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ADMITTED TO PRACTICE IN:
ARIZONA, COLORADO, MONTANA,
NEVADA, TEXAS, WYOMING,
DISTRICT OF COLUMBIA

October 8, 2009

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Arizona Corporation Commission
DOCKETED

OCT - 9 2009

DOCKETED BY
MS

Re: Mesquite Group's Post-Hearing Brief
Arizona Public Service Company
Docket No. E-01345A-08-0172

To Whom It May Concern:

Enclosed for filing are fourteen (14) additional copies of the Post-Hearing Brief ("Brief") on behalf of Mesquite Power, L.L.C., Southwestern Power Group II, L.L.C. and Bowie Power Station, L.L.C. (collectively the "Mesquite Group"). I mailed the original and thirteen copies of the Brief yesterday but inadvertently omitted Appendix "A," which is the prepared Direct Testimony of Leesa Nayudu, referenced within. The enclosed copies consist of the Brief in its entirety.

Also enclosed are two (2) additional copies of the Brief. I would appreciate it if you would "filed" stamp the same and return them to me in the enclosed stamped and addressed envelope. Thank you for your assistance. Please advise me if you have any questions.

Sincerely,

Angela R. Trujillo

Secretary

Lawrence V. Robertson, Jr.

BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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

2009 OCT -9 A 10: 50

A.C. CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF)
 ARIZONA PUBLIC SERVICE COMPANY FOR A)
 HEARING TO DETERMINE THE FAIR VALUE OF) DOCKET NO. E-01345A-08-0172
 THE UTILITY PROPERTY OF THE COMPANY)
 FOR RATEMAKING PURPOSES, TO FIX A JUST) MESQUITE GROUP'S
 AND REASONABLE RATE OF RETURN) POST-HEARING BRIEF
 THEREON, TO APPROVE RATE SCHEDULES)
 DESIGNED TO DEVELOP SUCH RETURN)

Pursuant to the directive of Chief Administrative Law Judge Lyn Farmer, Mesquite Power, L.L.C., Southwestern Power Group II, L.L.C. and Bowie Power Station, L.L.C. (collectively "Mesquite Group") hereby submit their Post-Hearing Brief in the above-captioned and above-docketed proceeding.

I.

INTRODUCTION

A. Background Overview.

The Mesquite Group is comprised of three (3) entities: (i) Mesquite Power, L.L.C., which has owned and operated a 1,250 MW natural gas-fired combined cycle generating facility near Arlington, Arizona since 2003; (ii) Bowie Power Station, L.L.C., which has received a Certificate of Environmental Compatibility and related authorizations to construct a 1,000 MW natural gas-fired combined cycle generating facility near Bowie, Arizona, and (iii) Southwestern Power Group II, L.L.C., the Project Manager for the SunZia Transmission Project, a proposed 460 mile, double-circuit 500 kV transmission facility, which will enable the transmission of electricity into Arizona from renewable energy generation facilities located in New Mexico.¹

¹ Tucson Electric Power Company and the Salt River Project are also participants in the SunZia Transmission Project.

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1 The members of the Mesquite Group participate as actual and prospective sellers in the
2 competitive wholesale power supply market in Arizona. Originally, their participation relied
3 upon conventional sources of generation, such as natural gas-fired combined cycle electric
4 generation facilities. In more recent years, the members of the Mesquite Group (or affiliated
5 entities) have begun to include generation projects which utilize renewable energy technology in
6 their respective business plans and marketing activities.

7 Arizona Public Service Company ("APS") has been and continues to be a major
8 participant and purchaser in the competitive wholesale power market in Arizona. As a
9 consequence, APS' financial condition, as reflected in its credit metrics and bond ratings, is of
10 substantial interest and concern to the members of the Mesquite Group. Simply stated, APS'
11 creditworthiness (or lack thereof) has a direct and substantial bearing (i) upon whether potential
12 sellers, including the members of the Mesquite Group, are able to extend long-term credit
13 arrangements to APS; and, if so, (ii) upon what terms and conditions. In that regard, the
14 members of the Mesquite Group have actively participated in all of APS' emergency and
15 permanent rate cases since 2003.

16 In addition, APS' creditworthiness is also of critical importance to its ratepayers, its
17 shareholders and the State of Arizona as a whole. As the evidentiary record in this proceeding
18 discloses, APS does not own enough generation resources to fully satisfy the requirements of its
19 customers for electric service. APS witness Guldner characterized this as a "net short position"
20 for the company. As a consequence, APS must look to the competitive wholesale electric market
21 to supply a significant portion of its electric power resource requirements, and that situation is
22 likely to continue for the foreseeable future. In that regard, APS has financial and practical
23 limitations upon the amount of debt and equity it can issue at any given point in time; and, its
24 capital expenditure needs are not confined to electric generation facilities. Rather, they include
25 transmission (including substation) and distribution facilities as well.

1 **B. Mesquite Group's Settlement Objectives and Position.**

2 A major objective of the Mesquite Group in this case was to achieve an end result which
3 would place APS in a sound financial position, consistent with the interests of APS' ratepayers
4 and shareholders, thereby ending the pattern of annual rate proceedings and financing instability
5 which has surrounded APS in recent years. A second and related major objective was to retain
6 that policy statement recognition of the importance of the competitive wholesale power market
7 to Arizona's energy future, which the Commission established in the Track "A" and Track "B"
8 proceedings in 2001, and has reiterated on a number of occasions since then. As the Commission
9 is aware, sometimes the most appropriate power resource choice for an electric utility is a long-
10 term Purchased Power Agreement ("PPA") or the acquisition of a developer-build project. Other
11 times, the most appropriate choice may be a self-build decision by the utility. However, each of
12 these power resource options requires a financially sound electric utility.

13 The Mesquite Group believes that the June 12, 2009 Settlement Agreement which is now
14 before the Commission provides for the realization of the aforesaid two (2) objectives, as well as
15 many of the objectives of the twenty-one (21) other signatory parties.² Significant in that regard,
16 is the explicit recognition in Paragraphs 1.4, 1.7, 1.15 and 3.4 of the Settlement Agreement of the
17 direct relationship between APS' financial condition and its ability to avail itself of favorable
18 purchase opportunities in the competitive wholesale power market, incident to the company
19 positioning itself to better serve its customers' future electric service needs.³

20 **C. Scope of Mesquite Group Brief.**

21 As noted above, there are a total of twenty-two (22) signatory parties to the Settlement
22 Agreement. Only one (1) party of the record did not execute the document, and her interest area

23 _____
24 ² Pursuant to the Procedural Order issued on April 25, 2009 in this proceeding, the Mesquite Group filed the
25 prepared Direct Testimony of Leesa Nayudu in support of the Settlement Agreement. Ms. Nayudu is the Director of
26 Origination for Sempra Generation, which owns Mesquite Power, L.L.C.; and, she also was testifying on behalf of
27 Bowie Power Station, L.L.C. and Southwestern Power Group II, L. L.C. In that regard, Ms. Nayudu's testimony
28 specifically addressed Sections I (Recitals), II (Rate Case Stability Provisions), VIII (Equity Infusions), XIII
 (Periodic Evaluation) and XV (Renewable Energy) of the Settlement Agreement; and, it was received into evidence
 as Exhibit Mesquite-1 in the instant proceeding. A copy of that exhibit is attached to this Post-Hearing Brief as
 Appendix "A," and is incorporated herein by this reference.

³ The existence of this direct relationship was also acknowledged by APS witnesses Hatfield and Guldner,
Commission Staff witness Abinah and RUCO witness Johnson during their respective cross-examination by counsel
for the Mesquite Group.

1 is of a discrete nature within the overall context of the Settlement Agreement, albeit an important
2 one. Given the multitude and complexity of questions addressed and resolved through the
3 settlement negotiation process, as well as the number of parties and diversity of interests
4 involved, the Settlement Agreement now before the Commission represents a remarkable
5 accomplishment. In the opinion of the signatory parties, the Settlement Agreement also
6 represents what they believe is a balancing of sometimes competing specific interests which is
7 consistent with the general "public interest."⁴

8 In this Post-Hearing Brief, the Mesquite Group discusses those aspects of the Settlement
9 Agreement which it believes it is best in a position to offer informed comment upon. It will
10 defer to other Signatory Parties to address those aspects or matters which are of particular
11 importance to them and/or within their respective areas of competence or expertise.

12 II. 13 DISCUSSION

14 A. APS' Creditworthiness.

15 As previously noted, Paragraphs 1.4, 1.7, 1.15 and 3.4 of the Settlement Agreement
16 explicitly recognize, and the testimony of several parties also acknowledges, the direct
17 relationship between APS' financial condition and its ability to avail itself of favorable purchase
18 opportunities in the competitive wholesale power market, incident to the company positioning
19 itself to better service its customers future electric service needs. Various provisions throughout
20 the Settlement Agreement are intended to address and significantly improve the "financial
21 condition" aspect of this relationship. Those provisions include the following:

- 22 1. A rate case stability plan which covers the period of January 1, 2010 through
23 December 31, 2014 [Section II, Paragraphs 2.1 through 2.5];
- 24 2. A \$196.3 million non-fuel Base Rate Increase, inclusive of the \$65.2 million interim
25 increase granted in 2008 [Section III, Paragraphs 3.1 through 3.4]; plus, an additional
26 increase of \$137.2 million in base fuel costs [Section III, Paragraph 3.6];

27
28 ⁴ Paragraph 1.16 of the Settlement Agreement summarizes the twenty-three (23) benefits which the Signatory Parties believe the Settlement Agreement provides, and they are listed in six (6) different subject matter categories.

- 1 3. The commitment of APS to reduce its expenses on an annual average basis by \$30
2 million for the period of January 1, 2010 through December 31, 2014. [Section VII,
3 Paragraphs 7.1 through 7.4];
- 4 4. The commitment of APS to complete equity infusions of at least \$700 million
5 between June 1, 2009 and December 31, 2014 [Section VIII, Paragraph 8.1];
- 6 5. The commitment of APS to use its best efforts to (a) maintain investment grade
7 beneficial ratios and a balanced capital structure, and (b) improve its financial metrics
8 and bond ratings [Section VIII, Paragraphs 8.2 and 8.3];
- 9 6. The commitment by APS to prepare and submit to the Commission and the Signatory
10 Parties, within 120 days from Commission approval of the Settlement Agreement, a
11 plan detailing the measures APS intends to take to maintain and improve its financial
12 ratings with the credit rating agencies [Section VIII, Paragraph 8.4];
- 13 7. The allowed deferral by APS for future recovery of a portion of its annual Pension
14 and OPEB costs above or below the test year level in 2011 and 2012, subject to the
15 limitations specified in the Settlement Agreement [Section IX, Paragraphs 9.1
16 through 9.5];
- 17 8. The treatment of Schedule 3 funds received by APS as revenues during the period
18 from January 1, 2010 through the earlier of December 31, 2012 or the conclusion of
19 APS' next general rate case [Section X, Paragraphs 10.1 through 10.7];
- 20 9. The prospect of an adjustment of depreciation rates associated with an extension of
21 the operating license for the Palo Verde Nuclear Generation Station [Section XI,
22 Paragraphs 11.1 through 11.5]; and,
- 23 10. The Performance Measures, Reporting Requirements and Benchmarking Study
24 provisions of the Settlement Agreement, which will augment the opportunity to
25 improve its financial soundness afforded to APS by virtue of the Settlement
26 Agreement as a whole [Section XIII, Paragraphs 13.1 through 13.5].
27
28

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1 Because of the foregoing provisions, the Mesquite Group believes that Commission
2 approval of the Settlement Agreement would afford APS with an opportunity to materially
3 improve its current financial condition (and resultant creditworthiness) in a manner that is
4 consistent with the best interests of APS' ratepayers, APS' investors and those who seek to do
5 business with APS, such as the Mesquite Group. Moreover, APS would be provided with the
6 opportunity to maintain such improvements over time and hopefully end the cycle of frequent
7 general rate cases that has been the pattern in recent years. At the same time, as discussed in
8 Subsection II(B) below, the Mesquite Group believes that the Settlement Agreement provides the
9 Commission and the Signatory Parties with meaningful means for monitoring and measuring the
10 manner and extent to which APS undertakes to maximize such opportunity.

11 **B. Monitoring and Measuring APS' Performance Prospectively.**

12 As noted in Section I(A) above, the Mesquite Group has actively participated in all of
13 APS' emergency and permanent rate cases since 2003, which were characterized by a pattern of
14 annual proceedings surrounded by financial instability. Against that background, the Mesquite
15 Group participated in the settlement negotiations in this proceeding with a desire to end that
16 pattern and place APS on the path to a financially sound condition. However, at the same time,
17 the Mesquite Group was firmly of the view that (i) it was incumbent upon APS to assume a
18 major role in rectifying its present financial circumstances; and, (ii) the Settlement Agreement
19 should expressly codify APS' responsibilities in that regard, and provide various means for
20 monitoring and measuring its progress. In this manner, the improvement of APS' financial
21 condition and creditworthiness could be the result of a balance of combined actions by the
22 Commission and the Company.

23 The Mesquite Group believes that the Settlement Agreement which resulted from the
24 settlement negotiations achieves that balance, and that it provides means by which APS'
25 discharge of its responsibilities may be monitored and measured prospectively by the
26 Commission and the Signatory Parties. Significant provisions in that regard include the
27 following:
28

- 1 1. The commitment of APS to reduce its expenses on an annual average basis by \$30
2 million for the period of January 1, 2010 through December 31, 2014. [Section VII,
3 Paragraphs 7.1 through 7.4];
- 4 2. The commitment of APS to complete equity infusions of at least \$700 million
5 between June 1, 2009 and December 31, 2014 [Section VIII, Paragraph 8.1];
- 6 3. The commitment of APS to use its best efforts to (a) maintain investment grade
7 beneficial ratios and a balanced capital structure, and (b) improve its financial metrics
8 and bond ratings [Section VIII, Paragraphs 8.2 and 8.3];
- 9 4. The commitment by APS to prepare and submit to the Commission and the Signatory
10 Parties, within 120 days from approval of the Settlement Agreement, a plan detailing
11 the measures APS intends to take to maintain and improve its financial ratings with
12 the credit rating agencies [Section VIII, Paragraph 8.4];
- 13 5. The Performance Measures, Reporting Requirements and Benchmarking Study
14 provisions of the Settlement Agreement, which will augment the opportunity to
15 improve its financial soundness afforded to APS by virtue of the Settlement
16 Agreement as a whole [Section XIII, Paragraphs 13.1 through 13.5].

17 In connection with the above, the Commission and the Signatory Parties will be able to
18 ascertain the extent to which APS endeavors to maximize the opportunity provided to it, in the
19 event of Commission approval of the Settlement Agreement; and, they will be in a position to
20 discern the degree of success of APS' efforts. In addition, they will be in a position to examine
21 the appropriateness of measures proposed to be undertaken, and actually undertaken, by APS to
22 discharge its responsibilities under the Settlement Agreement.

23 The following examples are illustrative in that regard. Paragraphs 8.4 and 13.2(g) of the
24 Settlement Agreement require that APS prepare and submit a plan detailing the measures it
25 intends to take to maintain and improve its financial ratings with the credit rating agencies.
26 Copies of this plan are to be provided to both the Commission and the Signatory Parties. As a
27 consequence, recipients of copies of the plan will have an opportunity to offer comment in
28

1 advance of implementation as to their perception of the adequacy and appropriateness of APS'
2 intended measures. This is markedly different from the current situation, where knowledge of
3 APS' intent and/or actions is sometimes obtained after-the-fact.

4 Similarly, the annual Financial Reporting requirements of Paragraph 13.4(b) of the
5 Settlement Agreement will provide the Commission and the Signatory Parties with a significant
6 amount of information on an ongoing basis relating to APS' financial performance moving
7 forward, and the extent to which it is achieving progress towards the financial and capital
8 structure targets established for it in the Settlement Agreement. Again, the Commission and the
9 Signatory Parties will have an opportunity to offer "interim" comment if they so desire, rather
10 than having to wait until APS' next rate case.

11 Finally, and of particular interest to the Mesquite Group, Paragraph 13.4(b)(xii) of the
12 Settlement Agreement provides that APS' annual Financial Reporting filing shall include

13 "Information regarding the Company's level of major capital
14 expenditures, and its consideration of available alternatives in
15 connection with such expenditures for generation facilities."
[emphasis added]

16 The Mesquite Group believes that information of this nature will enable both the Commission
17 and the Signatory Parties to ascertain whether (i) APS is making appropriate capital expenditure
18 decisions of this nature, and (ii) APS is complying with applicable Commission decisions and
19 procurement or resource planning regulations. As noted in Section I(B) above, the Commission
20 has recognized the importance of a competitive wholesale power market to Arizona's energy
21 future for a number of years. This provision of the Settlement Agreement will assist in
22 maintaining the ongoing viability of that market.⁵ In addition, it should assist in insuring that
23 APS makes prudent decisions in connection with the allocation of available funds for competing
24 capital expenditures (generation vs. transmission vs. distribution), given (i) the limitations of
25 funding from debt and equity issues available to APS at any point in time, and (ii) the availability
26 of generation resources through PPAs.

27 ⁵ In that regard, the requirement in Paragraph 15.3 of the Settlement Agreement that APS "initiate a competitive
28 procurement" in the manner therein contemplated, in connection with the "utility scale photovoltaic generation"
project which is the subject of Paragraph 15.3, is consistent with this policy position of the Commission.

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1 for filing this 7th day of October 2009 to:

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4 1200 West Washington Street
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5 A copy of the foregoing Post-Hearing Brief will
6 be mailed or emailed on October 9, 2009 to:

7 Administrative Law Judge Lyn Farmer
8 Arizona Corporation Commission
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Appendix “A”

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**BEFORE THE ARIZONA CORPORATION COMMISSION
RECEIVED**

COMMISSIONERS

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

2009 JUN 30 P 12:26

REC CORP COMMISSION
DOCKET CONTROL

**IN THE MATTER OF THE APPLICATION OF)
ARIZONA PUBLIC SERVICE COMPANY FOR)
A HEARING TO DETERMINE THE FAIR)
VALUE OF THE UTILITY PROPERTY OF THE)
COMPANY FOR RATEMAKING PURPOSES,)
TO FIX A JUST AND REASONABLE RATE OF)
RETURN THEREON, TO APPROVE RATE)
SCHEDULES DESIGNED TO DEVELOP SUCH)
RETURN)**

DOCKET NO. E-01345A-08-0172

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**DIRECT TESTIMONY OF LEESA NAYUDU ON BEHALF OF
MESQUITE POWER, L.L.C., SOUTHWESTERN POWER GROUP II, L.L.C.,
AND BOWIE POWER STATION, L.L.C. ("COLLECTIVELY "MESQUITE GROUP")**

**DIRECT TESTIMONY
OF
LEESA NAYUDU**

1
2
3
4
5 **Q.1 Please state your name and business affiliation.**

6 A.1 My name is Leesa Nayudu, and I am Director of Origination with Sempra Generation,
7 which owns Mesquite Power, L.L.C. ("Mesquite").
8

9 **Q.2 On whose behalf are you providing this testimony?**

10 A.2 I am testifying on behalf of Mesquite, Southwestern Power Group II, L.L.C. ("SWPG")
11 and Bowie Power Station, L.L.C. ("Bowie") (collectively "Mesquite Group"). The
12 Mesquite Group was granted intervention in this proceeding by means of a Procedural
13 Order issued on April 25, 2008. Thereafter, we were active participants throughout the
14 settlement negotiations which resulted in the June 12, 2009 Settlement Agreement that
15 has been filed with the Commission.
16

17 **Q.3 Have the members of the Mesquite Group previously participated in proceedings**
18 **before the Commission in which Arizona Public Service Company ("APS") was**
19 **either the Applicant or a major participant?**

20 A.3 Yes, we have actually participated in a number of proceedings of that nature before the
21 Commission. Included among those proceedings were (i) the Track "A" proceeding, (ii)
22 the Track "B" proceeding, (iii) APS' \$500 million financing proceeding, (iv) APS'
23 acquisition of the Sundance Generating assets, (v) APS' 2003 rate case, (vi) APS' 2005
24 Power Supply Adjuster/Surcharge proceeding, (vii) APS' request for an emergency
25 interim rate increase, (viii) APS' 2005 rate case, (ix) APS' Yuma RFP proceeding, (x) the
26 APS "self-build" moratorium 40-252 proceeding and (xi) this rate proceeding.
27
28

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1 **Q.4 What is the purpose of your testimony at this time?**

2 A.4 Each of the companies comprising the Mesquite Group has signed the Settlement
3 Agreement. Pursuant to the Procedural Order issued by the Chief Administrative Law
4 Judge Lyn Farmer on May 3, 2009, the Mesquite Group is providing this Direct
5 Testimony in support of the Settlement Agreement as it relates to their collective
6 interests.

7
8 **Q.5 What is the nature of those "collective interests" as they pertain to this proceeding?**

9 A.5 The members of the Mesquite Group participate as actual and prospective vendors in the
10 competitive wholesale power supply market in Arizona. Originally, their participation
11 relied upon conventional sources of electric generation, such as natural gas-fired
12 combined cycle electric generation facilities. Examples of these are the 1,250 MW
13 Mesquite generation facility, which has been in service since 2003; and, the 1,000 MW
14 Bowie power station, which is currently under construction. In more recent years, the
15 members of the Mesquite Group (or affiliated entities) have begun to include generation
16 projects which utilize renewable technology in their respective business plans and
17 marketing activities. In addition, SWPG is serving as Project Manager for the proposed
18 Sun Zia renewables energy transmission project, which entails 460 miles of 500 kV
19 double-circuit electric transmission facilities in Arizona and New Mexico.

20
21 **Q.6 Have one or more members of the Mesquite Group participated in competitive**
22 **power procurements conducted by APS?**

23 A.6 Yes. It is my understanding that at various times since 2003 one or more members of the
24 Mesquite Group (or affiliated entities) have participated in Request(s) For Proposal
25 ("RFP") and other forms of competitive procurement conducted by APS, which have
26 involved both conventional and renewable sources of generation.

27
28

1 **Q.7 Does the Mesquite Group believe that the Settlement Agreement adequately**
2 **addresses its “collective interests”?**

3 **A.7 Yes, for reasons I will discuss in my testimony.**
4

5 **Q.8 Please identify those areas of the Settlement Agreement which you will address in**
6 **your testimony.**

7 **A.8 I will be discussing portions of Sections I (Recitals), II (Rate Case Stability Provisions),**
8 **VIII (Equity Infusions), XIII (Periodic Evaluation) and XV (Renewable Energy).**
9

10 **Q.9 Please begin your discussion with Section I (Recitals).**

11 **A.9 Typically, Recitals are used to provide background and context for the document in**
12 **question. In this instance, the language of Paragraphs 1.4, 1.7 and 1.15 is very important**
13 **to the Mesquite Group because it expressly recognizes that APS’ credit ratings directly**
14 **impact both (i) its ability to raise capital on favorable terms for capital expenditures, and**
15 **(ii) its ability to obtain credit on favorable terms from vendors as a purchaser in the**
16 **competitive wholesale electric market. In turn, this latter recognition is reflective of the**
17 **Commission’s previous policy determination that the ongoing existence of a viable**
18 **competitive wholesale electric market in Arizona is in the best interest of both Arizona’s**
19 **electric utilities and their ratepayers. Given APS’ status as the largest electric utility in**
20 **the state of Arizona, and its role as a major purchaser in the competitive wholesale**
21 **electric market, its financial stability and resulting creditworthiness is essential to the**
22 **successful functioning and viability of that market.**

23 As the Commission is aware, sometimes the most appropriate power resource
24 choice for an electric utility is a long-term Purchased Power Agreement or the acquisition
25 of a developer-build project. Other times, the most appropriate choice may be a self-
26 build decision by the utility. Paragraphs 1.4, 1.7 and 1.15 of the Settlement Agreement
27 recognize the importance of providing and preserving this operational flexibility for APS
28 as a stated objective of the Settlement Agreement; and, that recognition enables the

1 Mesquite Group to support the Settlement Agreement. Before concluding my remarks on
2 this subject, I would note that Paragraph 3.4 of the Settlement Agreement also expressly
3 acknowledges the importance of such operational flexibility.
4

5 **Q.10 Please comment on Section II of the Settlement Agreement.**

6 A.10 Section II is entitled "Rate Case Stability Provisions," and that is precisely the intended
7 end result of the provisions contained in that portion of the Settlement Agreement.
8 Recent years have been characterized by a pattern of back-to-back APS rate or rate-
9 related proceedings before the Commission. In addition to the time and expense these
10 proceedings have entailed for all concerned, including the Mesquite Group, this
11 seemingly unbroken chain of proceedings has created uncertainty as to APS' financial
12 circumstances and stability for its ratepayers, its investors, its vendors and lenders, and
13 the financial community as a whole.

14 Against that background, the provisions of Section II are designed to provide a
15 measure of predictability as to the timing of, and appropriate intervals between, APS'
16 filing of rate cases for the next few years. In addition, in combination with the provisions
17 of other sections in the Settlement Agreement, the provisions of Section II are designed
18 to provide APS and the aforesaid stakeholders with a period of revenue stability during
19 the next few years. The Mesquite Group believes that such stability clearly is in the best
20 interests of all concerned.
21

22 **Q.11 Please discuss why the Mesquite Group believes Section VIII is an important part of**
23 **the Settlement Agreement.**

24 A.11 In addition to APS' agreement to complete infusions of at least \$700 million of additional
25 equity between June 1, 2009 and December 31, 2014, this section of the Settlement
26 Agreement contains several additional provisions which the Mesquite Group believes
27 will contribute to the financial stability and strength of APS during the next few years.
28

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More specifically, Paragraph 8.2 contains an express acknowledgement by APS that the Company has a responsibility to exert its "best efforts" to both (i) maintain investment grade financial ratios and a balanced capital structure, and (ii) work to improve its existing ratings with the financial rating agencies. Each of these, in turn, will contribute towards improving the financial stability and creditworthiness of the Company.

In that regard, Paragraph 8.4 provides that APS will prepare and submit to the Commission and the signatory parties to the Settlement Agreement a "plan detailing steps it [APS] intends to take to maintain and improve its financial ratings." The Mesquite Group believes that this is a very important provision, because it will provide the signatory parties with an opportunity to file comments, and the Commission an opportunity to act, in advance of APS beginning to substantially implement its "plan," in the event that the Commission and/or a signatory party or parties believe(s) that APS' "plan" is poorly conceived or lacking in that detail to be desired. In the past, both the Commission and intervenors in APS' interim and permanent rate proceedings have found themselves in a reactive posture, where the options for ameliorative action were narrowly circumscribed by then existing circumstances.

Q.12 In the opinion of the Mesquite Group, is there a relationship between APS' responsibilities under Section VIII of the Settlement Agreement, and the \$30 million annual average reduction in expenditures by APS provided for in Section V of the Settlement Agreement?

A.12 Yes. The Mesquite Group believes it is incumbent upon APS to exert its best efforts to reduce annual expenses, consistent with the ongoing provision of adequate and reliable electric service at reasonable costs, as a part of the company's concerted effort to stabilize its financial performance and improve its credit metrics. The \$30 million average annual reduction in expenses provided for in the Settlement Agreement, and which has been agreed to by APS, is consistent with our philosophy in that regard. It also

1 is our perception that APS intends to meet, if not exceed, that annual target as well as the
2 five (5)-year aggregate target of \$150 million. Achieving these targets should materially
3 assist APS in discharging its responsibilities under Paragraph 8.2.
4

5 **Q.13 Please comment on why the Mesquite Group believes that Section XIII is an**
6 **important part of the Settlement Agreement.**

7 **A.13 Both the language and tone of Paragraph 13.1 establish a conceptual framework which**
8 **the Mesquite Group believes is very important. That paragraph provides as follows:**

9
10 “13.1 The Signatories agree that the Company should exert its best efforts
11 on an ongoing basis to maximize opportunities for financial soundness
12 provided by virtue of this Agreement; and that such efforts by the
13 Company should be subject to periodic evaluation through the use of the
14 Performance Measurements and Reporting Requirements.” [emphasis
15 added]

16 As I have previously indicated, the Mesquite Group executed and supports the
17 Settlement Agreement, because it believes that the provisions of the same provide APS
18 with genuine opportunities to stabilize and improve its financial metrics and
19 creditworthiness to the benefit of its ratepayers, its investors, its vendors and lenders and
20 the financial community as a whole; and, the language of Paragraph 13.1 contains an
21 express recognition to that effect. At the same time, the Mesquite Group believes that
22 APS should be required to periodically report upon the activities it has undertaken to
23 maximize those opportunities, and the results of those activities. Paragraph 13.1 and the
24 provisions of Section XIII as a whole provide for such periodic reporting and evaluation,
25 and thus warrant the Mesquite Group’s support.

26 In that regard, and in addition to the general Financial Reporting provided for
27 under Section XIII (B) (i) through (xii) of the Settlement Agreement, the Mesquite Group
28 is also quite interested in the information to be reported under Paragraph 13.4 (b) (xii),
which requires APS to periodically report

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1 "xii. Information regarding the Company's level of major capital
2 expenditures, and its consideration of available alternatives in connection
3 with such capital expenditures for generation facilities." [emphasis added]

4 The Mesquite Group believes that the periodic reporting of information of the nature
5 contemplated by this provision should enable the Commission and other interested
6 persons (such as the Mesquite Group) to determine (i) whether APS is giving appropriate
7 consideration to power resource alternatives and arrangements available from the
8 competitive market in connection with decisions APS makes to satisfy its power resource
9 requirements; and, (ii) whether APS has complied with the Commission's Recommended
10 Best Practices for Procurement, the Commission's RES regulations, and APS' Renewable
11 Energy Competitive Procurement Procedure to the extent applicable.

12 **Q.14 Please discuss those portions of Section XV of the Settlement Agreement which are**
13 **of direct interest to the Mesquite Group.**

14 A.14 There are two (2), namely, Paragraph 15.1 and Paragraph 15.3. In that regard, as
15 indicated earlier in my testimony, in recent years the members of the Mesquite Group
16 have begun to include generation projects which utilize renewable technology in their
17 respective business plans and marketing activities.

18 Paragraph 15.1 provides that APS will exert its "best efforts" to significantly
19 acquire additional new renewable energy resources with in-service dates by or before
20 December 31, 2015. It is quite conceivable that some of these resources may offer
21 potential business opportunities to one (1) or more members of the Mesquite Group (or
22 affiliated entities).

23 Paragraph 15.3 expressly provides that APS shall file a "plan" with the
24 Commission for a utility scale photovoltaic generation project (with the indicated
25 commencement of construction date) within 120 days from a Commission decision
26 approving the Settlement Agreement. In addition, this paragraph expressly requires that
27 APS "shall initiate a competitive procurement" as the means for identifying and selecting
28 the project which will be the subject of APS' "plan." The competitive procurement must

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comply with APS' Renewable Energy Competitive Procurement Procedure to which I previously referred; and, pursuant to Paragraph 15.3, any signatory to the Settlement Agreement may file comments on APS' "plan." Both the contemplated timing of this particular project, and the use of a "competitive procurement" project selection process are matters in which the members of the Mesquite Group (or affiliated entities) have an interest.

Q.15 Does this complete your discussion of those areas of the Settlement Agreement that you wished to address in your pre-filed Direct Testimony?

A.15 Yes, it does.