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AZ CORP COMMISSION
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BEFORE THE ARIZONA CORPORATION COMMISSION

1
2 WILLIAM A. MUNDELL
3 Chairman
4 JIM IRVIN
5 Commissioner
6 MARC SPITZER
7 Commissioner

8 IN THE MATTER OF THE GENERIC
9 PROCEEDINGS CONCERNING ELECTRIC
10 RESTRUCTURING

DOCKET NO. E-00000A-02-0051

11 IN THE MATTER OF ARIZONA PUBLIC
12 SERVICE COMPANY'S REQUEST FOR VARIANCE
13 OF CERTAIN REQUIREMENTS OF A.A.C. 4-14-2-
14 1606

DOCKET NO. E-01345A-01-0822

15 IN THE MATTER OF THE GENERIC PROCEEDING
16 CONCERNING THE ARIZONA INDEPENDENT
17 SCHEDULING ADMINISTRATOR

DOCKET NO. E-00000A-01-0630

18 IN THE MATTER OF TUCSON ELECTRIC POWER
19 COMPANY'S APPLICATION FOR A VARIANCE
20 OF CERTAIN ELECTRIC POWER COMPETITION
21 RULES COMPLIANCE DATES

DOCKET NO. E-01933A-98-0471

22 ISSUES IN THE MATTER OF TUCSON ELECTRIC
23 POWER COMPANY'S APPLICATION FOR A
24 VARIANCE OF CERTAIN ELECTRIC
25 COMPETITION RULES COMPLIANCE DATES.

DOCKET NO. E-01933A-02-0069

**ARIZONA PUBLIC SERVICE COMPANY'S RESPONSE TO
REQUEST FOR ORDER TO SHOW CAUSE**

26 Pursuant to the direction of the Chief Administrative Law Judge of the Arizona
Corporation Commission ("Commission"), Arizona Public Service Company ("APS" or
"Company") hereby responds to the Request for Order to Show Cause submitted by

Arizona Corporation Commission
DOCKETED

MAR 29 2002

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1 intervenor Panda Gila River, L.P. (“Panda”).¹ As explained below, the Chief
2 Administrative Law Judge should reject Panda’s latest attempt to frustrate prompt
3 Commission consideration of the Company’s filing.

4 I. INTRODUCTION.

5 At its core, Panda’s Request represents yet another attempt by the various merchant
6 generators to block or delay Commission adjudication of APS’ Request for a Partial
7 Variance filed over six months ago. Now, just a month from the hearing, Panda makes the
8 purely fictional claim that APS—which itself raised and framed the critical issues
9 affecting reliability and price stability in its October 2001 filing—has “delay[ed]” the
10 resolution of those same issues and that it would now be “unfair” to allow APS to present
11 its case at hearing. (See Panda’s Request at p. 12.) Panda does not and cannot support
12 such claims.

13 The broader question in this case is not, as Panda contends, whether to pursue
14 competitive bidding; competitive bidding is specifically called for in the Purchase Power
15 Agreement (“PPA”) with Pinnacle West Capital Corporation (“Pinnacle West”) proposed
16 by APS. Rather, the question is whether APS’ Request for a Partial Variance is superior to
17 a “flash-cut” to the 50 percent competitive bid component of A.A.C. R14-2-1606(B)
18 (“Rule 1606(B)"). These two alternatives are necessarily mutually-exclusive strategies for
19 resource acquisition. The answer is either 50 percent competitive bidding under Rule
20 1606(B) or the proposed PPA—not try one, then the other, and later maybe something
21 else.

22 ¹ At the March 20, 2002 Procedural Conference, the Chief Administrative Law Judge directed APS
23 to respond to Panda’s Request on or before March 29, 2002. On March 26, 2002—prior to APS filing this
24 response—Commissioner Spitzer docketed a letter proposing that the Commission request responsive
25 briefs and convene an open meeting regarding the merits of proceeding with a Request for Proposals
26 process. As of the date this response was prepared, no Commission action has been taken regarding
Commissioner Spitzer’s March 26, 2002 letter. Accordingly, this response is directed solely at Panda’s
Request for an Order to Show Cause and is not intended as a specific response to Commissioner Spitzer’s
letter. APS reserves the right to supplement this response if the Commission directs additional briefing as
suggested in Commissioner Spitzer’s letter.

1 Further, Panda's Request brushes aside insoluble obstacles to even conducting a
2 meaningful competitive bid now, prior to adjudicating APS' Request for a Partial
3 Variance and completing the transfer of APS' generating assets. For example, Rule
4 1606(B) is itself premised on the transfer of an Affected Utility's generating assets, which
5 for APS will not occur until later this year. Also, the proposed PPA would not constitute
6 Pinnacle West's bid in any competitive bidding process, and so cannot serve as a
7 comparative benchmark as suggested by Panda. Indeed, comparisons of anything less than
8 bids for a full-requirements contract lasting through 2015 with delivery at multiple points
9 on APS' system with significant fuel and geographic diversity would be meaningless and
10 unhelpful in evaluating the proposed PPA. As such, the only logical, legal, prudent and
11 procedurally warranted approach is to hear APS' Request and APS' evidence before
12 determining whether it is appropriate to comply with hastily considered bidding rules that
13 APS believes will be detrimental to its customers.

14 Apart from these core substantive and logical failings in Panda's Request, there are
15 numerous other flaws that warrant rejection of Panda's Request. First, Panda already has
16 requested the same specific relief in its December 19, 2001 Joint Brief with the Arizona
17 Competitive Power Alliance ("ACPA"). The Chief Administrative Law Judge denied that
18 relief, and Panda's Request is simply an inappropriate second bite at the same already
19 well-chewed apple. (*See* February 8, 2002 Procedural Order at pp. 2, 8-12.) Second,
20 Panda's Request is premised on the facially-erroneous assumption that APS is presently
21 violating a rule that is not effective as to APS until January 1, 2003 and which cannot
22 become effective until APS transfers its generation assets. Finally, Panda's Request
23 misapplies and mischaracterizes both Arizona law and federal law with respect to issues
24 surrounding APS' Request for a Partial Variance and Rule 1606(B).

25 APS should be allowed to present its evidence and have its case heard by the
26 Commission in an evidentiary hearing commencing on April 29, 2002—a schedule that

1 Panda has known of since early February 2002. This is also a schedule that keeps the
2 horse before the cart. If the Commission determines, following a full and fair hearing, that
3 50 percent competitive bidding is more appropriate than the proposed PPA, all parties
4 (including Pinnacle West, which would thereby be relieved from the PPA) can proceed
5 with such competitive bidding. Based on the record as it stands today, the Chief
6 Administrative Law Judge should deny Panda's Request and move forward with the
7 procedural schedule that is already in place.

8 **II. PANDA'S REQUEST IS SIMPLY THE LATEST ATTEMPT BY**
9 **A MERCHANT GENERATOR TO DELAY THE ADJUDICATION**
10 **OF APS' REQUEST FOR A PARTIAL VARIANCE.**

11 Panda's Request asks the Chief Administrative Law Judge to "immediately" stay
12 the procedural schedule established to adjudicate APS' Request for a Partial Variance, and
13 order APS to issue a Request for Proposals ("RFP"). Thus, again, Panda seeks to delay or
14 forestall Commission consideration of APS' Request—an effort that has been echoed by
15 other merchant generators since early in this proceeding and that ignores APS' right to
16 have its request heard under A.A.C. R14-2-1614(C) ("Rule 1614(C)"). Panda's proposal
17 would not provide the Commission any meaningful comparison to the proposed PPA, and
18 the Chief Administrative Law Judge should reject Panda's shop-worn argument that the
19 only means of testing the merits of APS' case is to immediately proceed with competitive
20 bidding.

21 **A. The "Trial by Combat" Suggested by Panda Could Not**
22 **Practically Be Undertaken Nor Would It Allow a Meaningful**
23 **Comparison to the Proposed PPA.**

24 APS has not yet transferred its generation assets to an affiliate—a fundamental and
25 necessary prerequisite to competitive bidding. The Commission has long recognized and
26 acknowledged that the competitive bidding provisions of Rule 1606(B) are dependent
upon and only apply when the divestiture provisions of Rule 1615 have been

1 implemented. *See* Decision No. 61973 (compliance with Rule 1606(B) tied to compliance
2 with Rule 1615). Indeed, while many provisions of the Electric Competition Rules are
3 generally applicable to “Affected Utilities” such as APS, Rule 1606(B) is, by its own
4 terms, applicable only to investor-owned “Utility Distribution Companies”—a term that
5 describes APS post-divestiture. Thus, a competitive bid under Rule 1606(B) simply
6 cannot be completed before APS transfers its generation assets, which is a step that APS
7 has proposed for later in the year but which Staff appears to now be contesting.

8 Also, the proposed PPA is not and was never intended to be a “backstop” or option
9 agreement in the event that actual competitive bidding failed to produce results acceptable
10 to the Commission. As a cost-based contract, the PPA certainly does not and would not
11 represent Pinnacle West’s “bid” in any such process, as Panda’s Request would suggest.
12 A full requirements contract like the proposed PPA is much different from proposal(s)
13 that Pinnacle West might submit in a competitive bid. Indeed, if competitive bidding were
14 directed today by the Commission, APS and Pinnacle West would have no other choice
15 but to move immediately to transfer the generating assets pursuant to the 1999 APS
16 Settlement Agreement and Rule 1615 in order to proceed with such bidding.

17 Further, Panda’s Request describes its views on the competitive bidding process
18 and is clearly seeking to restrict APS’ flexibility in conducting and developing any such
19 process. (*See* Panda’s Request at pp. 10-11). Thus, if granted, Panda’s Request appears
20 likely to shift the Commission’s entire substantive focus from whether or not APS’
21 Request for a Partial Variance is in the public interest, to nothing more than litigation over
22 the competitive bidding process itself. At best, Panda’s suggestions on the competitive bid
23 process amount to a request for a rulemaking, because any of the detail to Rule 1606(B)
24 proposed in Panda’s Request would require the Commission to convene a formal
25 rulemaking under the Arizona Administrative Procedure Act to adopt such requirements.

26

1 Ultimately, however, even if a competitive bid were somehow conducted now, a
2 comparison of any bids received to the proposed PPA would simply not be probative, let
3 alone dispositive. For example, one cannot meaningfully compare a full requirements
4 contract delivering energy from fuel-diverse resources at multiple points to APS' system
5 through 2015 with, for example, an assemblage of shorter-term offers to each deliver 500
6 MW of gas-fired generation from a single plant to the Palo Verde hub. A \$40/MWh bid
7 for baseload generation or an \$80/MWh bid for peaking power cannot be directly
8 compared to a full requirements, 24x7 agreement. Nor could a fixed-price, variable-output
9 contract based on actual cost be readily compared to a fixed-output, index-priced contract.
10 Panda's Request, however, seems to relegate this fundamental comparability problem to
11 an inconsequential afterthought.

12 In addition to the issues of timing and comparability, there is another important
13 reason to doubt the utility of any "trial" bidding program as suggested by Panda. Because
14 the Commission would have to eventually return to the task of considering the Company's
15 Request for a Partial Variance, any bids submitted would necessarily be with reservation.
16 That is, the bid would be binding on neither the bidder nor APS pending the eventual
17 Commission ruling on APS' filing. It is obviously easier to submit a favorable bid when
18 the process is not legally binding.

19 Even if a competitive bid were procedurally appropriate at this juncture, the
20 process would inevitably and very significantly delay the necessary hearing on APS'
21 Request for a Partial Variance. This would add even more to the concern over timing that
22 APS has raised since filing its Request in October 2001. Moreover, all this effort and
23 delay would occur without ever actually answering the questions surrounding competitive
24 bidding or the customer concerns presented in APS' Request, and it would ultimately tell
25 the Commission virtually nothing about whether the proposed PPA is reasonable.
26 Therefore, it is both impractical and imprudent to leap first and look later by starting a

1 competitive bidding process before the Commission has even had an opportunity to
2 consider the issues presented in APS' Request for a Partial Variance.

3 **B. APS Should Be Allowed to Show Why the Public Interest Is**
4 **Served Through the Partial Variance and Proposed PPA.**

5 Under Rule 1614(C), APS is entitled to request a variance from "the terms of any
6 of the rules" that comprise the Commission's Electric Competition Rules. Rule 1614(C)
7 only requires that APS' application "set forth the reasons why the public interest will be
8 served by the variation or exemption from the Commission rules or regulations." That rule
9 does not require, as Panda implicitly suggests, that the applicant pursue some extra-
10 administrative procedural burden to prove its case, such as the issuance of an RFP under
11 circumstances that, as argued above, make such an effort wholly impractical. If Panda's
12 argument is accepted, it would force APS to simultaneously prove that its Request for a
13 Partial Variance is in the public interest, while attempting to draw out the details for a
14 future process that is itself dependent on the resolution of APS' underlying request.

15 In this case, APS has presented testimony as to why it does not believe that literal
16 compliance with Rule 1606(B) is appropriate and why its proposed PPA is in the public
17 interest. At the time this response was prepared, Panda had not yet presented any evidence
18 to contradict the testimony already docketed in this matter, nor has APS had the
19 opportunity to rebut whatever evidence Panda may seek to submit through its March 29,
20 2002 testimony. In fact, Panda has never even specifically alleged that a full 50 percent of
21 APS' power requirements could be feasibly obtained by competitive bidding starting on
22 January 1, 2003. When asked in discovery by APS for any evidence that such bidding
23 would succeed today, Panda objected to the question and refused to provide APS even
24 anecdotal evidence of its claims. Apparently, based on Panda's Request and its discovery
25 responses, the Commission is not supposed to hear any actual evidence on whether
26 bidding pursuant to Rule 1606(B) may or may not work. Instead, it is told by Panda that

1 the only way to find out is to terminate APS' hearing, conduct the bid, and simply skip
2 any evaluation of whether such bidding is appropriate or in the public interest in the first
3 place. This docket greatly concerns the interests of APS' customers, and should not be
4 treated like a game of poker where the Commission has to bet APS customers' money to
5 get a peek at Panda's hole card.

6 Further, with no citation to any applicable Arizona authority, Panda claims that
7 "APS cannot possibly be deemed to have been prudent" if it does not issue an RFP rather
8 than continue with its Request for a Partial Variance. (Panda's Request at p. 7.) This, of
9 course, is incorrect as a matter of law and the Commission is not as restricted as Panda
10 argues. Arizona law nowhere requires an RFP to determine prudence and in practice the
11 Commission has repeatedly passed on the prudence of APS generation resource
12 acquisition decisions without the need for an RFP. Here, the Commission's Chief
13 Administrative Law Judge has already determined that APS is entitled to present its
14 evidence and obtain a fair hearing on its request, just as the other parties are entitled to
15 present their cases to the Commission.

16 **C. The Relief that Panda Seeks Has Already Been Denied by the**
17 **Chief Administrative Law Judge.**

18 Finally, Panda has already sought—and the Chief Administrative Law Judge has
19 already denied—the specific relief it seeks through its Request for an Order to Show
20 Cause. In its December 19, 2001 joint brief² on the proper procedural mechanism for
21 APS' Request for a Partial Variance, Panda and the ACPA both requested that the
22 Commission dismiss APS' Request for a Partial Variance and order APS to submit a
23 "Plan of Administration" for competitive bidding. The Procedural Order that was issued
24 following the parties' briefing restated Panda's and the ACPA's request that APS be

25 ² The joint brief was captioned as the Brief of the ACPA on the Proper Procedural Mechanism for
26 Consideration of APS' Request for a Partial Variance, but was signed by both Panda and the ACPA.

1 ordered to proceed with a competitive bid in lieu of its Request for a Partial Variance. The
2 Chief Administrative Law Judge, however, did not order APS to submit a “Plan of
3 Administration” and proceed with a competitive bid, but instead established the
4 procedural schedule that will allow the Commission to hear APS’ case. Thus, through its
5 Request, Panda is simply and inappropriately re-arguing this already decided request
6 using a differently-captioned pleading.

7 **III. PANDA FAILS TO PRESENT ANY EVIDENCE THAT APS HAS NOT OR**
8 **WILL NOT COMPLY WITH ANY COMMISSION RULE OR REGULATION.**

9 In its Request, Panda apparently argues that part of the order to show cause must
10 direct APS to comply with Rule 1606(B). However, APS has stated as far back as the
11 Procedural Conference on December 5, 2001, that it would comply with Rule 1606(B) if
12 the Commission were to deny APS’ Request for a Partial Variance, even though APS
13 believes that this result would not be in the public interest. APS has never stated that if the
14 Commission denied its Request for a Partial Variance, it would simply ignore that
15 outcome.³ Accordingly, the underpinning of Panda’s Request is legally premature as a
16 matter of law in that APS has not violated Rule 1606(B)—a rule that even Panda admits
17 does not take effect until January 1, 2003.

18 Ironically, Panda’s own Request demonstrates the deficiency of its argument. In its
19 Request, Panda notes that competitive bidding processes have been undertaken by electric
20 utilities on an accelerated basis in Virginia (71 days) and by Arizona Electric Power
21 Cooperative (4 ½ months). (Panda’s Request at p.9.) Indeed, citing the Virginia
22 experience, Panda claims that a competitive bid process can be “easily” completed in
23 three months. (*Id.*) The factual precedent discussed by Panda suggests that APS could
24 implement a competitive bidding program in June 2002, or even later, to comply with

25 ³ See, for example, the Transcript of the December 5, 2001 Procedural Conference in Docket No. E-
26 01345A-01-0822, at page 72.

1 Rule 1606(B) if the Commission denies APS' Request for a Partial Variance.⁴
2 Accordingly, as a matter of law, Panda cannot establish now that APS will violate Rule
3 1606(B) in the future and that an order to show cause is thus warranted today.

4 **IV. PANDA'S ARGUMENT REGARDING FEDERAL APPROVAL**
5 **OF THE PROPOSED PPA IS LEGALLY INCORRECT.**

6 In a diversionary attack on APS' filing, Panda also claims that if APS does not
7 immediately conduct an RFP, it will be unable to obtain approval of the proposed
8 Purchase Power Agreement from the Federal Energy Regulatory Commission ("FERC")
9 under existing market-based rate authority. (Panda's Request at Section III.) However,
10 this entire argument is simply wrong. In fact, Panda failed to cite any of the directly
11 relevant FERC decisions that have already decided this issue.

12 Specifically, Panda relies on *Boston Edison Company Re: Edgar Electric*
13 *Company*, 55 FERC ¶ 61,382 (1991), which addresses the standard that FERC applies to
14 transactions at market rates between affiliates that have not mitigated the potential for
15 benefits to be transferred from a traditional utility affiliate's captive retail and wholesale
16 customers to its shareholders. *Boston Edison*, however, does not apply to Pinnacle West or
17 its affiliates (the "Pinnacle West Companies") because FERC has already determined that
18 the Pinnacle West Companies have mitigated any potential for affiliate abuse. Indeed,
19 FERC has expressly authorized the Pinnacle West Companies to transact with each other
20 and has eliminated all relevant blanket tariff provisions prohibiting inter-affiliate
21 transactions. *See Pinnacle West Capital Corporation, et al.*, 91 FERC ¶ 61, 290 (2000),
22 *reh'g denied*, 95 FERC ¶ 61,300 (2001); *Pinnacle West Energy Corporation*, 92 FERC ¶
23 61, 248 (2000), *reh'g denied*, 95 FERC ¶ 61,301 (2001). FERC has also specifically
24 determined that APS need not seek separate authorization for each affiliate transaction,

25 ⁴ Additionally, Panda's apparent attempt to use an order to show cause to impose "rules" on the
26 competitive bidding process that are clearly not in the Commission's Electric Competition Rules is both
inappropriate and irrelevant to APS' Request for a Partial Variance.

1 such as the PPA. *See Pinnacle West Capital*, 91 FERC at 61,999 (“[APS’] application in
2 this proceeding (seeking authority to engage in affiliate sales at market-based rates)
3 constitutes the separate filing under section 205 that is required by the Commission.”); *see*
4 *also id.*, n. 20. Therefore, no further substantive review by FERC will be required for the
5 proposed PPA.

6 In fact, although the Pinnacle West Companies are required to submit to FERC
7 wholesale power contracts, including the proposed PPA, contracts submitted pursuant to
8 previously approved blanket tariffs granting market-based rate authority are not traditional
9 rate filings under Section 205 of the Federal Power Act. Rather, they are informational
10 filings submitted in response to the filing requirements contained in the orders authorizing
11 the Pinnacle West Companies’ authority to transact at market-based rates. *GWF Energy*
12 *LLC*, 97 FERC ¶ 61,297 (2002). Because FERC has already accepted for filing the
13 market-rate tariffs that permit the Pinnacle West Companies to engage in inter-affiliate
14 sales at market-based rates, FERC is not required to find that individual power sales
15 agreements filed under the previously approved rates are just and reasonable under
16 Section 205 of the Federal Power Act. Moreover, the filing of new agreements under the
17 existing blanket tariffs “does not serve as a vehicle to challenge the justness and
18 reasonableness of either the agreements themselves or the underlying market-based rate
19 authority.” *Id.* *See also, Pinnacle West Capital Corp.*, 91 FERC at 61,999 and n. 20.

20 V. CONCLUSION

21 Competitive bidding under Rule 1606(B) was never contemplated or required
22 absent the divestiture of APS’ generating assets, nor can Rule 1606(B)’s competitive
23 bidding be conducted in parallel with APS’ Request for a Partial Variance. They are
24 mutually exclusive resource acquisition strategies. The Commission cannot meaningfully
25 or prudently consider the competitive bid question before addressing the issues raised in
26 APS’ Request and certainly must realize that the proposed PPA would not constitute

1 Pinnacle West's "bid" in a competitive process. These premises have not changed from
2 the earlier decision in this proceeding to reject the specific relief that Panda is again
3 requesting. Moreover, APS has not violated any Commission rule, has indicated no
4 intention to violate Rule 1606(B) in the future if the Commission were to deny APS'
5 Request for a Partial Variance, and Panda's own pleading indicates Panda's belief that
6 there is time to first decide APS' case and, if then necessary, conduct whatever amount of
7 competitive bidding the Commission finds appropriate. Finally, Panda's entire argument
8 regarding potential FERC rejection of the proposed PPA is incorrect as a matter of law.

9 In sum, there is simply no legal basis for issuing an Order to Show Cause at this
10 time. Accordingly, APS respectfully requests that the Chief Administrative Law Judge
11 deny Panda's Request for an Order to Show Cause in its entirety.

12 RESPECTFULLY SUBMITTED this 29th day of March 2002.

13 SNELL & WILMER L.L.P.

14 

15 Thomas L. Mumaw

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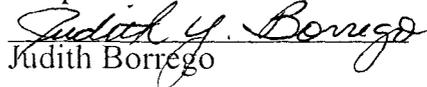
18 Attorneys for Arizona Public Service Company

19 Original and 18 copies of the foregoing
20 filed this 29th day of March, 2002, with:

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All parties of record

27 
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