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ARIZONA CORPORATION COMMISSION

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March 9, 2010

Re: Line Extension Policies of Electric Utilities, Docket No. E-00000J-10-0044

Dear Interested Parties:

The Commission is preparing to hold workshops on line extension policies for electric utilities. I have been asked by my fellow commissioners to compile the attached Notice of Inquiry ("NOI") in connection with this endeavor. The purpose of the NOI is to solicit input from interested parties so that the Commission may have a fully informed and productive discussion during the workshop process.

Please file all comments in Docket No. E-00000J-10-0044 by **April 16, 2010**.

Thank you,

Commissioner Gary Pierce

- cc. Chairman Kristin Mayes
- Commissioner Paul Newman
- Commissioner Sandra Kennedy
- Commissioner Bob Stump
- Ernest Johnson
- Steve Olea
- Janice Alward
- Lyn Farmer
- Rebecca Wilder
- Amy Love
- Docket Control

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Line Extension Notice of Inquiry

E-00000J-10-0044

In the matter of the Commission's inquiry and potential rulemaking regarding line extension policies of electric utilities, including but not limited to, alternative rate designs related to apportionment and rate recovery of costs of construction and installation of electric utility line extensions, the use of free footage and/or dollar allowances in line extension tariffs, the treatment of proceeds associated with line extensions as contributions in aid of construction (CIAC) and/or revenue, and the ability for third-party vendors to contract to install line extensions for electric utilities.

- 1) What factors should the Commission consider when establishing policies governing electric line extensions?
- 2) Should the principles of cost-causation be the predominant consideration (i.e. requiring costs to be borne by the cost-causer)? If not, what should be the predominant consideration?
- 3) Is it possible for the Commission to devise line extension policies that will result in existing customers subsidizing growth? If so, please provide an example.
- 4) Is it possible for the Commission to devise line extension policies that will result in growth subsidizing existing customers? If so, please provide an example.
- 5) Should growth pay for growth or should it be subsidized by existing customers? If you believe growth should be subsidized by existing customers, in what amount and by what mechanism? Should growth costs be included in base rates and allocated to all customers or should they be allocated to specific customer classes?
- 6) Should growth be required to pay for more than growth? If not, why not? Does APS' existing line extension policy require growth to pay for more than growth?
- 7) Should certain customer groups (such as low income customers, Native Americans on Native American lands, rural customers, etc.) be exempted from an otherwise generally applicable line extension policy? If so, what groups should be exempted and why?
- 8) Should new line extensions have excess capacity? If so, should new customers be required to pay for that excess capacity? Is there a minimum level of electric capacity that all new customers should be required to have irrespective of their own electric demand? If so, what is that minimum electric capacity and what is the potential incremental cost of installing electric lines at the minimum electric capacity versus the customer's actual electric demand? What percentage of line extensions are single-customer installations, versus those that 'grow the grid' to further extend company service capability?
- 9) Explain how any applicable line extension charges should be calculated. Under what circumstances and on what basis, are customer refunds of customer-financed line extensions appropriate? Should the initial applicant be required to pay the total cost with a refunding mechanism if subsequent applicants use any common facility paid for by the original applicant or should the initial customer only be required to pay for the common plant constructed on a pro rata basis?
- 10) Should line extension policies vary depending on the type of customer? In other words should line extension policies vary among the following types of customers:
 - an individual owner, or a small group of owners, of land who will not subdivide their respective properties and are seeking service exclusively for a future residence and not for a development.
 - larger developments, residential subdivisions, or master-planned communities.
 - commercial and/or industrial customers.

11) What were the original considerations for establishing a 1,000 foot line extension policy for APS, and why wasn't the same line extension policy adopted for the other electric utilities?

12) Has the changed character of APS's service territory, i.e. rural/urban mix, removed the need for a line extension subsidy? Given the fact that APS' line extension policy was in place for 50+ years prior to 2006, has the original purpose of this subsidy been served?

13) What is the appropriate time interval for examining subsidy costs? I.e., should subsidies be re-examined every 50 years, 10 years, 5 years or less? Should subsidies be set on a downward glide path or is it appropriate for customers to expect their perpetual existence?

14) Is it inconsistent for the Commission to establish some subsidies that decline over time and some subsidies that do not decline over time? Should the Commission pursue an across-the-board phase out of all subsidies?

15) Should line extension policies for electric utilities be uniform across the state and established via rulemaking or should they be decided on a case by case basis? Should electric cooperatives be treated differently than investor-owned electric utilities? If so, how and why or why not?

16) Should line extension policies for electric utilities be uniform with line extension policies for telecommunications, gas, water and sewer utilities?

17) If the Commission reinstates a free footage allowance for utilities, should the Commission make the new policy retroactive? Should existing customers be compensated who were previously negatively affected by the "no free allowance" policy? If so, how? If one is opposed to retroactive application, is that opposition based in law, policy or both?

18) What costs should be captured in line extension policies? In other words, should line extension policies consider the costs of local facilities, system or backbone facilities, and upgrades to existing facilities?

19) What are the comparative advantages and disadvantages of free footage allowance versus a dollar allowance policies? What would be the cost to ratepayers if the policy were changed to include an "equipment allowance" of a specified amount for only individual residential homeowners?

20) If you are an electric utility, what is your current line extension policy and how has your line extension policy changed over the last fifty years? For APS, what percent of line extensions are installed inside Maricopa County versus outside of Maricopa County? What percentage of line extensions are for residential service versus commercial and industrial service? How many residential line extension estimates has APS provided since 2007 that did not result in a subsequent payment and request for a line extension and service?

21) Please describe the optimal line extension policy that, in your view, best balances the interests of existing and future customers. If you believe that a historical line extension policy (e.g., APS' 1000 free feet line extension policy) is the best, please explain why you believe it is better than alternative proposals (e.g., why is 1000 free feet better than 500 free feet, why is 1000 free feet better than 2000 free feet, etc.)

22) If the optimal line extension policy is different than existing and/or historical line extension policies, should the Commission transition to the optimal policy? If so, how?

23) Please estimate the impact on the economy and new construction from the current line extension policies. What is the impact on land values?

24) Should the Commission be concerned about the potential for new line extensions becoming idle (i.e., "building a line to nowhere")? If so, what provisions should be made to protect against such contingencies?

25) Should an economic model be used to determine the benefits of new customers versus the costs associated with providing line extensions?

- 26) What prompted the changes to line extension policies that go beyond the elimination of free footage allowances? For example, what prompted the change in categorizing line extensions associated with subdivisions from "advances in aid of construction" to "contributions in aid of construction"? If the policy was changed back to an "advance" what would be the impact on electric utility rates? What would be the impact on electric utilities' financial condition?
- 27) How much, if any, additional funding has the change in line extension policies brought to electric utilities?
- 28) Is it possible to change line extension policies without affecting rates? If so, how?
- 29) How do the costs of construction of electric lines compare today with the costs of construction in 2006? How are adjustments made to the costs of construction? Are adjustments made to these costs pursuant to a tariff?
- 30) If the actual costs associated with construction are less than the amounts paid in advance by the developer, are those overages refunded? Can ratepayers obtain the actual costs for materials and the actual labor costs? What is the linear cost difference between buried electric line extensions and overhead, pole-attached line extensions?
- 31) Should the Commission adopt a separate line extension policy for "extraordinary" customers, waiving costs or the like for developer commitments such as, all electric subdivisions, Energy Star homes, or solar installation programs, etc. If so, what should be the criteria for establishing such waivers?
- 32) What flexibility does a utility or cooperative have in interpreting and implementing line extension policies? What flexibility *should* they have?
- 33) What changes in line extension policies can occur in a generic docket? What changes must occur in a rate case?
- 34) Would a change in the line extension policy be detrimental to energy efficiency or DSM goals?
- 35) Would a change in the line extension policy provide an economic incentive to build homes in Arizona? If so, does the benefit of increased construction outweigh the costs of increased rates for all ratepayers? Can any increase in new home construction be quantified?

Accounting Treatment of Line Extension Proceeds:

- 36) Are the funds associated with line extensions treated as contributions in aid of construction (CIAC) or as revenue in your electric utility?
- 37) Should the accounting treatment for any funds collected for line extensions be treated as revenues, as contributions-in-aid of construction, or determined on a case-by-case basis?
- 38) To what extent is the accounting treatment of line extension proceeds relevant to the over-arching policy discussion regarding who pays for the cost of the line extension and whether growth pays for growth?
- 39) Does the shift in accounting treatment from CIAC to revenue result in growth subsidizing existing customers? In answering this question please respond to the following scenarios.

The Commission recently authorized Arizona Public Service Company (APS) to treat all Schedule 3 proceeds as revenue instead of CIAC. Under the settlement agreement approved by the Commission, APS will be allowed to treat as revenue all line extension funds collected during January 1, 2010 and the earlier of December 31, 2012 or the conclusion of its next general rate case. Thereafter, Schedule 3 proceeds will be recorded as CIAC unless otherwise ordered by the Commission. APS' next base rate change from its next rate case will be effective no sooner than July 1, 2012. Assuming that the test year of APS' next general rate case ends on December 31, 2011 and that the Commission allows Schedule 3 proceeds to revert back to CIAC, please answer the following:

- A. A hypothetical new customer pays APS \$25,000 to extend a line 1000 feet to his new home in 2011. Would such a customer be better off having his \$25,000 treated as revenue instead of CIAC? Will such a customer begin to pay for his line “again” once it is placed into rate base and put into APS’ rates on July 1, 2012? To what extent, can it be said that existing customers have been insulated from the costs of growth, if the \$25,000 paid by the new customer, is still placed into APS’ rates on July 1, 2012? To what extent, if any, has this new customer benefitted by having his \$25,000 treated as revenue instead of CIAC? Will this new customer receive any benefits under a revenue approach if he first begins taking service from APS on December 31, 2011? What if he first begins taking service from APS on June 30, 2012, the day before the next APS rate case is decided? To the extent that this new customer is not benefitted by treating his \$25,000 as revenue instead of CIAC, are there other customers who are benefitted? Who are these customers and how have they benefitted? Has the change in accounting treatment resulted in this new customer subsidizing these other customers? Does the shift in accounting treatment result in growth subsidizing existing customers?
- B. A hypothetical developer is developing a new community along the East Verde River, ten miles west of Payson and is paying the full cost (approximately \$6 million) for extending electric services from Payson to the new community. The developer pays the full \$6 million to APS in 2011 and the lines are constructed, and become used and useful to the new community by December, 2011. Are the developer and the residents of this new community better off having the \$6 million treated as CIAC or revenue? Will existing customers have to pay for the \$6 million “again” after it is put into rate base and APS’ new rates become effective on July 1, 2012? Once APS’ new rates go into effect will APS begin to earn a rate of return on the \$6 million that was paid by the developer?

Third Party Vendors:

- 40) Should third-party contractors or vendors be allowed to install electric line extensions? If so, under what circumstances and conditions?
- 41) What are the potential cost-savings of third-party vendors?
- 42) What should be the scope of third-party involvement? (e.g., design; construction; right-of-way acquisition; licenses and permits, etc.)
- 43) How should the host utility ensure quality control? How should warranty, insurance and liability issues be resolved? Who would bear responsibility for accidents, injuries, and fatalities among patrons and workers resulting from substandard work from third-party contractors?
- 44) Can we be certain that any benefits from a third-party contractor option will not be offset by safety and reliability issues?
- 45) Would the inclusion of a third-party option generally promote the “convenience, comfort, and safety, and the preservation of the health, of the employees and patrons” of electric utilities?
- 46) Have other jurisdictions permitted third-party contractors to construct line extensions? If so, what has been their experience? Have there been any “hidden costs” (e.g., design, inspection, and repair costs borne by utilities and ratepayers, but not captured in contractors’ prices), delays, and complaints associated with such work?

Catch-all Question:

- 47) What other questions or issues should be answered or addressed in connection with this inquiry?