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BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL
CHAIRMAN
JIM IRVIN
COMMISSIONER
MARC SPITZER
COMMISSIONER

IN THE MATTER OF THE GENERIC
PROCEEDING CONCERNING ELECTRIC
RESTRUCTURING ISSUES

DOCKET NO. E-00000A-02-0051

IN THE MATTER OF ARIZONA PUBLIC
SERVICE COMPANY'S REQUEST FOR
VARIANCE OF CERTAIN REQUIREMENTS
OF A.A.C. R14-2-1606

DOCKET NO. E-01345A-01-0822

IN THE MATTER OF THE GENERIC
PROCEEDING CONCERNING THE ARIZONA
INDEPENDENT SCHEDULING
ADMINISTRATOR

~~DOCKET NO. E-00000A-01-062~~

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

DOCKET NO. E-01933A-02-0069

IN THE MATTER OF THE APPLICATION OF
TUCSON ELECTRIC POWER COMPANY FOR
APPROVAL OF ITS STRANDED COST
RECOVERY

DOCKET NO. E-01933A-98-0471

**RESPONSES OF RELIANT RESOURCES, INC. TO ARIZONA CORPORATION
COMMISSION STAFF'S "LIST OF TRACK B ISSUES"**

1 Reliant Resources, Inc. ("Reliant"), by and through its attorneys, hereby provides the
2 Arizona Corporation Commission ("Commission" or "ACC") with its Comments to the List
3 of Track B Issues referred to in its June 20, 2002 Procedural Order.

4 Reliant Resources, Inc. ("Reliant") appreciates the opportunity to respond to
5 the Arizona Corporation Commission's ("Commission" or "ACC") List of Track B Issues
6 questionnaire. Reliant believes the responses to these questions will provide the necessary
7 framework for constructive and timely solutions to the issues involved in Track B. Our
8 responses follow:
9

10
11 **1. What types of competitive solicitation process(es) should be utilized?**

12 Generally, a number of solicitation processes may be used. Reliant recommends a two-tiered
13 approach to competitive solicitation. First, to mitigate the concentration of assets and
14 concerns regarding market power, approximately one-third of the output of the generation
15 capacity being transferred to Pinnacle West Energy Corporation from APS should be
16 auctioned to wholesale market participants. All qualified bidders could participate in the
17 capacity auction with the exception of Pinnacle West and its affiliates.
18

19
20 The capacity auction would include a variety of capacity products (i.e., baseload,
21 intermediate, cyclic, and peaking) and the resulting capacity contracts would vary in length
22 (i.e., monthly, annual, bi-annual). These capacity contracts would have additional
23 characteristics, such as system transmission entitlement and must-offer requirements. A
24 successful bidder in the capacity auction would receive an entitlement in the form of a call
25 option on a specified amount of capacity. The successful bidders in the capacity auction
26

1 should be required to offer the purchased capacity entitlements into the 1606(B) competitive
2 power procurement process. Reliant envisions the capacity auction to be a short-term,
3 market-based solution to several parties' concerns that one market participant will have a
4 concentration of the available resources. As new generation and transmission resources
5 become available, the need for capacity auctions will diminish.
6

7
8 To comply with the requirement of Rule 1606(B) for APS to acquire at least 50% of its
9 Standard Offer power requirements through a competitive bid process, Reliant envisions a
10 "slice-of-system" competitive solicitation. Participants would be competing on the basis of
11 price to provide a specific percentage of APS' daily Standard Offer load requirement. Under
12 this auction procedure, APS would be purchasing a fixed price product. All qualified market
13 participants, including Pinnacle West and its affiliates, would be eligible to participate in the
14 Rule 1606(B) procurement auctions. Pursuant to the Rule, the remaining portion of APS'
15 Standard Offer requirements would be met through arm's length bilateral transactions. The
16 Commission can rely on the results of the capacity auction and the "slice-of-system" auction
17 as a guide in determining the reasonableness of any bilateral contracts between APS and
18 other parties, including Pinnacle West.
19

20
21 Although a formal RTO is not yet in place, the incumbent utilities already have the capability
22 to buy and sell capacity and energy from third parties. Interim protocols will need to be in
23 place for any competitive solicitation process, until a RTO is in place. The interim protocols
24 can be designed to accommodate capacity auctions and slice of system sales, as well as RFPs
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a. *When should the competitive solicitation begin?*

Immediately after or as part of the resolution of this docket, stakeholder workshops should begin to develop appropriate protocols for both the capacity auction and the slice-of-system competitive solicitation. The protocols should include the procedures of resource scheduling, unity commitment and dispatch, provision for imbalance energy, ancillary services and associated settlement procedures. Shortly after the protocols are in place, the capacity auction should occur. The slice-of-system auction should occur within three months of the capacity auction. Delivery of the capacity auction products should begin at the same time as delivery of the slice-of-system products. We envision delivery to begin in July 2003.

The competitive solicitation should provide for staggered delivery dates and varying contract term lengths. The initial solicitation should provide for delivery beginning in July 2003, and have contract terms extending no longer than three years. The companion solicitations should establish an initial delivery date of July 2005 and July 2006, and should provide for varying contract lengths in the range of 2-4 years, 5-7 years, and 10-15 years. The utilization of multiple delivery dates and varying contract term lengths will allow bids to include additional proposed generation as it becomes available.

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b. *How will the competitive solicitations be disseminated?*

A capacity auction for entitlements to 33% of the generation assets transferred from APS to Pinnacle West should be made available as soon as protocols for solicitation are completed. Shortly thereafter, a load auction for 50% of the Standard Offer load of APS should be held. Reliant envisions this process to be completed by the middle of 2003. Additional solicitations will occur over time as previous supply contracts expire.

c. *What percentage of a utility's power requirements should be obtained through a competitive solicitation process?*

As required by Rule 1606(B), 100% of APS' Standard Offer load should be obtained competitively with not more than 50% through arms length bilateral contracts. To the extent the Commission concludes the circumstances and issues being addressed in Track A necessitate delaying full competition for a short period, the Commission should provide a firm schedule by which time full competition will be achieved. Testimony in Track A indicates that as much as 4000 MW of uncommitted capacity is scheduled to come on line within Arizona by the end of 2004.

1 *d. Should the percentage of a utility's power requirement be obtained through the*
2 *competitive solicitation process be established at one time or should it be phased-in.*

3
4 As prescribed in Rule 1606(B), Reliant expects that a minimum of 50% of Arizona's
5 Standard Offer load would be available via the competitive solicitation. However, as the
6 market evolves in Arizona, it may be efficient to phase-in additional procurement via slice-
7 of-system load auctions. It is also important to note that during the initial procurement,
8 delivery for some portion of the load should reflect staggered delivery dates over the next 3 –
9 5 years.

10
11
12 *e. How will the competitive solicitation percentage be calculated?*

13
14
15 Rule 1606(B) already requires a minimum of 50% of the Standard Offer load be made
16 available for competitive procurement. To the extent that the market would support
17 additional load via competitive solicitation, the Commission should approve such increases
18 in solicitation to bring additional benefits of competition to Arizona's ratepayers.

19
20 *f. Will a utility be subject to penalties if it does not meet the competitive solicitation*
21 *percentage?*

22
23
24 This would depend on the reason for not meeting the competitive solicitation percentage. If a
25 utility fails to proceed in good faith, then a penalty, such as a disallowance of some power
26

1 costs, may be appropriate. If a utility is unable to meet the competition solicitation
2 percentage due to system constraints or unfavorable bids, as determined by the Commission,
3 then no penalty would be appropriate. Systems should be designed and implemented as
4 quickly as possible to facilitate moving to full competition as currently required by Rule
5 1606(B).
6

7 *g. If a utility exceeds the annual competitive solicitation percentage, will the excess*
8 *carry over to next year?*
9

10 No. Contracts would be staggered in length and initial delivery dates. Any substantial
11 deviation from the Commission approved schedule would need to be approved by the
12 Commission after consideration of the impacts on the competitive market as a whole. There
13 could be bandwidths that would build-in flexibility.
14

15
16 *h. What requirements, if any, should be imposed on the purchase of power that is*
17 *obtained outside of the competitive solicitation process?*
18

19 All purchases should be through the competitive process. If the Commission approves a
20 phase-in process, then such purchases whether from affiliates or out of market should be
21 strictly limited to time and quantity as necessary to accomplish the transition to competition
22 as quickly as possible. Any transaction with an affiliate must be subject to all appropriate
23 affiliate transaction and code of conduct rules. Any purchases secured outside the
24
25
26

1 competitive solicitation process should be subject to comparison with prices and terms
2 secured through the competitive solicitation process.

3
4 *i. What are the time frames for initiating and completing the steps of the competitive*
5 *solicitation process?*
6

7
8 The move to competitive solicitation should begin with the resolution of Track A and Track
9 B issues. Competitive solicitation protocols should be determined by stakeholder workshops
10 as soon as possible, preferably not later than March 2003. Delivery of competitively
11 procured power should begin no later than June 2003 for at least a portion of the APS
12 Standard Offer load.
13

14
15 *j. Who will determine the components of each utility's portfolio of competitively*
16 *solicited purchases?*
17

18 While the utility must be provided sufficient flexibility to design the content of its portfolios,
19 the Commission should provide general parameters to ensure transparency, to counter market
20 power issues and ensure compliance with Rule 1606(B). Details of those parameters should
21 be a primary focus of the Track B workshops.
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k. What are the criteria and the process for determining which offer(s) in response to competitive solicitations should be selected by a utility?

In Reliant's proposal, the terms of service are standardized for each like product. Therefore, the only necessary criteria to determine the offer to select to serve the competitive solicitation is price. An independent third party evaluator should determine the "winning" offer. The Commission would then give final approval to the results based upon a predetermined set of criteria.

l. What mechanism will be in place for dispute resolutions related to competitive solicitations?

The competitive procurement rules should be designed to avoid disputes during the procurement process. As mentioned above, an independent third party evaluation of the winning offers with final approval from the Commission is suggested. Any dispute resolution mechanism should be timely and definitive. After the fact disputes would be treated like any other contractual dispute.

m. What protections will be in place to maintain the confidentiality of utility and participant information?

These protections are best decided in stakeholder workshops to determine the appropriate competitive solicitation protocols after the completion of this docket. However, Reliant

1 suggests that for the sake of market transparency, the final price in any competitive
2 solicitation under our proposal be made publicly available. The party or parties serving this
3 competitive solicitation may or may not be made public. To the extent that the terms of
4 service are different for non-standard contracts, those terms should not be made public.
5

6
7 *n. In the event that a supplier of power defaults on the obligation to provide the power,*
8 *how will replacement energy be obtained?*

9 In the short-term, replacement power could be procured from the spot market. As soon as
10 possible after the default, the defaulting party's contract should be made available for
11 competitive solicitation.
12

13
14 *o. How should the competitive solicitation process factor alternative delivery and*
15 *transmission points?*
16

17 The testimony in Tract A has highlighted the importance of the location of generation. The
18 competitive procurement process should encourage solicitations to replace RMR units and
19 in-area generation. The competitive procurement process should weight those offers that
20 address system constraints and that enhance reliability, replace older, less efficient generation
21 and reduce transmission congestion. This is an area that should be a primary focus of the
22 Track B workshops.
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p. *Will the competitive solicitation process utilize the "Western Systems Power Pool umbrella agreement" or similar agreements?*

Yes. The competitive solicitation process should utilize the "Western Systems Power Pool umbrella agreement" or similar agreements (e.g., EEI) customized as necessary for the conditions in Arizona and any regional authorities (e.g., an RTO) ultimately developed for the region.

q. *What are the appropriate contract duration periods?*

For a balanced Standard Offer service portfolio, the contract should have staggered delivery dates and varying lengths, the contract duration should vary between 1 and fifteen years with an average duration between 5 and 7 years. In recognition of the incumbent utilities' current concentration of resources, the average duration of contracts may need to be shorter initially.

r. *What are the appropriate delivery dates?*

While not firm, the first delivery date should be within 6 months of the completion of this docket. Further delivery dates should be staggered to ensure a level playing field for all current and potential participants. In the long-term we envision that competitive solicitation will rotate such that a reasonable amount of load (e.g., between 15 and 30% of the total load) would be bid-out on a regular basis every 2 to 3 years.

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s. *Will demand-side management options be allowed to compete?*

Competitive solicitation should not preclude demand from bidding for Standard Offer load. Demand should be required to participate under the same terms and conditions as other market participants in the competitive solicitation.

t. *Will the costs for local transmission upgrades for proposed projects be directly assigned to each bid or included as general transmission costs?*

Proposed generation projects will be responsible for connecting to the transmission grid. Upgrades to the transmission system beyond that should be included as general transmission costs.

u. *Will there be a price ceiling for bids?*

There should be no price ceiling for bids in the competitive solicitation, unless determined necessary to mitigate short-term influence from the concentration of resources in the incumbent utilities. In the longer-term (2006 deliveries) solicitations are for forward supply and will include many participants Competition is expected to be fierce and any need for a price ceiling will be eliminated. Furthermore, Reliant suggests the Commission retain a role in approving the results of the competitive solicitation.

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v. *Will there be a maximum limit on the number of MW bid by an entity?*

The Commission must consider the concentration of resources of the incumbent utilities and its impact on the competitive market. While a maximum limit on the number of MW bid by an entity is one way to address this concern, as is the Capacity auction proposed by Reliant, in the end, the Commission needs to ensure that the incumbent utility affiliates will be bidding their resources on a competitive basis.

w. *How will the competitive solicitation process be evaluated for future improvements?*

Both the ACC and the participants will be able to track the progress of competitive solicitation. As the market gains experience, the protocols should allow for review and improvement upon the request of the ACC or market participants.

x. *Will the utilization of this process(es) develop an optimal portfolio resulting in the best price?*

The process will develop a portfolio resulting in an efficient price.

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2. What types of products will be subject to competitive solicitation?

Please see Reliant's description under Question No. 1 above as well as our March 29, 2002 and May 29, 2002 testimony in these dockets for a description of the products available through competitive solicitation.

a. *Will the competitive solicitation process include financial and physical options?*

Yes.

b. *Will the competitive solicitation percentage include standard block purchases through a broker or power pool?*

Reliant is not certain of the thrust of this question, but under Reliant's proposal, standard block purchases through a broker or power pool may be permissible.

c. *How will power produced by "must-run" generators be considered in the competitive solicitation process?*

To the extent practicable, plants should be subject to the competitive process. To the extent that competitive alternatives are not available, existing must-run plants should be covered by short-term RMR contracts, until the market provides competitive alternatives.

1 d. *Should the competitive solicitation percentage consist of block energy purchases,*
2 *purchases shaped like the utility's load, or a combination thereof.*

3
4 While Reliant believes that in the long run the competitive procurement should consist
5 primarily of purchases shaped like the utility's load, in the short run the competitive
6 solicitation process can consist of a combination of both.

7
8
9 e. *What are the characteristics of the power to be bid (peak/off-peak, energy/capacity,*
10 *etc.)?*

11
12 The capacity auction product is an entitlement to the output of a specific portion of the
13 generation owner's portfolio. Their peak and off-peak capabilities are determined by the
14 specific product and the dispatch schedule chosen by the entitlement holder. The slice-of-
15 system product is a fixed price, full requirements energy product.

16
17
18 **3. What transmission constraints have been identified or anticipated by the utilities that**
19 **will affect delivery of competitively procured power?**

20
21 Staff has identified several transmission constraints in their March 22, 2002 *Staff Report in*
22 *the Generic Electric Restructuring Docket E-00000A-02-0051*. Reliant believes this is an
23 appropriate starting point for discussion of transmission constraints in Arizona that impact
24 the delivery of competitively procured power.
25
26

1 a. *To what extent would transmission constraints affect delivery of competitively*
2 *procured power?*

3
4 In the short term, the constraints could limit the amount of competitively procured power
5 delivered to the constrained areas without appropriate Network Resource designations.
6

7
8 b. *How and when could the constraints be resolved?*

9
10 Over the long-term, new transmission and generation will eliminate most transmission
11 constraint concerns. The Staff report states that the constraints will be partially mitigated
12 beginning in the summer of 2003 and continuing through 2008. Subjecting the RMR
13 generation to the competitive process will assist in determining whether constructing new
14 transmission, retaining existing RMR, building new generation or pursuing load management
15 options are the most economical in the long run.
16

17
18 c. *How will constraints be reflected in bid evaluation?*

19
20 While Reliant agrees that the bid evaluation criteria must reflect locational requirements,
21 their ability to enhance reliability and relieve congestion. Reliant believes this topic must be
22 addressed and resolved in the Track B workshops.
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4. What issues will affect the participants to the competitive solicitation process?

The competitive solicitation process should utilize fair, non-discriminatory terms and conditions. This will facilitate an open and transparent process to foster competition and ensure Arizona ratepayers an efficient and competitive price for electricity.

a. How will potential suppliers become qualified participants in the competitive solicitation process?

The stakeholder workshop process to determine the appropriate protocols will determine the necessary qualifications to become a participant. Items likely to be required include a standard master supply contract, some form of credit requirement, and an entry fee.

b. Will potential suppliers be required to obtain authorization from the Commission?

The Commission could potentially approve the standards for qualification and/or approve applications for qualification. The specifics of this should be determined in the stakeholder workshops to address competitive solicitation protocols.

c. Will potential suppliers be required to submit proposal fees or bonds?

It is likely that potential suppliers will be required to submit some form of credit assurance. This could include posting a bond or letter of credit. The appropriate level of credit should

1 be determined during protocol workshops. Reliant believes that utilities and their affiliates
2 must meet the same credit requirements as other entities.

3
4 *d. How will utility affiliates be treated in the competitive solicitation process?*

5
6
7 If affiliates are eligible to participate in the competitive solicitation process, they should be
8 expected to adhere to any code of conduct and affiliate transaction rules applicable in
9 Arizona. Outside of those applicable rules, they will be treated the same as all other
10 competitors.

11
12 *e. How will utility-owned generating units be treated in the competitive solicitation*
13 *process?*

14
15
16 Reliant understands that the utility will no longer own the generating units. To the extent
17 some generation is retained by the UDC, the nature of the units retained by the UDC needs to
18 be determined before one can determine the appropriate treatment to be afforded the unit(s)
19 in a competitive solicitation process. For example, as discussed above, RMRs should be
20 subject to the competitive solicitation process where practicable. Furthermore, the
21 concentration of resources must be mitigated to provide a level playing field. Reliant's
22 proposal for a capacity auction is a potential approach. At a minimum, the delivery dates and
23 length of contracts must be structured to facilitate competition in the long term.
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f. *Will the Commission keep a list of qualified suppliers?*

If competitive solicitation is expected to be an on-going process, as is proposed by Reliant, it may be in the Commission's best interest to keep a list of qualified suppliers. This will prevent the Commission from having to review full applications for every competitive solicitation. The details of this process can be determined in workshops following the completion of this docket.

5. How will the cost of procured power be recovered by the utility?

Reliant supports the timely cost recovery of power purchased through the competitive process.

a. *What will be the scope, terms, and effect of a utility's purchase power adjustment clause?*

The purchase power adjustment clause should be designed after the competitive procurement process is established because the two are related.

1 **6. If a competitive bid process is adopted, will least-cost planning be used for the**
2 **evaluation of all competitive bids?**

3
4 The bid evaluation process should be based upon price and other factors, such as locational
5 value. Least cost planning is inherent in the competitive marketplace.

6
7 *a. If not, how will the bids be evaluated?*

8
9 Please see response above.

10
11 *b. Will a least-cost planning framework be used to evaluate the benefits of more*
12 *transmission given the location of existing and planned generating units?*

13
14
15 While least-cost planning can be utilized in evaluating the need for additional transmission,
16 the competitive market can also select the most effective solution to transmission issues. See
17 answer to 3 c above.

18
19 **7. How will the potential for the exercise of market power be assessed for competitive**
20 **bids, in order to determine whether or not the bids are reasonably competitive?**

21
22
23 An independent third party evaluator should be utilized to determine the exercise of market
24 power via the competitive solicitation of power for Standard Offer customers in Arizona. In
25 addition, Reliant envisions a role for the ACC to approve the final outcome of any
26

1 competitive solicitation based upon a clearly defined set of criteria. This system of checks
2 and balances should minimize the potential exercise of market power in the competitive
3 solicitation.

4
5
6 a. *If there are not enough competitive bids, will there a re-bid?*

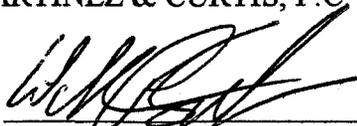
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8 It depends upon what is meant by "not enough competitive bids." If this means that not all of
9 the load available was bid upon, then yes, it should be re-bid with changes to the
10 procurement plan as necessary. However, considering the amount of generation currently
11 on-line in the region, we do not expect there to be a lack of competitive bids.

12
13 b. *Will the utilities be obligated to calculate a price baseline derived from a least-cost*
14 *plan consisting of self-built generation at regulated prices in order to determine if the*
15 *"competitive" bids are likely to save ratepayers money?*

16
17
18 No. As mentioned above, the competitive market substitutes for least cost planning.

19 RESPECTFULLY submitted this 1st day of July, 2002.

20 MARTINEZ & CURTIS, P.C.

21
22 By 

23 Michael A. Curtis
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1 Original and eighteen (18) copies of the foregoing document filed with service list
2 this 1st day of July, 2002 with:

3 Docket Control
4 Arizona Corporation Commission
5 1200 West Washington Street
6 Phoenix, Arizona 85007

7 Copies of the foregoing hand-delivered without a copy of the service list
8 this 1st day of July, 2002 to:

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10 Arizona Corporation Commission
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