APPROVE RATES DESIGNED TO DEVELOP SUCH RETURN AND FOR RELATED APPROVALS.	DOCKET NO. E-01575A-08-0328

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

REPLY BRIEF OF

SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

June 9, 2009

TABLE OF CONTENTS

Page

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

I. INTRODUCTION

On May 22, 2009, Sulphur Springs Valley Electric Cooperative, Inc. ("SSVEC" or "Cooperative") and the Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") each filed their Closing Briefs in Docket No. E-10575A-08-0328 relating to SSVEC's June 30, 2009, Application for a Hearing to Determine the Fair Value of its Property for Ratemaking Purposes, To Fix a Just and Reasonable Return Thereon, to Approve Rates Designed to Develop Such Return and for Related Approvals ("Application"). SSVEC hereby submits this Reply to Staff's Closing Brief ("Reply Brief").[1] In responding to Staff's Opening Brief, SSVEC's Reply Brief will generally follow the same format as SSVEC's Closing Brief. Please note that Section V (Conclusion) of this Reply Brief contains SSVEC's revised recommendation requests for the Recommended Opinion and Order ("ROO") and is intended to replace those set forth in the Cooperative's Closing Brief.

II. ISSUES WHERE THE COOPERATIVE AND STAFF ARE IN AGREEMENT

The issues where the Cooperative and Staff (collectively the "Parties") are in agreement were set forth in Section III of SSVEC's Closing Brief.[2] The Cooperative shared the list of such issues with Staff prior to filing the Closing Brief. In its Closing Brief, Staff indicated its concurrence regarding the issues where the Parties are in agreement.[3] However, Staff indicated that in light of the supplemental rebuttal testimony of Steve Irvine regarding the approval of new and revised DSM programs that was attached to its Closing Brief as Exhibit A, the DSM adjustor rate (set forth in Section III.U)[4] of the Cooperative's Closing Brief should be increased.[5] The Cooperative will

[1] SSVEC hereby incorporates its Closing Brief dated May 22, 2009.
[2] SSVEC's Closing Brief at page 7, line 5 through page 13, line 5.
[3] Staff's Closing Brief at page 21, lines 12-15.
[4] SSVEC's Closing Brief at page 12, line 6.
[5] Staff's Closing Brief at page 21, line 13.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

discuss its position regarding Staff's revised DSM-related recommendations (including the DSM adjustor rate) in Section IV below.[6]

Additionally, the Cooperative and Staff are in agreement on one additional issue that was not included in SSVEC's Closing Brief relating to the Commission's approval of SSVEC continuing to offer its existing Commission-approved DSM programs that were included in the Direct Testimony of Jack Blair. Counsel for SSVEC has discussed inclusion of this additional issue in the list of agreed-upon issues set forth in Section III of SSVEC's Closing Brief and Staff has no objection. Accordingly, the following should be considered as an additional agreed upon issue:

Approval of SSVEC's Existing Commission-Approved DSM Programs – *The Parties have agreed that SSVEC's existing Commission-approved DSM programs contained in Exhibit A-17, Attachment A, should continue to be approved as modified by the agreed-upon and other DSM-related modifications to SSVEC's DSM Program adopted by the Commission in the Decision.*

Finally, although Staff indicated its concurrence with the agreed-upon issues that were set forth in Section III of SSVEC's Closing Brief, Staff's Closing Brief still discusses some of those issues in detail. Those agreed-upon issues include:

- DSM and REST-related issues;
- WPFCA bank balance thresholds; and
- SSVEC filing written power procurement procedures.

Because the Parties are in agreement on these issues, SSVEC will not discuss these issues further herein.[7]

---

[6] *See* also related discussion regarding future amendments to SSVEC's DSM programs discussed in Section IV.C below.

[7] Although SSVEC does not believe it is necessary to further discuss these issues in light of the Parties' concurrence on such issues, SSVEC does not necessarily agree with all of Staff's characterizations of such issues set forth in it Staff's Closing Brief. Accordingly, by not specifically responding herein, SSVEC does not waive any right to disagree or object to such characterizations in the future.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

III. ISSUES WHERE THE COOPERATIVE AND STAFF DISAGREE

A. REVENUE REQUIREMENT ADJUSTMENTS.

Both the Cooperative and Staff continue to be in agreement that SSVEC should obtain a 30 percent equity-to-long-term debt capitalization ratio by the year 2016. However, SSVEC maintains that it will not be possible to achieve this without adoption of its proposed revenue requirement of $102,688,240. SSVEC's proposed revenue requirement would produce a return on fair value rate base (or operating margin) of $16,706,387 for a 12.57 percent rate of return on the agreed-upon original cost rate base of $132,886,202. SSVEC's proposed revenue requirement produces a 2.46 net operating TIER and a 2.25 DSC, which SSVEC believes represents the necessary and appropriate debt service coverages in order to meet its financial and operational goals and objectives. In order to achieve these objectives, the following proposed Staff adjustments should be rejected:

1. *Reduced operating margin resulting from Staff's proposed revenue requirement ($1,340,871)* -

Contrary to the evidence presented at the hearing, Staff's Closing Brief reiterates its position that SSVEC should experience an increase in equity by a lowering of the Cooperative's long-term debt by utilizing $3 million from $8.8 million of its own net margins and by making an assumption that SSVEC's debt will fall by 10 percent commencing in 2012.[8] Staff also states that SSVEC: (i) developed its revenue requirement to allow for higher capital credit retirements; (ii) made unreasonable assumptions on long-term debt that are not reasonable and, accordingly, Staff adjusted SSVEC's projections downward; and (iii) made debt projections that reflected the minimum amount of debt it could incur, not that it would incur.[9] The following discussion addresses these points.

---

[8] Staff's Closing Brief at page 6, lines 4-8.
[9] *Id.* at page 6, lines 15-19.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

a. <u>There is no basis for Staff to lower long-term debt by $3 million.</u>

Staff's Closing Brief does not cite to any evidence in the record that demonstrates the rationale or the reasonableness of this calculation and simply cites to CSB 8 of Exhibit S-7 where the calculation was made. In contrast, Mr. Hedrick testified in his Rejoinder Testimony regarding the inappropriateness of Staff's calculation.[10] However, the most compelling evidence from the hearing clearly demonstrates that there is no basis to lower long-term debt by $3 million.

As discussed in more detail in the Cooperative's Closing Brief, Staff derives the $3 million reduction from two adjustments; $918,806 and $2,081,194. Based upon a review of the Staff's Surrebuttal Testimony and Surrebuttal Schedule CSB-23, one can not determine from where these adjustments came. Therefore, Staff was asked to explain these two adjustments at the hearing. First, Ms. Brown testified at the hearing that the $918,806 that Staff had previously agreed SSVEC was entitled to was derived from the increase in margin in the Fort Huachuca contract.[11] Staff then arbitrarily (and without explanation in its pre-filed testimony) assigned that portion of the increase in margin towards reduction of long-term debt.[12] In essence, Staff agreed with the Cooperative that it was entitled to an additional $918,806 in margin expense associated with the Fort Huachuca contract, yet took it away from the Cooperative by assigning it to long-term debt reduction in order to arbitrarily inflate the equity ratio.

Next, when asked from where the $2,081,194 was derived, Ms. Brown testified that it came from existing margin *or* depreciation expense.[13] Staff

[10] Exhibit A-9 at page 8, line 10 through page 9, line 11.
[11] Transcript of Hearing ("Trans.") at page 390, line 5 through page 391, line 11.
[12] *Id.* at page 389, line 21 through page 390 at line 4.
[13] *Id.* at page 391, line 12 through page 394 line 9.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

admitted that it came up with $2,081,194 because it determined it wanted to decrease long-term debt by $3 million, so after applying the $918,806 adjustment, it simply subtracted that amount to come up with the additional $2,081,194 in order to "back in" to the $3 million reduction. When asked why Staff decided to reduce long-term debt by $3 million, Ms. Brown testified that Staff wanted the Cooperative to contribute $3 million of its own equity to reduce debt, which in turn, would increase equity.[14] If Staff's recommendation was adopted, the Cooperative would require an additional $3 million of margin to reduce long-term debt; therefore, based on Staff's analysis, the Cooperative would be $3 million short per year of meeting its margin needs to build equity.

b. <u>There is no basis for the assumption that SSVEC's debt will fall by 10 percent in 2012.</u>

Staff's Closing Brief does not cite to any evidence in the record that demonstrates the rationale or the reasonableness of the assumption and simply cites to CSB 8 of Exhibit S-7 where the calculation was made. Mr. Hedrick testified both in his Rejoinder Testimony and at the hearing regarding the inappropriateness of this calculation.[15] However, there is compelling evidence that clearly demonstrates that there is no basis to assume that SSVEC's debt will fall by 10 percent after 2012.

As discussed in more detail in SSVEC's Closing Brief, Staff arbitrarily reduced long-term debt by an additional 10 percent, or $1,916,057, *starting in 2012* based upon the "bad economy." Ms. Brown testified that Staff does not believe the Cooperative will grow at the same pace and, therefore, will not have to borrow as much.[16] When asked from where the 10 percent came, Ms. Brown

[14] *Id* at page 394, lines 14-19.
[15] Exhibit A-9 at page 9, line 13 through page 11, line 2.
[16] Trans. at page 396 at line 7 through page 397, line 5.

Snell & Wilmer L.L.P. LAW OFFICES One Arizona Center, 400 E. Van Buren Phoenix, Arizona 85004-2202 (602) 382-6000

testified that this was based upon "Staff's professional judgment" as to what would happen in the future.[17] Again, this was an arbitrary determination to further reduce long-term debt in order to justify a lowering of the Cooperative's operating margin to mitigate the rate increase and will significantly hinder the Cooperative's ability to reach a 30 percent equity level by 2016.[18]

Staff's Closing Brief further states that SSVEC made unreasonable assumptions on long-term debt and, accordingly, Staff adjusted SSVEC's projections downward.[19] Staff also asserts that SSVEC made debt projections that reflected the minimum amount of debt that it could incur and not that it would incur.[20] However, Mr. Huber testified that SSVEC's level of capital projects would continue into the future, which would require SSVEC to continue its current level of borrowing.[21] Additionally, Staff offered no evidence regarding the Cooperative's level of growth or need for plant additions to support its recommendation. Instead, as discussed above, Staff just *assumes* there will be a bad economy commencing in 2012 and that the Cooperative will not grow at the same pace and, therefore, will not have to borrow as much. SSVEC agrees that it did make its debt projections to reflect the *minimum* amount of debt that it could incur. Yet, nobody knows what will happen in the future. However, as Mr. Huber, the person with the most direct knowledge on this point, testified, SSVEC has prudently planned for its capital projects to continue into the future, which will require SSVEC to continue its current level of borrowing. Mr. Hedrick also testified that "SSVEC has no expectation or reason to believe that the level of loan

[17] *Id.* at page 397, lines 6-12.
[18] *Id.* at page 398, line 23 through page 399, line 10.
[19] Staff's Closing Brief at page 6, lines 16 and 17.
[20] *Id.* at page 6, lines 17-19.
[21] Trans. at page 85, line 15 through page 87, line 19.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

10097471.3

funds required will be reduced."[22] Contrary to the implication raised in Staff's Closing Brief, SSVEC based its debt projections to reflect the *minimum* amount of debt that it anticipates it will incur as a *conservative* approach in which the Commission should agree.

c. <u>The Cooperative developed its revenue requirement to allow for higher capital credit retirements.</u>

Staff's Closing Brief asserts that the Cooperative developed its revenue requirement to allow for higher capital credit retirements.[23] Staff cites to the Direct Testimony of Creden Huber for this proposition. However, the Direct Testimony of Creden Huber specifically states that one of the factors that went into the development of the revenue requirement was to "[a]llow for higher capital credit retirement *once the 30% equity is attained.*" (Emphasis added.)[24] Mr. Hedrick also testified to this at the hearing and said that it was the Cooperative's goal to increase capital credit retirements *after* the 30 percent equity goal is reached and that until the Cooperative does reach a 30 percent equity level, capital credit retirements is really "not an issue" in this case.[25]

As stated throughout this proceeding, SSVEC's proposed revenue requirement was established to allow the Cooperative to attain a 30 percent equity level by 2016. The implication contained in Staff's Closing Brief that SSVEC's proposed revenue requirement is higher than necessary because of capital credit retirements is unfounded and not supported by the record.

Staff's proposed margin adjustments reduce the annual revenue requirement by $1,340,871. The evidence presented overwhelmingly demonstrates that Staff's proposed

[22] Exhibit A-9 at page 11, lines 24-26.
[23] Staff's Closing Brief at page 6, lines 15 and 16.
[24] Exhibit A-2 at page 12, line 24.
[25] Trans. at page 233, lines 5-10; page 249, lines 22-24.

Snell & Wilmer L.L.P. LAW OFFICES One Arizona Center, 400 E. Van Buren Phoenix, Arizona 85004-2202 (602) 382-6000

operating margin adjustment is arbitrarily determined for the sole purpose of lowering the rates and not supported by the evidence. Mere speculation and arbitrary conclusions are not substantial evidence and cannot be determinative. *City of Tucson v. Citizens Utilities Water Company*, 17 Ariz. App. 477, 481, 498 P.2d 551, 555 (Ct. App. 1972). Accordingly, the margin adjustments should not be adopted.

2. <u>*Payroll Expense Adjustment ($523,570)*</u> -

Staff's reduction of known and measurable post-Test Year payroll expenses is not appropriate. Staff reduced payroll expenses by $523,570 as a result of the Cooperative's inclusion of 10 employees that were hired after the Test Year in 2008. In its Closing Brief, Staff reiterates its position that since these employees were hired after the Test Year, it is not appropriate to include the expenses associated with such employees and that inclusion of such employees creates a matching problem.[26] SSVEC acknowledges that these employees were hired outside of the Test Year, however, as the Cooperative points out in its Closing Brief, those employees were hired within four months of the end of the Test Year and the expenses associated with such employees are, in fact, known and measurable.

Although Staff argues that it is inappropriate to include these out of Test Year payroll expenses and that a "matching problem" is created, Staff ignores the testimony at the hearing where Staff acknowledges that Staff did in fact make a pro forma adjustment to interest expense that occurred in November 2008, <u>11 months</u> after the end of the Test Year. Staff did this to provide a more realistic relationship between expenses and rate base and because Staff believed that the expense was reflective of reasonable interest expense for SSVEC going forward. In this instance, Staff did not consider that adjustment to cause a "matching problem."[27] If Staff considers an interest expense that occurred 11 months after

---

[26] Staff's Closing Brief at page 2, lines 9-20
[27] Trans. at page 372, line 13 through page 373, line 14; Exhibit S-6 at page 21, lines 23-25.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

the Test Year to be known and measurable, it is inconsistent to say that 10 employees that were hired a mere four months out of the Test Year and are still on the payroll today, are not a known and measurable expense. As with Staff's November 2008 interest expense adjustment, including the payroll expenses of these 10 employees would in fact provide a more realistic relationship between expenses and rates and would not create a "matching problem" any more than the inclusion of the interest expense (which SSVEC agrees with Staff is an appropriate pro forma adjustment.)

In addition, Staff does not address the testimony of Mr. Hedrick wherein he testified that: (i) the reduction was due to seasonal or part-time employees leaving, and the staffing level included in the Application shows a net gain of 10 employees; (ii) the payroll level proposed by SSVEC is representative of the known, measureable, and continuing level of payroll expenses needed to provide quality of service to members; and (iii) the Cooperative experienced significant growth over the past five years. Accordingly, the number of employees is reasonable and necessary in order to serve the members.[28]

Finally, Staff appears to take issue with the Cooperative's concern regarding inherent regulatory lag and that SSVEC should not have to wait until quality and service levels decline before seeking inclusion of the expenses for new employees. Staff then for some reason, equates this with the Cooperative not filing for a rate increase in 16 years.[29] The employees at issue were hired just four months after the end of the Test Year. Given that these employees represent known and measurable expenses because they were hired to enable the Cooperative to maintain quality of service for its members, based upon the evidence presented at the hearing, the Cooperative should not have to file another rate case (as Staff seems to suggest) to include these expenses.

. . .

---

[28] Exhibit A-8 at page 8, line 9 through page 9, line 23.
[29] Staff's Closing Brief at page 2, line 21 through page 3 line 2.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

Finally, Staff does not discuss its acknowledgement that because these 10 employees are on the payroll today, SSVEC would have to continue paying these employees from its margins.[30] If this adjustment is adopted without a corresponding increase in margin, SSVEC's margin would be reduced by an additional $523,570, thereby further inhibiting the Cooperative's ability to attain its agreed-upon goal of achieving a 30 percent level by 2016.

The evidence does not support Staff's proposed adjustment of payroll expenses by $523,570. Accordingly, such adjustment should not be adopted.

3. *Charitable Contribution Adjustment ($298,622)* –

Staff's Closing Brief seems to imply that in the Cooperative's last rate case (Decision No. 58358), the Commission did not authorize SSVEC to include charitable contributions on a going forward basis.[31] However, Decision No. 58358 speaks for itself. Decision No. 58358 states the following:

> These expenses go to the difficult issue of the role of a Cooperative today. We are mindful of the impassioned arguments made by members of the Cooperative and its board of directors during the public comment session who said that these expenses are appropriate for SSVEC's rural community; that the activities supported may be the only ones available to young people in the area and may not otherwise take place; and, that SSVEC's support is essential for much needed economic development. Additionally, we recognize that the cost of SSVEC's support for all of these expenses averages by $1.76 per customer per year. Were this an investor-owned utility, we would require that the investors, not the ratepayers, bear the cost of the corporation's community mindedness. With a cooperative the ratepayers cannot be separated from their member-owners. For these reasons, we will allow the costs in the instant case. However, we share the concerns of RUCO and Staff that members' choices are made for them. Therefore, we will require in its next rate proceeding, to demonstrate that a majority of its members have ratified the Board's expenditures of their funds for these purposes. If it does not, we will

---

[30] Trans. at page 387, line 9-16.

[31] Staff's Closing Brief at page 3, lines 5-13.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

disallow the expenditures. (Emphasis added.)[32]

The Decision went on to establish the procedures that SSVEC was required to follow for member ratification.[33]

With respect to the underlined language above as it applies to this instant case:

i) As with the prior rate case, the Rebuttal Testimony of Mr. Jack Blair outlines why it is so important for a rural cooperative such as SSVEC to be able to continue to make charitable contributions;[34]

ii) At the February 11, 2009, public comments session held in Sierra Vista, Arizona, there were several members of the public that praised the Cooperative for, and spoke in favor of, its charitable contribution programs;[35]

iii) Mr. Blair testified that the charitable programs represent only about .3 percent of total revenue;[36]

iv) The Commission makes a distinction between a cooperative and an investor-owned utility, which is the same distinction SSVEC made in the instant case;

v) The Commission expressly *allowed* the inclusion of the charitable contributions in the last rate case; and

vi) The Commission required SSVEC to demonstrate in its next rate case (the instant case) that the Cooperative had obtained member ratification consistent with the requirements set forth in the decision, and, if SSVEC did not do so, the Commission would disallow the expenses. SSVEC provided

---

[32] Decision No. 58358 at page 18, line 16 through page 19, line 6.
[33] *Id.* at page 19, lines 8-18.
[34] Exhibit A-18 at page 13, line 11 through page 14, line 2.
[35] *See* Transcript of February 11, 2009, public comment session.
[36] Exhibit A-18 at page 13, line 18-20.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

evidence at the hearing that it complied with the member ratification requirements that had been reviewed by the Commission's Director of Utilities and that over 90 percent of the membership ratified the Cooperative's ability to continue making charitable contributions and donations. [37] Therefore, the expense should be allowed in the instant rate case consistent with the Commission's prior decision.

Although Staff states in its Closing Brief that the trend is for the Commission to disallow charitable contributions, it is clear from the above-cited language that this "trend" started more than 16 years ago, as this was an issue that the Commission specifically dealt with in the last rate case. The evidence presented clearly demonstrates that the Cooperative complied with the provisions of Decision No. 58358. Moreover, without a corresponding increase in operating margin, Staff's proposed adjustment will effectively reduce operating margin by $298,622, as SSVEC's member/ratepayers will continue to pay for such programs even if the adjustment is adopted. This is inconsistent with SSVEC achieving the agreed-upon 30 percent equity level by 2016.

The evidence does not support Staff's proposed adjustment of charitable expenses by $298,622. Accordingly, such adjustment should not be adopted.

4. <u>*Rate Case Expenses Adjustment ($59,522)*</u> –

Surprisingly, despite the overwhelming evidence presented by the Cooperative demonstrating that SSVEC's request for an additional $59,522 in rate case expenses was reasonable, Staff continues to assert that "rate case expenses above the original $100,000 estimate are uncontrollable costs that are unreasonable."[38] First, the characterization that the $100,000 was an estimate of total rate case expenses is not correct or supported by the evidence. Ms. Payne testified that:

[37] Exhibit A-18 at page 13, line 15 through page 16, line 8; Rebuttal Exhibits JB-1 and JB-2; *See* also Tr. page 341 line 7 through page 348, line 4.

[38] Staff's Closing Brief at page 5, lines 4-5.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

> [a]ctual rate case expense will only be known at the time of the hearing/settlement. Schedule RAP-2 shows invoices related to this case incurred up to the filing. We propose to file invoices to ACC Staff for all additional rate case related expenses for a final determination of rate case expense. (Emphasis added.)[39]

Based upon the evidence, as well as the subsequent Rebuttal and Rejoinder Testimony of Mr. Hedrick as more fully described in SSVEC's Closing Brief, there can be no question that the $100,000 included in the Application was not an "estimate" but a placeholder to be trued up as rate case expenses became known and measurable.

Second, Staff asserts in its Closing Brief "that had SSVEC been more proactive in managing rate case expenses, it could have avoided quadrupling those costs from its original lump sum estimate of $100,000."[40] However, Staff presented no evidence in support of this statement wherein SSVEC presented evidence to the contrary. Staff's Closing Brief did not address Staff admissions at the hearing that:

- The Cooperative provided Staff copies of invoices for rate case expenses through February 2009, totaling $331,527, consistent with Ms. Payne's testimony;[41]
- Staff reviewed those invoices and did not find any problem with them.[42]
- The Commission has in the past awarded more rate case expenses than what was requested in the initial Application;[43]
- For an investor-owned utility, shareholders would bear the cost of unrecovered rate case expenses, where as for a cooperative, it would be the member ratepayers that would bear the cost.[44]
- Although SSVEC incurred rate case expenses totaling $384,819 as of April 15, 2009, it had not increased its recovery request despite having to incur

[39] Exhibit A-15 at page 7, lines 3-11.
[40] Staff's Closing Brief at page 5, lines 9-11.
[41] Trans. at page 401, line 15 through page 402, line 25; page 409, line 20 through page 410, line 20; Exhibit A-9 at page 6, lines 24-26.
[42] Trans. at page 422, lines 19-25.
[43] *Id.* at page 403, lines 10-19.
[44] *Id.* at page 403, line 25 through page 404, line 7.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

additional expenses for Rejoinder Testimony, the hearing, briefing, etc.[45]

- When the Cooperative was preparing its rate case, it had no way of knowing how many data requests would be issued, how many witnesses there would be for the hearing, or what additional issues would be interjected into the rate case proceeding.[46]
- The Company offered to amortize its rate case expenses over five years, as opposed to three or four years, which has been more typical.[47]
- The total amount of rate case expenses will exceed $400,000, and SSVEC requested reimbursement for only $397,606.[48]
- The SSVEC rate case could not be litigated for $100,000.[49]
- The Cooperative had no choice but to answer the 17 sets of data requests propounded by Staff and could not refuse to answer them even if it had prepared a budget;[50]
- Staff was willing to approve rate case expenses for the pending Trico rate case in excess of $100,000, despite being a much smaller case with fewer issues.[51]
- If Staff's recommendation was adopted, SSVEC would have to pay its rate case expenses from operating margin.[52]

Third, it is unclear why Staff believes it is important to note that the Commission approved SSVEC's estimate of rate case expenses in its last rate case. This is an "apples to oranges" comparison. Staff presented no direct evidence to compare the situation that existed at the time of the last rate case to the instant situation. Perhaps the amount requested by SSVEC was an "estimate," which is different from the amount included in the instant case because this was merely a placeholder. Regardless, the comparison is inappropriate.

---

[45] *Id.* at page 410, line 21 through page 411, line 25.
[46] *Id.* at page 413, line 25 through page 419, line 15.
[47] *Id.* at page 423, lines 5-18.
[48] *Id.* at page 424, lines 5-18.
[49] *Id.* at page 424 line 24 through page 25, line 7.
[50] *Id.* at page 414, line 25 through page 415, line 5.
[51] *Id.* at page 426, line 22 through page 428, line 7.
[52] *Id.* at page 428, lines 9-21.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

Finally, Staff did not address or controvert the evidence presented in Rejoinder Exhibit DH 1.0 to Mr. Hedrick's Rejoinder Testimony (which was also attached to SSVEC's Closing Brief) which contained a representative sample of cases where the Commission awarded rate case expenses. Several of those cases were discussed in more detail in SSVEC's Closing Brief.

Of the $397,608 of requested rate case expenses, Staff reviewed $331,527 of invoices through February 2009 and did not find any problem with them.[53] SSVEC presented evidence that as of April 15, 2009, prior to the rate case hearing, it had incurred $384,819. The amount of rate case expenses requested by the Cooperative is less than the total amount of rate case expenses that it will ultimately incur. The evidence presented demonstrates that the rate case expenses that were incurred were reasonable under the circumstances. As a cooperative, SSVEC's member-ratepayers will be responsible for paying these expenses. Without a corresponding increase in operating margin, Staff's proposed adjustment will effectively reduce SSVEC's operating margin by $59,522. This is inconsistent with SSVEC achieving the agreed-upon 30 percent equity level by 2016.

The evidence does not support Staff's proposed adjustment of rate case expenses by $59,522. Accordingly, such adjustment should not be adopted.

5. <u>*Christmas and Safety Pay Adjustment ($45,058)*</u> -

SSVEC has never asserted that the Christmas or safety pay is part of employees' base pay. SSVEC has, however, presented evidence that the Cooperative treated such payments as not being incentive-based *per se* and should, therefore, be considered part of the employees' compensation package for ratemaking purposes. Although the Cooperative is not required to pay these amounts, they have been consistently paid each year including the Test Year and were paid to all 195 employees.[54] Staff also did not

---

[53] Trans. at page 422, lines 19-25; *see* also Exhibit A-9 at page 6, line 24 through page 7, line 5.
[54] Exhibit A-8 at page 11, lines 10-23; Exhibit A-9 at page 4, lines 11-18.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

dispute that in SSVEC's last rate case, the Commission found "that the Cooperative has shown this [safety] expense to be appropriate and of benefit to the Cooperative's ratepayers and will not disallow it."[55]

Staff recommended that these expenses be paid from SSVEC's internally-generated cash flows. This would have the effect of further reducing SSVEC's margin, which is inconsistent with the goal of achieving a 30 percent equity level by 2016.[56] Accordingly, the Commission should not adopt Staff's proposed adjustment for these expenses.

B. THE COOPERATIVE SHOULD NOT BE REQUIRED TO SEEK COMMISSION APPROVAL EACH AND EVERY TIME IT DETERMINES IT MUST INCREASE THE WPFCA.

1. *Staff's recommendation is unnecessary and overly burdensome to the Cooperative and should not be adopted.*

Staff's Closing Brief reiterates Staff's recommendation that "SSVEC be required to submit proposed increases to the WPCA rate to the Commission for approval, but not be required to seek approval for decreases in the WPCA rate."[57] Staff also reiterates the same reasons for its recommendations as set forth in its pre-filed testimonies.[58] Staff, however, did not address the evidence showing that (i) SSVEC will still obtain approximately 80 percent of its power needs from AEPCO; (ii) through 2012, SSVEC anticipates that it will obtain between 75.3 and 88.3 percent of its power from AEPCO; and (iii) SSVEC can not control these costs which AEPCO passes through to its members pursuant to its Commission-approved adjustor.[59]

---

[55] Decision No. 58358 at page 14, lines 4-6.
[56] Exhibit S-7 at page 9, lines 2-5; *see* also Trans. at page 369, lines 17 through page 370, line 25. Although Ms. Brown testified that this could also be paid from the Cooperative's depreciation expense, she provided no support for SSVEC being required to do this as both SSVEC and Staff had previously agreed on the amount of depreciation expense that SSVEC was entitled to recover.
[57] Staff's Closing Brief at page 12, lines 10-11.
[58] *Id.* at page 13, lines 8-17.
[59] Exhibit S-13 at page 3, lines 12-25.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

Moreover, Staff did not address the evidence presented by the Cooperative that demonstrates that its recommendation applies to *all* increases, even if the increase will not result in any customer "rate shock" whatsoever and no matter how miniscule the increase, which would be burdensome for the Cooperative. In contrast, SSVEC presented evidence demonstrating that having to file for any and all increases in its WPFCA would:

(i) negatively impact the ability of the Cooperative to properly administer its bank balance;

(ii) require the Cooperative to use its equity margin to "lay out" the money to purchase the power (that as a public utility it is obligated to acquire) for extended periods of time;

(iii) spend time, money, and resources going through a Commission proceeding (just to implement a small increase);

(iv) cause significant delay in the Cooperative's ability to recover costs; and

(v) hinder the Cooperative's ability to be in compliance with the under-collection bank balance threshold.

Requiring Commission approval defeats the purpose of the adjustor mechanism, which is to allow timely recovery of wholesale costs incurred that are outside the Cooperative's control.[60] Moreover, the Cooperative has already agreed that a $2 million threshold for under-collections and a $1 million threshold for over-collections be established for the WPFCA bank balance.[61] This mechanism will help ensure the bank balance does not grow to a level that will cause rate shock when the Cooperative increases its adjustor.

The discussion in Staff's Closing Brief regarding the recommendation that SSVEC file for all increases in its WPFCA does not address the fact that Staff's witnesses acknowledged that purchased power prices SSVEC paid in 2008 during the January through October timeframe were not likely to be representative of purchased power prices

[60] Exhibit A-8 at page 18, line 25 through page 19, line 2.
[61] Exhibit S-12 at page 9, lines 14-16; Exhibit A-9 at page 12, lines 13-15.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

in 2009.[62] SSVEC believes that Staff's recommendation is simply an overreaction to an anomalous situation that existed in 2008 and should not be adopted.

2. *The Cooperative has proposed a reasonable alternative that will achieve Staff's objective*.

In its Closing Brief, Staff continues to take issue with the Cooperative's alternative proposal that it be permitted to adjust its WPFCA rate without Commission approval unless such adjustment would result in a cumulative annual increase in the total average rate collected from customers per kWh greater than 10 percent. Staff argues that (i) there was no way of knowing what the actual impact would be on customer bills; (ii) the proposal is unduly complex and would be difficult to track in terms of compliance; and (iii) there is a lack of transparency to members.[63] Staff also argued that there was an inconsistency between what was proposed in Mr. Hedrick's pre-filed testimony and what he testified to at the hearing.[64]

As set forth in Mr. Hedrick's Rebuttal Testimony, the Cooperative would file for Commission approval of the increase if the "adjustment would result in a cumulative annual increase in the total average rate collected from customers per kWh greater than 10 percent."[65] Moreover, in its Closing Brief, SSVEC provides the exchange that took place between Mr. Hedrick and the Administrative Law Judge ("ALJ") wherein he explained how the mechanism would work.[66]

The proposed mechanism that Mr. Hedrick testified to at the hearing is consistent with what he testified to in his Rebuttal Testimony. Moreover, it is not overly complex and can certainly be worked out with Staff through the filing of a Commission-approved tariff that would govern the administration of the mechanism and set forth the

[62] Trans. at page 128, lines 12-19.
[63] Staff's Closing Brief at page 13, lines 18-22.
[64] *Id.* at page 14, lines 1-11.
[65] Exhibit A-8 at page 19, line 15 through page 20, line 2.
[66] Trans. at page 286, lines 13 through page 287, line 18.

Snell & Wilmer L.L.P. LAW OFFICES One Arizona Center, 400 E. Van Buren Phoenix, Arizona 85004-2202 (602) 382-6000

Cooperative's filing requirements to ensure transparency to both the Commission and SSVEC's members.

If Staff's primary concern is the avoidance of "rate shock" for customers, in addition to the thresholds that the Cooperative has already agreed to, SSVEC has proposed a reasonable compromise position consistent with the purpose and intent behind adjustor mechanisms. This position takes into consideration the issue discussed above relating to the Cooperative being forced to file for very small increases that will not result in customer rate shock. SSVEC believes this proposal to be a reasonable compromise that will address Staff's concerns and allow the Cooperative to avoid the unnecessary burden resulting from being required to file for each and every increase, no matter how small and regardless of whether it will cause rate shock.

3. *If the Commission requires SSVEC to file for increases in the WPFCA, the agreed-upon WPFCA rate should be considered an initial ceiling for adjustment purposes.*

Staff did not address the issue of the agreed-upon WPFCA rate being considered as a ceiling for adjustment purposes in its Closing Brief. It arose in the context of the cross-examination of Staff witness Julie Mcneely-Kirwan (who expressed opposition to this) that was discussed in SSVEC's Closing Brief.[67] In its Closing Brief, SSVEC details why it is appropriate for the Commission to consider the agreed-upon WPFCA as an initial ceiling for adjustment purposes and how the process would work.[68] SSVEC requests that if the Cooperative is required to seek Commission approval for increases in the WPFCA, the mechanism established be consistent with what SSVEC proposed in its Closing Brief regarding the establishment of the initial ceiling.

[67] *Id.* at page 610, lines 4 through page 611, line 10; SSVEC's Closing Brief at page 35, line 22 through page 37, line 20.
[68] SSVEC's Closing Brief at page 36, line 23 through page 37, line 17.

Snell & Wilmer L.L.P. LAW OFFICES One Arizona Center, 400 E. Van Buren Phoenix, Arizona 85004-2202 (602) 382-6000

4. *If the Commission requires the Cooperative to file for an increase in its WPFCA, the increase should go into effect if the Commission does not act upon the filing within 60 days.*

Staff's Closing Brief states that Staff does not agree with the 60-day time frame SSVEC is proposing and simply cites to the Surrebuttal Testimony of Julie Mcneely-Kirwan as support.[69] Staff's Closing Brief does not address the evidence presented by SSVEC in the Rebuttal or Rejoinder Testimonies of Mr. Hedrick[70], or the extensive cross-examination of Ms. Mcneely-Kirwan on this issue.[71]

As SSVEC stated in its Closing Brief, if the Commission determined that SSVEC must file for increases in its WPFCA, because timely recovery of expenses are critical to the Cooperative, SSVEC has proposed a mechanism that the Commission has authorized in the past that will ensure the Commission's ability to review and approve the increase in a timely manner, as such review and approval process is primarily out of the Cooperative's control. Staff admitted that it can typically take as long as four to five months for the Commission to approve an adjustor reset.[72] Moreover, the Commission previously approved adjustors for three other utilities that go into effect unless suspended by the Commission. Those utilities are AEPCO (Decision No. 68071, August 17, 2005), Arizona Public Service (Decision No. 6963, June 11, 2007), and UNS Electric (Decision No. 70360, May 27, 2008).[73] SSVEC requests that if the Commission does require the Cooperative to seek approval of WPFCA increases, the Commission treat SSVEC in the same manner as it has treated the utilities listed above.

. . .

. . .

---

[69] Staff's Closing Brief at page 12, line 12.
[70] Exhibit A-8 at page 19 lines 21-25; Exhibit A-9 at page 13, lines 22 through page 14, line 8.
[71] Trans. at page 633, line 5 through page 642, line 6.
[72] *Id.* at page 539, lines 7-16.
[73] Trans. at page 641, line 2 through page 642, line 6; SSVEC Closing Brief, Attachment B.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

5. *<u>If the Commission requires the Cooperative to file for an increase in its WPFCA, power purchased from AEPCO that is passed through the Commission-approved AEPCO adjustor should not be considered for purposes of an increase to the WPFCA</u>.*

Staff did not address the issue of excluding power purchased from AEPCO for purposes of increasing the WPFCA in its Closing Brief. It arose in the context of the cross-examination of Staff witness Julie Mcneely-Kirwan (who expressed opposition to this) that was discussed in SSVEC's Closing Brief.[74] In its Closing Brief, SSVEC details why it is appropriate for the Commission to exclude power purchased from AEPCO that is passed through the Commission-approved AEPCO adjustor for purposes of an increase to the WPFCA. SSVEC requests that if the Cooperative is required to seek Commission approval for increases in the WPFCA, the mechanism established be consistent with what SSVEC proposed in its Closing Brief regarding AEPCO purchased power costs.

6. *<u>The $453,347 of DSM Program expenses for 2007 and 2008 should be excluded for purposes of increases in the WPFCA and the $2 million under-recovery threshold level</u>.*

Staff did not address this issue of excluding the 2007 and 2008 DSM Program expenses for purposes of increasing the WPFCA in its Closing Brief. It arose in the context of the cross-examination of Staff witness Julie Mcneely-Kirwan (who expressed opposition to this) and was discussed in SSVEC's Closing Brief.[75] In its Closing Brief, SSVEC discussed why the $453,347 of DSM Program expenses for 2007 and 2008 should be excluded for purposes of increases in the WPFCA and the $2 million under-recovery threshold level.

On May 22, 2009, Staff issued a letter to the Cooperative approving $416,383.11 of SSVEC's 2007 and 2008 DSM Program expenses. These expenses will be recovered through SSVEC's WPCA/WPFCA. SSVEC requests that if the Cooperative is required to

[74] Trans. at page 632, line 19 through page 633, line 14; SSVEC's Closing Brief at page 39, lines 14-25.
[75] Trans. at page 608, line 1 through page 609, line 18; SSVEC's Closing Brief at page 40, line 1 through page 42, line 6.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

seek Commission approval for increases in the WPFCA, the mechanism established be consistent with what SSVEC proposed in its Closing Brief regarding the 2007 and 2008 DSM Program expenses.

C. <u>THE COOPERATIVE SHOULD NOT BE REQUIRED TO FILE FOR A PRUDENCY REVIEW OF ITS POWER PROCUREMENT ACTIVITIES</u>.

In its Closing Brief, Staff discussed its recommendation that the Cooperative be subject to prudence reviews of its power procurement activities within three years of the Decision or as part of its next rate case, whichever comes first. Staff states in its Closing Brief that "[w]hile their may be a punitive aspect to a prudence review, its main purpose in this case is to help ensure that resources are not imprudently incurred."[76] Staff also agrees with SSVEC that purchased power prices from January 2008 through October 31, 2008, are not representative of prices for 2009 and beyond.[77]

Staff further claims there is no distinction between a for-profit and a non-profit with regard to power purchases.[78] To the contrary. A cooperative is very different than a for-profit utility in this regard. The performance of SSVEC's management and Board of Directors ("Board") is evaluated (in part) based on its decisions with regard to power purchasing. If SSVEC's cost is too high, the cooperative membership can overturn the Board, or the Board could make changes in the cooperative's management structure. The ratepayers are the owners, and thus the owners pay the power costs. In contrast, with an investor-owned utility, the owners do not pay the costs or the higher rates which translates into higher earnings for the owners.[79] This conflict between outside owners and ratepayers in the investor-owned model is the fundamental basis for regulation and for prudence reviews. The ratepayers of an investor-owned utility have a more heightened

---

[76] Staff's Closing Brief at page 21, lines 5-6.
[77] *Id.* at page 17, lines 21-22.
[78] *Id.* at page 20, lines 1-2.
[79] Exhibit A-6 at page 12, lines 8-15.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

need for direct Commission oversight of their interests because, unlike a member-owned cooperative, the natural incentive to keep rates down in an investor-owned utility is not the same. Consequently, a prudence review for the Cooperative's power purchase activities is not necessary. The Commission already monitors SSVEC's cost of power, and it has the ability to review and evaluate SSVEC's power procurement activities. SSVEC files a power cost report monthly for Commission review, and the Commission at any time has the discretion to request more information from SSVEC to further evaluate SSVEC's activities.[80]

There is also the reality that with a cooperative, any costs that were found to be imprudent as part of a prudence review cannot be charged to anyone other than the member ratepayers. In an investor-owned setting, where prudence reviews are more common, imprudent costs can be charged back against earnings, and, therefore, the stockholders bear the brunt of the costs, not the ratepayers.[81] In SSVEC's case, the ratepayers and the owners are one and the same. SSVEC always endeavors to avoid imprudent costs, and the existence of a requirement to undergo a future prudence review will not alter SSVEC's activities to procure power at the lowest possible cost.

In its Closing Brief, and again herein, SSVEC demonstrated through the evidence presented in the Rebuttal and Rejoinder Testimonies of Mr. Brian, that Staff's recommendation for the imposition of additional regulatory requirements in the form of prudency reviews are unnecessary for a small rural cooperative and will cause SSVEC to devote additional and significant time, its limited resources, and expense, to comply with this requirement. SSVEC believes that this recommendation is premature and is a punitive overreaction to an anomalous and "perfect storm" set of circumstances that arose in 2008. Moreover, SSVEC agreed to prepare and submit written power procurement

---

[80] *Id.* at page 13, lines 22-26.
[81] *Id.* at lines 18-22.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

procedures under which it will operate and has demonstrated that the vast majority of its purchased power needs will still be supplied by AEPCO in the future. Accordingly, until sufficient time has gone by for the Commission to be in a better position to judge SSVEC's power procurement activities, the Commission should not adopt Staff's recommendation for a prudency review on such a small amount of non-AEPCO purchased power.

D. THE ANNUAL DSM ADJUSTOR RESET SHOULD BE DEEMED APPROVED IF THE COMMISSION DOES NOT ACT BY JUNE 1.

The Parties have agreed that by March 1 of each year, SSVEC would file for a reset of its DSM adjustor. However, Staff proposed that the reset of the adjustor become effective on June 1 after Commission approval.[82] Although the Cooperative does not disagree with this *per se*, its concern is that it is unlikely that the Commission will actually be in a position to approve the filing on or before June 1 of each year.[83] Therefore, SSVEC proposes that if the Commission does not act on the filing by June 1, the adjustor be automatically reset.[84]

In its Closing Brief, Staff reiterates the positions taken in its pre-filed testimonies by stating that an automatic reset of the DSM adjustor if the Commission does not act prior to June 1 is not appropriate. Staff states that adjudication of the filings by the Commission will allow the Commission to directly manage recovery of the DSM adjustor rate and the impact on ratepayers and the rate should be set by order of the Commission. Staff further states that SSVEC will continue to collect DSM expenses through its existing adjustor until such time that the new adjustor rate is implemented.[85]

---

[82] Exhibit S-11 at page 7, lines 8-9.
[83] Exhibit A-18 at page 5, line 25 through page 6, line 13.
[84] *Id.* at page 6, line 15 through page 7, line 13.
[85] Staff's Closing Brief at page 10, lines 6-15.

Snell & Wilmer L.L.P. LAW OFFICES One Arizona Center, 400 E. Van Buren Phoenix, Arizona 85004-2202 (602) 382-6000

Staff's Closing Brief does not address or refute the evidence presented by SSVEC where Mr. Blair testified that the Cooperative's proposal:[86]

- Does not deny the Commission the *opportunity* to consider and approve the matter.
- Provides the Commission flexibility under the circumstances.
- Provides the Commission with 90 days to consider and approve the filing.
- The Commission could "true-up" the adjustor the following year if it did not approve the adjustor the previous year.
- The Cooperative is provided certainty by not placing the Cooperative at a disadvantage by having to further wait to recover additional program expenses (or reduce the adjustor for its customers if appropriate) until such time that the Staff and the Commission decide to act on the filing, which is completely outside the Cooperative's control.
- SSVEC is more motivated to promote and proliferate DSM programs consistent with the Commission objectives by ensuring that SSVEC will receive timely recovery of program expenses.

Nor did Staff's Closing Brief address the cross-examination of Mr. Irvine where he acknowledged the following:

- If the Commission did not approve the filing by June 1, the adjustor would not be reset.[87]
- It can typically take as long as four to five months for the Commission to approve an adjustor reset.[88]
- DSM Program expenses that SSVEC incurred in the prior calendar year could not be recovered until such time as the Commission acted;[89]
- The process of Staff review and Commission approval is completely outside the control of the Cooperative (assuming SSVEC is timely with the filing and its responses to data requests).[90]

---

[86] Exhibit A-19 at page 2, line 14 through page 3 line 18.
[87] Trans. at page 559 lines 19 through page 560 at line 1.
[88] *Id.* at page 539, lines 7-16.
[89] *Id.* at page 561, line 15 through page 562, line 10.
[90] *Id.* at page 562, line 11 through 564, line 1.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

- From the period 2001 through 2006, SSVEC had semi-annually submitted for Staff approval of $549,929 of DSM Program expenses per the mechanism established in the last rate case decision that it took Staff until July 8, 2008, to approve $502,414 of such expenses.[91]

- SSVEC submitted for Staff approval its 2007 and 2008 DSM Program expenses on a semi-annual basis totaling approximately $453,000, and Staff had still not acted upon the filings by the time of the hearing.[92]

- If the adjustor went into effect automatically in a given year, the Commission could true-up the adjustor the following year for the two-year period, thereby continuing its oversight of the adjustor, although it would be over two years, instead of one.[93]

- If the Commission adopts SSVEC's request for an automatic reset of the adjustor on June 1, and if the Commission does not act, then the adoption of this mechanism would be embodied in the Decision of the Commission that derives from this rate case proceeding.[94]

As SSVEC stated in its Closing Brief, each of the points listed above directly refute the rationale that form the basis of Staff's opposition to SSVEC's proposal and/or illustrate the Cooperative's concern as to why the DSM adjustor reset should not be an open-ended process. Accordingly, the Commission should adopt SSVEC's proposal that the DSM adjustor be reset on June 1 of each if not acted upon by the Commission by such time.[95] Additionally, for the reasons stated in the Cooperative's Closing Brief, SSVEC requests that there be language in the ROO that would not preclude SSVEC from filing for a reset of its DSM adjustor more than once a year if the Cooperative deemed it necessary.

. . .

. . .

---

[91] *Id* at page 564, lines 5 through page 566, line 1; Exhibit A-24 and A-25.

[92] *Id.* at page 566, line 1 through page 567, line 3.

[93] *Id.* at page 568, line 19 through page 570, line 9.

[94] *Id* at page 572, lines 1-22.

[95] It should be noted that as discussed in Section III.B.4 above, the Commission has permitted automatic adjustor resets for fuel and purchased power expenses if the Commission does not act within a certain time frame. Such resets generally have a greater impact on customer bills than would changes in a DSM adjustor.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

E. THE COMMISSION SHOULD ADOPT SSVEC'S PROPOSED CUSTOMER CHARGES.

Staff's Closing Brief reiterates that its recommendation regarding SSVEC's customer charges is based on trying to limit the increase of this particular charge to approximately 10 percent consistent with the overall proposed revenue increase, and to encourage customers to implement conservation measures more effectively based upon three rate design principles.[96] However, Staff's recommendations neither address the testimony of Mr. Hedrick nor the cross examination of Mr. Musgrove cited in the Cooperative's Closing Brief where it was established that:

- SSVEC's proposed charge brings the charge closer to its actual cost.[97]
- To say that it represents a 67 percent increase, although technically accurate if a customer had no kWh usage and his electric bill was only the customer charge of $7.50 per month is misleading because it singles out only one component of the requested rate increase.[98]
- The Commission has previously approved increases in customer charges for other cooperatives which are similar to those requested by SSVEC. TRICO Electric Cooperative and Navopache Electric Cooperative both received substantial increases in the customer charge component of the rate in their last rate filings before the Commission.[99]
- Under Mr. Musgrove's principle of "gradualism," it would take over 20 rate changes to reach the actual $23.31 cost of providing the service if the rate could only be increased by $.075 per rate case.[100]

Based upon this evidence, Staff's recommendation is not reasonable, and the Cooperative's proposed customer charges should be adopted.

. . .

. . .

. . .

---

[96] Staff's Closing Brief at page 15, lines 1-6.
[97] Exhibit A-8 at page 20, lines 6-25.
[98] Exhibit A-9 at page 16, lines 11-25.
[99] Exhibit A-8 at page 21, lines 8-17.
[100] Exhibit A-9 at page 14, line 23 through page 15, line 2.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

F. THE COMMISSION SHOULD ADOPT SSVEC'S PROPOSED $50 CHARGE FOR REGULAR HOUR CONNECTIONS AND NON-PAY TRIPS.

In its Closing Brief, Staff states that the additional $10.00 increase in the above service charges would "produce approximately $200,000 in additional revenues."[101] It is unclear why and how that is relevant, especially when one of the primary objectives of this proceeding is to permit the Cooperative to build equity to a 30 percent level by 2016. Also, Staff continues to imply that there is something wrong when the charge associated with providing a particular service moves closer to the actual cost of providing that service. The fact that Staff recommended an allocation of $6.4 million "to other rate classes and service charges" has no bearing as to whether the Cooperative's proposed service charges are just and reasonable.

In recommending the $40 charge for these two services, Staff started from a flawed starting point. Staff's approach to setting the rates took into consideration the increase in the cost of labor since 1993 without regard to whether the rate established in 1993 covered the Cooperative's actual cost of providing the service.[102] As more fully discussed in the Cooperative's Closing Brief, to the extent the Cooperative was not recovering its costs in 1993, it is not the appropriate starting point to set the rate in 2009. Mr. Hedrick testified that "the Commission has expressed the intent that to the extent practicable, the costs of providing service should be borne by those that cause the costs to be incurred" and that "the establishment of appropriate service is a clear way to accomplish this objective."[103]

SSVEC believes that the additional $10 increase in these two service charges to $50 move the charges closer to the actual cost of providing the services[104] and helps to mitigate the need for the Cooperative to subsidize the costs from other sources; such as

[101] Staff's Closing Brief at page 16, lines 11-13.
[102] Mr. Musgrove testified that he did consider transportation costs through the increased mileage charge. *See* Trans. at page 487, lines 4-9.
[103] Exhibit A-9 at page 17, lines 22 through 26.
[104] *Id.* at line 26 through page 18, line 1.

from equity.

IV. STAFF'S RECOMMENDATIONS REGARDING THE COOPERATIVE'S PROPOSED DSM PROGRAMS

A. BACKGROUND.

As part of its Application, SSVEC submitted for Commission approval three new DSM programs, as well as a modification to one of its existing programs. The proposed new programs are the (1) Energy Efficient Water Heater Rebate Program; (2) Commercial and Industrial Energy Efficiency Improvement Loan Program ("C&ILP"); and (3) Energy Efficient New Home or Remodel Rebate Program[105] (collectively "New Programs"). SSVEC also proposed modifications to its existing loan program which would now be called the Energy Efficient Improvement Loan Program ("EEILP"). SSVEC requested these New Programs and the EEILP modifications be approved as part of the Decision in this docket. By the time of the hearing, Staff had not completed its review of SSVEC's proposals with respect to these DSM programs but indicated at the hearing, that it intended to complete its review and provide a late-filed exhibit addressing Staff's recommendations on these DSM programs.[106] As part of its Closing Brief, Staff attached Supplemental Testimony of Steve Irvine dated May 22, 2009, ("Supplemental Testimony") relating its recommendations on the New Programs, the EEILP, and the 2007 and 2008 DSM Program expense reports that were discussed above.

B. STAFF'S RECOMMENDATIONS AND SSVEC'S CONCURRENCE REGARDING THE NEW AND REVISED PROGRAMS.

In the Supplemental Testimony, Staff summarized its recommendations regarding SSVEC's proposals regarding its DSM programs.[107] SSVEC reviewed the Supplemental

[105] Staff did not recommend approval of this DSM program.
[106] Trans. at page 671, lines 12-17.
[107] Supplemental Testimony of Steve Irvine dated May 22, 2009 ("Supp. Test.) at page 18, line 18 through page 19, line 18.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

Testimony and the recommendations and agrees with all of Staff's recommendations except as discussed below.

Regarding the C&ILP and the EEILP, Staff recommended that SSVEC's proposed three (3) percent interest rate be lowered to a zero (0) interest rate to make the programs more accessible to customers.[108] Although SSVEC does not oppose this recommendation *per se*, it does have two concerns that it raised with Staff. First, by lowering the interest rate from three (3) percent to zero (0) percent, this will result in increased costs to the Cooperative that are not reflected in Staff's revised proposed DSM adjustor rate of $0.000474 per kWh. Second, Jack Blair has since reviewed the data and contacted several of the people from the focus groups that were originally used to help formulate the Cooperative's DSM programs to evaluate the impact of reducing the interest rate from three (3) percent to zero (0) percent.[109] Based upon this information, the Cooperative agrees with Staff that lowering the interest rate will make the C&ILP and the EEILP more accessible to customers and will increase participation. However, because of this increase in participation and the lowering of the interest rate, the Cooperative will incur additional expenses more quickly because of the reduced interest rate. As the Cooperative is not in a position to "lay out" even more money until such time as there is a DSM adjustor reset (as discussed above), SSVEC believes that the initial DSM adjustor rate should be set higher than $0.000474.kWh recommended in the Supplemental Testimony to take into account the additional costs the Cooperative will incur as a result of the lowering of the interest rate and the increase in member participation in the programs.

The Cooperative has discussed this issue with Staff and as a result, the Parties are in agreement that the Commission should set the DSM adjustor rate at $0.00088 per kWh. With that agreed upon modification to the DSM adjustor rate, the Cooperative has agreed

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

[108] *Id.* at page14, lines 3-8.
[109] *See* Exhibit A-17 at page 9, lines 7-22.

to all of Staff's recommendations set forth in the Supplemental Testimony.[110]

C. <u>FUTURE AMENDMENTS TO SSVEC'S DSM PROGRAMS INCLUDING THE TWO NEW DSM PROGRAMS APPROVED IN THIS PROCEEDING</u>.

As part of the Decision that will be issued in this proceeding, the Commission will approve the Cooperative ability to continue its existing DSM programs set forth in the Application, as well as approve the new Energy Efficient Water Heater Rebate Program, the C&ILP and the modifications to the EEILP, consistent with the recommendations contained in the Supplemental Testimony. Commission approval of the Cooperative's DSM programs are not part of the rate application *per se* (with the exception of the DSM adjustor) and were included as part of the rate case Application (as opposed to a separate application) for the convenience of the Parties and for judicial economy. Therefore, in the event that SSVEC needs to modify or amend any of its Commission-approved DSM programs approved as part of the Decision issued in this docket (including the Energy Efficient Water Heater Rebate Program, the C&ILP, and the EEILP), the Cooperative should be required to file a new application with the Commission, as opposed to an application to amend the rate case Decision pursuant to A.R.S. §40-252.

V. CONCLUSION

Staff concluded its Closing Brief by stating that the adoption of Staff's recommendations will result in just and reasonable rates for SSVEC.[111] However, the Cooperative has presented compelling evidence that demonstrates Staff's proposed adjustments will result in a reduction of SSVEC's proposed revenue requirement that the Cooperative demonstrated is necessary for SSVEC to achieve its operational and financial objectives. As stated in SSVEC's Closing Brief, when setting rates for public utilities, the Commission should focus on the principle that "total revenue, including income from

---

[110] Supp. Test. At page 18, line 19 through page 219, line18.
[111] Staff's Closing Brief at page 21, lines 17-18.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

rates and charges, should be sufficient to meet a utility's operating costs and to give the utility and its stockholders a reasonable rate of return on the utility's investment." *Scates v. Arizona Corp. Comm'n,* 118 Ariz. 531, 533-34, 578 P.2d 612, 614-15 (App. 1978). In the case of a cooperative such as SSVEC, the return on investment relates to the operating margin necessary for the Cooperative to build its equity to the agreed-upon level of 30 percent by 2016. If the Commission adopts Staff's operating margin adjustments, this will not occur. An average increase of 10.46 percent after 16 years constitutes a just and reasonable rate increase. Based upon the evidence presented, it is not necessary for the Commission to adopt Staff's adjustments for the purpose of mitigating and artificially lowering the amount of the increase.

Finally, the Cooperative's management has demonstrated good stewardship over these last 16 years. Staff's recommendations relating to Commission approval of each and every WPFCA increase and the need for purchased power prudency reviews are simply not warranted at this time. Moreover, the Commission should not inhibit the Cooperative's ability to continue its proliferation of DSM programs by requiring the Cooperative to wait more than 90 days to reset its DSM adjustor.

Based upon the evidence presented at the hearing as outlined and discussed in SSVEC's Closing Brief and in this Reply Brief, SSVEC respectfully requests that the ALJ issue a ROO recommending that:

- SSVEC's Application be approved as modified herein.
- SSVEC has a Test Year original cost rate base of $132,886,202 and is entitled to an opportunity to earn a return on fair value rate base (margin) of 12.57.
- In order for SSVEC to achieve its financial and operational objectives, including the achievement of a 30 percent equity-to-long-term debt capitalization ratio by 2016, the Commission adopt SSVEC's proposed revenue requirement of $102,688,240 set forth in Section IV.A of its Closing Brief.

. . .

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

- SSVEC's proposed revenue requirement produces a net 2.46 operating TIER and a 2.25 DSC.

- All of the agreed-upon issues set forth in Section III of the Cooperative's Closing Brief be adopted with the exception of the DSM adjustor rate set forth in Section III.U, which the Parties agree, should now be set at $0.00088 per kWh. This should also include the following additional agreed-upon condition set forth in Section II above:

  <u>Approval of SSVEC's Existing Commission-Approved DSM Programs</u> – The Parties have agreed that SSVEC's existing Commission-approved DSM programs contained in Exhibit A-17, Attachment A, should continue to be approved as modified by the agreed-upon and other DSM-related modifications to SSVEC's DSM Program adopted by the Commission in the Decision.

- Staff's revenue requirement adjustments set forth in Section IV.A.1-5 of SSVEC's Closing Brief be denied. To the extent, however, that any of Staff's proposed adjustments are adopted for ratemaking purposes, the Commission should increase SSVEC's operating margin by a like amount to ensure that SSVEC's proposed revenue requirement is realized so the Cooperative will have sufficient revenue to achieve its financial and operational objectives.

- SSVEC should not be required to file for Commission approval of WPFCA increases. If, however, approval of WPFCA increases are required, that (i) such filings be limited to increases that will result in a cumulative annual increase in the total average rate collected from customers per kWh greater than 10 percent; (ii) increases should be limited to those increases that increase the WPFCA rate above the WPFCA factor in effect at the time SSVEC implements the new rates and charges pursuant to the Decision; (iii) power purchased from AEPCO that is passed through the Commission-approved AEPCO adjustor should not be considered for purposes of an increase to the WPFCA; (iv) once the Commission increases the adjustor per a filing by SSVEC, such new rate should be considered the ceiling for future filings; (v) the increase should automatically go into effect 60 days after the filing unless suspended by the Commission; and (vi) the $453,347 of DSM Program expenses for 2007 and 2008 to be included in the WPFCA not be considered for purposes of the $2 million under-collection threshold or for WPFCA adjustor increase calculations.

- The Cooperative not be required to file for a prudency review of its power procurement activities at the next rate case or within three years, whichever comes first.

- The annual reset of the Cooperative's DSM adjustor should be deemed approved if the Commission does not act to suspend the Cooperative's filing by June 1.

. . .

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000

- SSVEC be permitted to file for a DSM reset more than once a year if the Cooperative deems it to be necessary for the timely recovery of DSM Program expenses.
- The Commission adopt SSVEC's proposed Customer Charges.
- The Commission adopt SSVEC's proposed $50 charge for Regular Hour Connections and Regular Hour Non-Pay Trips.
- The Commission approve SSVEC's Energy Efficient Water Heater Rebate Program, C&ILP, and EEILP consistent with the recommendations contained in the Supplemental Testimony.
- If the Cooperative needs to amend any of its DSM programs in the future, including, but not limited to, the Energy Efficient Water Heater Rebate Program, the C&ILP, and the EEILP as approved in this Decision, SSVEC shall file a new application to amend its DSM program with the Commission and not an application to amend the Decision in this docket pursuant to A.R.S. §40-252.

Snell & Wilmer
L.L.P.
LAW OFFICES
One Arizona Center, 400 E. Van Buren
Phoenix, Arizona 85004-2202
(602) 382-6000