

APS ORIGINAL



0000109745

47

Leland R. Snook
Director
State Regulation & Pricing

Tel. 602-250-3730
Fax 602-250-3003
e-mail Leland.Snook@aps.com

Mail Station 9708
PO Box 53999
Phoenix, Arizona 85072-3999

April 2, 2010

Arizona Corporation Commission
DOCKETED

APR -2 2010

DOCKETED BY *MM*

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

RE: IN THE MATTER OF ARIZONA PUBLIC SERVICE COMPANY'S COMMENTS ON
RETAIL ELECTRIC COMPETITION
DOCKET NO(S). E-00000A-05-0051 and E-00000A-01-0630

On January 30, 2009, Arizona Public Service Company ("APS") submitted comments in the above-reference matter. On March 12, 2010, Staff requested that parties update comments in this same matter. APS hereby submits the attached updated comments on retail electric competition.

If you have any questions, please contact Erinn Andreasen at (602) 250-3276.

Sincerely,

Leland R. Snook

LS/sl
Attachments

cc: Barbara Keene
Terri Ford
Steve Olea
Parties of Record

RECEIVED
2010 APR -2 PM 3:03
Arizona Corporation Commission
Docket Control

Copies of the foregoing delivered/mailed
this 2nd day of April, 2010 to:

Ernest Johnson
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Janice Alward
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Lyn Farmer
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Daniel Pozefsky
Chief Counsel
RUCO
1110 West Washington, Suite 220
Phoenix, AZ 85007

Jodi Jerich
Director
RUCO
1110 West Washington, Suite 220
Phoenix, AZ 85007

Jana Brandt
Kelly Barr
Regulatory Affairs and Contracts
Salt River Project
Mail Station PAB 221
P.O. Box 52025
Phoenix, AZ 85072-2025

C. Webb Crockett
Patrick J. Black
Fennemore Craig
3003 North Central, Suite 2600
Phoenix, AZ 85012-2913

John Wallace
Grand Canyon State Electric
Cooperative
120 North 44th Street, Suite 100
Phoenix, AZ 85034

Michael Grant
Gallagher & Kennedy, P.A.
2575 East Camelback Road
Phoenix, AZ 85016

Robert S. Lynch
Robert S. Lynch & Associates
Utility Group
340 East Palm Lane, Suite 140
Phoenix, AZ 85004-4529

Jeri Kishiyama Auther
Robert S. Lynch & Associates
Utility Group
340 East Palm Lane, Suite 140
Phoenix, AZ 85004-4529

David Berry
Western Resource Advocates
P.O. Box 1064
Scottsdale, AZ 85252-1064

Kevin Higgins
Energy Strategies, LLC
215 South State Street, Suite 200
Salt Lake City, UT 84111

Lawrence V. Robertson, Jr.
2247 E. Frontage Road
Tubac, AZ 85646

Michael A. Curtis
William P. Sullivan
Ian D. Quinn
Curtis, Goodwin, Sullivan, Udall &
Schwab, PLC
501 East Thomas Road
Phoenix, AZ 85012

Jay I. Moyes
MOYES, SELLERS, & SIMS
1850 North Central Avenue, Suite
1100
Phoenix, AZ 85004

Vicki Sandler
AzISA
14402 S. Canyon Dr.
Phoenix, AZ 85048

Gary Yaquinto
Arizona Investment Council
3008 N. Civic Center Plaza
Scottsdale, AZ 85251

Christopher Hitchcock
Law Offices of Christopher Hitchcock
PO Box AT
Bisbee, AZ 85603
Peter Nyce
Department of the Army
901 N. Stuart Street, Room 713
Arlington, VA 22203

Michael W. Patten
Jason D. Gellman
Timothy J. Sabo
Roshka De Wulf & Patten, PLC
400 E. Van Buren, Suite 800
Phoenix, AZ 85007

Dan Neidlinger
Neidlinger & Associates
3020 N. 17th Drive
Phoenix, AZ 85015

Dimitrios J. Loloudakis
Energy Management Superintendent
Metro Facilities & Energy Management
2631 S. 33rd Ave
Phoenix, AZ 85009

Russell E. Jones
Waterfall Economidis Caldwell
Hanshaw & Villamana, P.C.
5210 E. Williams Circle #800
Tucson, AZ 85711

Kenneth C. Sundlof, Jr.
Jennings, Stouss & Salmon, P.L.C.
201 E. Washington Street, 11th Floor
Phoenix, AZ 85004

William D. Baker
Ellis & Baker, P.C.
7301 North 16th Street, Suite 102
Phoenix, AZ 85020

Craig Goodman
Stacey Rantala
National Energy Marketers Assoc.
3333 K. Street, NW, Suite 110
Washington, DC 20007

Philip J. Dion
Michelle Livengood
Unisource Energy Company
One South Church Avenue, Suite 2003
Tucson, AZ 85701

Dave Couture
Unisource Energy Company
One South Church Avenue, Suite 200
Tucson, AZ 85701

**Arizona Public Service Company
Electric Competition Comments
Docket No. E-0000A-02-0051
April 2, 2010**

In response to Arizona Corporation Commission (Commission) Decision No. 70485 (September 3, 2008),¹ Commission Staff (Staff) initiated an electric competition workshop process. Arizona Public Service Company (“APS” or “Company”) submitted written Comments on January 30, 2009 in Docket Nos. E-00000A-02-0051 and E-00000A-01-0630. A copy of those Comments is attached as Exhibit A. On March 12, 2010, the Commission Staff requested that interested parties update their earlier comments to the extent necessary.

Simply stated, none of the issues raised in the Company’s January 2009 Comments has diminished in importance or been satisfactorily addressed. The questions remaining from the *Phelps Dodge* decision as to the viability of the essential elements of electric competition under Arizona “fair value” regulation are still unresolved. There are still no clear-cut examples of competition’s success in achieving lower costs for all classes of consumers, greater technological innovation or improved efficiency. Organized wholesale markets and regional transmission organizations in the Southwest, anticipated to emerge in this market when the Competition Rules were adopted, still do not exist. The significant administrative costs to incumbent utilities (let alone the Commission) of reinstating direct access are undiminished.

Then what has changed? In the several years following the legal and regulatory decisions that first called the electric competition rules into question, the Commission has set extensive energy policies that can realistically be achieved only under a fully regulated market. The Commission is in the process of approving both comprehensive resource planning regulations and one of the most ambitious energy efficiency standards in the United States. The Commission has likewise authorized a series of bold steps, beginning with the Company’s 2009 rate settlement and Arizona Sun that commit APS to a significant new expansion of its renewable generation well beyond that required by the RES. Third, distributed generation has taken off as never before thanks to utility rebate programs, tax credits, net metering and a general public enthusiasm for solar energy.

Under retail access, resource planning becomes a frustrating and inefficient exercise at best and a futile one at worst, because the decentralized marketplace

¹ Application of Sempra Energy Solutions LLC for a Certificate of Convenience and Necessity. Docket No. E-03964A-06-0168.

of largely unregulated power plant developers determines what resources should be built and when and for whom, rather than a comprehensive and public regulatory process. Many important policy considerations, such as investment in renewable resources and energy efficiency, the offering of limited income and other public assistance programming, as well as the treatment of externalities, may be ignored or marginalized in a market-driven resource selection process. Large capital-intensive projects, whether they be nuclear or solar, become difficult if not impossible to plan or finance. And the impact of sales lost to potential competitors (almost certainly a select group of the most profitable sales) will compound the impacts of energy efficiency and distributed generation to the detriment of the Company's core base of residential and small business customers. After all, there will remain fixed costs from these investments in renewables, energy efficiency and other infrastructure that will need to be recovered from such customers. Arizona consumers are still paying off the costs related to the last move toward retail electric competition in the late 1990s. If the Commission determines it is appropriate to move forward with competition, it must recognize that a new competitive framework will create a new generation of competition-related stranded costs for consumers to pay.

The public interest is broader than the interests of a handful of new potential competitors, and it is broader than the desires of individual customers for lower rates than those established by this Commission to meet its energy policy goals. The public interest encompasses not only all electric consumers but those who benefit from a wide range of regulatory programs ranging from the RES to energy efficiency to resource planning to the protection of society's most vulnerable members.

Exhibit A



Leland R. Snook
Director
State Regulation & Pricing

Tel. 602-250-3730
Fax 602-250-3003
e-mail Leland.Snook@aps.com

RECEIVED

Mail Station 9708
PO Box 53999
Phoenix, Arizona 85072-3999

2009 JAN 30 P 4 15
AZ CORP COMMISSION
DOCKET CONTROL

January 30, 2009

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

RECEIVED
JAN 30 2009
AZ CORP COMMISSION
Director of...

RE: Arizona Public Service Company's Comments on Retail Electric Competition
Docket No. E-00000A-02-0051 + E-00000A-01-0630

Arizona Corporation Commission Staff held a workshop on retail electric competition on November 14, 2008. At that workshop, Staff requested that the participants file written comments on various topics related to electric competition. Attached are Arizona Public Service Company's comments.

If you have any questions please call Jeff Johnson at 602-250-2661.


Leland R. Snook

Attachments

LS/dt

CC: Barbara Keene
Brian Bozzo
Ernest Johnson
Parties of Record

Copies of the foregoing emailed or mailed
This 30^h day of January 2009 to:

Ernest Johnson
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Janice Alward
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Lyn Farmer
Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

Daniel Pozefsky
Chief Counsel
RUCO
1110 West Washington, Suite 220
Phoenix, AZ 85007

Stephen Ahearn
Director
RUCO
1110 West Washington, Suite 220
Phoenix, AZ 85007

Jana Brandt
Kelly Barr
Regulatory Affairs and Contracts
Salt River Project
Mail Station PAB 221
P.O. Box 52025
Phoenix, AZ 85072-2025

C. Webb Crockett
Patrick J. Black
Fennemore Craig
3003 North Central, Suite 2600
Phoenix, AZ 85012-2913

John Wallace
Grand Canyon State Electric
Cooperative
120 North 44th Street, Suite 100
Phoenix, AZ 85034

Michael Grant
Gallagher & Kennedy, P.A.
2575 East Camelback Road
Phoenix, AZ 85016

Robert S. Lynch
Robert S. Lynch & Associates
Utility Group
340 East Palm Lane, Suite 140
Phoenix, AZ 85004-4529

Jeri Kishiyama Auther
Robert S. Lynch & Associates
Utility Group
340 East Palm Lane, Suite 140
Phoenix, AZ 85004-4529

David Berry
Western Resource Advocates
P.O. Box 1064
Scottsdale, AZ 85252-1064

Kevin Higgins
Energy Strategies, LLC
215 South State Street, Suite 200
Salt Lake City, UT 84111

Lawrence V. Robertson, Jr.
2247 E. Frontage Road
Tubac, AZ 85646

Michael A. Curtis
William P. Sullivan
Ian D. Quinn
Curtis, Goodwin, Sullivan, Udall &
Schwab, PLC
501 East Thomas Road
Phoenix, AZ 85012

Jay I. Moyes
MOYES, SELLERS, & SIMS
1850 North Central Avenue, Suite
1100
Phoenix, AZ 85004

Vicki Sandler
AzISA
14402 S. Canyon Dr.
Phoenix, AZ 85048

Gary Yaquinto
Arizona Investment Council
3008 N. Civic Center Plaza
Scottsdale, AZ 85251

Christopher Hitchcock
Law Offices of Christopher
Hitchcock
PO Box AT
Bisbee, AZ 85603

Peter Nyce
Department of the Army
901 N. Stuart Street, Room 713
Arlington, VA 22203

Dan Neidlinger
Neidlinger & Associates
3020 N. 17th Drive
Phoenix, AZ 85015

Dimitrios J. Loloudakis
Energy Management Superintendent
Metro Facilities & Energy Management
2631 S. 33rd Ave
Phoenix, AZ 85009

Russell E. Jones
Waterfall Economidis Caldwell
Hanshaw & Villamana, P.C.
5210 E. Williams Circle #800
Tucson, AZ 85711

Kenneth C. Sundlof, Jr.
Jennings, Stouss & Salmon, P.L.C.
201 E. Washington Street, 11th Floor
Phoenix, AZ 85004

William D. Baker
Ellis & Baker, P.C.
7301 North 16th Street, Suite 102
Phoenix, AZ 85020

Craig Goodman
Stacey Rantala
National Energy Marketers Assoc.
3333 K. Street, NW, Suite 110
Washington, DC 20007

Philip J. Dion
Michelle Livengood
Unisource Energy Company
One South Church Avenue, Suite 2003
Tucson, AZ 85701

Dave Couture
Unisource Energy Company
One South Church Avenue, Suite 200
Tucson, AZ 85701

Michael W. Patten
Jason D. Gellman
Timothy J. Sabo
Roshka De Wulf & Patten, PLC
400 E. Van Buren, Suite 800
Phoenix, AZ 85007

Arizona Public Service Company
Electric Competition Workshop Comments
Docket No. E-00000A-02-0051
January 30, 2009

In response to Arizona Corporation Commission (Commission) Decision No. 70485,¹ Commission Staff (Staff) initiated an electric competition workshop process. At the first electric competition workshop held on November 14, 2008, Staff requested that interested parties file written comments in response to questions raised by Staff. Specifically, Staff requested comments regarding the adequacy of the current Retail Electric Competition Rules², whether retail electric competition is in the public interest, an identification of the risks and benefits of adopting retail electric competition, Provider of Last Resort issues, and the costs associated with reinstating Direct Access. Additionally, parties were also invited to comment on any other issues believed to be relevant. Arizona Public Service Company (APS) offers the following comments in response to that request.

Retail Electric Competition Rules

Retail electric competition has been under Commission consideration in various proceedings since the mid-1990s. The Commission first began its consideration of retail electric competition in 1994 which led to the adoption of a set of Retail Electric Competition Rules (Rules) in 1996³ and subsequent amendments to the Rules were adopted in 1998⁴ and 1999.⁵

Since that time, the Commission has issued decisions divergent from the provisions of the Rules, such as "Track A."⁶ Track A required APS and TEP to halt divestiture of its generation assets to a competitive affiliate contrary to provisions in the Rules and also required Staff to open a rulemaking to review the Rules. The Track A decision altered what the Commission had believed was a critical component of the Rules that required incumbent utilities to divest their generation assets.

More recently, the Rules were challenged in the Arizona Court of Appeals. In the *Phelps Dodge*⁷ decision, several sections of the Rules were found by the Court to be either unconstitutional or invalid. In addition, in Commission Decision No. 70485 the Commission recently found that prior to issuing Certificates of Convenience and Necessity (CC&N) for Electric Service Providers (ESP) pursuant to the Rules, the

¹ Application of Sempra Energy Solutions LLC for a Certificate of Convenience and Necessity. Docket No. E-03964A-06-0168

² Arizona Administrative Code R14-2-1601 et seq.

³ Decision No. 59943 (December 26, 1996)

⁴ Decision No. 61272 (December 11, 1998)

⁵ Decision No. 61969 (September 29, 1999)

⁶ Decision No. 65154 (September 10, 2002)

⁷ *Phelps Dodge v Arizona Elec. Power Coop.*, 207 Ariz. 95, 83 P. 3d 573 (App. 2004).

Commission should determine whether the public interest would be served by granting CC&Ns and authorizing competitive services in Arizona.

Clearly, much has changed since the adoption of the most recent set of Rules in 1999. Not only have the rules themselves been called into question by the *Phelps Dodge* decision, but retail competitive markets in the United States have not developed as some had anticipated at the time such markets were first created.

Impact of the Phelps Dodge Decision and the Issuance of Competitive CC&Ns

The Court in *Phelps Dodge* invalidated many of the Rules. In most instances, the legal defects were largely procedural and arguably could be cured by the Commission by submitting portions of a modified set of competition rules to the Attorney General for certification. However, two components of the Rules were invalidated on substantive grounds that would require either legislation, or more likely, a constitutional amendment to reinstate them.

The first was mandatory divestiture of generation. Many states have adopted policies that require generation divestiture as a necessary prerequisite for retail competition, and such was apparently the belief of the Commission when it included such a requirement to the Rules. Whether that is still believed to be an important or even essential consideration in determining the public interest of retail competition must be addressed by the Commission.

The second substantive defect in the Rules was the provision allowing for competitive pricing of retail electric services. Pricing flexibility, along with easy supplier entry to and exit from the market, are generally considered the basic essentials of any competitive market system. Whether *Phelps Dodge* permits the requisite amount of pricing flexibility for retail electric competition is something that might only be resolved through further litigation.

Public Interest Concerns and Evaluation of Benefits

In order to determine if retail electric competition is in the public interest, the Commission should first determine what goals it is attempting to achieve through retail electric competition. Is it increased innovation and efficiency? Is it producing the lowest overall prices? Is it to provide customers with additional and more innovative pricing or service options? Is it to drive prices closer to cost and let "the chips fall where they may" in regards traditional notions of equity as between customer classes? Is it merely to provide customer choice among suppliers? Whether or not any of these goals with the exception of the last has been achieved as a result of retail electric competition in other jurisdictions is open to debate, and there appears to be conflicting evidence from a number of sources.

Having established specific goals for retail electric competition, the Commission should next determine how those goals could best be achieved by incumbent utilities and/or

ESPs consistent with the Commission's recently established policies. For instance, the Commission has adopted a statewide renewable energy standard,⁸ encouraged significant development of demand-side management and energy efficiency programs, and is currently in the process of developing new resource planning rules.⁹

Considerations and Impacts - Retail Electric Competition

Wholesale Market Development

An essential element of successful retail competition is a well functioning competitive wholesale market. A key component to adopting competition at wholesale level includes participation in centralized electricity markets operated by independent regional transmission organizations (RTO) or independent system operators (ISO). To date, the southwestern wholesale market has not developed as anticipated when the Rules were adopted as the formation of RTOs or ISOs have not occurred.

Resource Planning Impacts

One of the major risks of implementing retail electric competition is that long-term utility resource planning objectives for transmission and generation are more difficult to achieve within a competitive framework due to the uncertainty of customer migration to and from retail generation suppliers. Resource planning is vital to developing long-term energy plans for the State, and the current competitive market does not purport to provide a suitable alternative to this planning function.¹⁰ With the greater uncertainty and risks of a competitive retail market, both the incumbent utilities and competitive suppliers will reduce financial risk by gravitating towards generation investments with a shorter-term focus. This could result in a decrease in the development of capital intensive baseload assets or renewable energy sources, similar to what occurred during Arizona's first experience with retail electric competition. Under retail competition, the incumbent utility as Provider of Last Resort has a diminished ability to economically plan for long-term resources and can only pass costs of maintaining an excess of supply reserves on to its remaining Standard Offer customers.

In addition, without stringent switching rules, it will become increasingly difficult for the incumbent utility to conduct effective commodity hedging activities due to the uncertainty associated with the customer migration. This will likely expose the Standard Offer customers to increasing levels of generation price risk and volatility.

⁸ Arizona Administrative Code AAC R14-2-1801 et seq.

⁹ Docket No. E-00000E-05-0431

¹⁰ For example, in many RTO/ISO systems, formal capacity markets have been or are being developed, or specific regulatory policies for long-term resource adequacy or procurement have been created, to reduce reliance on spot markets for retail supply.

Renewables and Energy Efficiency

The Commission has established public policy goals of promoting renewables and energy efficiency. Under retail competition, the costs passed on to Standard Offer customers for the development of large renewable projects or energy efficiency projects could be higher as customers leave the incumbent utilities system. However, this impact could be ameliorated if renewable energy standards and demand-side management/energy efficiency obligations are also applied to competitive retail suppliers. Such an approach would eliminate the artificial incentive to leave the incumbent utility as a way of avoiding the incumbent's charges for renewable energy and energy efficiency.

Reinstitution of Direct Access

It has been approximately 8 years since retail competition has been active. APS anticipates that the Direct Access functions that must be established prior to the onset of competition can be reinstated, but will require updates, system changes, or redevelopment due to changes in technology and computer system interfaces. APS will require additional staff and staff training, computer systems, as well as computer programming. The actual costs of reinstating Direct Access functions will depend on the market structure required by any future retail competition rules ultimately adopted by the Commission and the number and type of customers switching to Direct Access.

Along with the updating of systems and processes to facilitate Direct Access, the Statewide Standards and processes established by the Process Standardization Working Group¹¹ (PSWG) for switching customers from Standard Offer to Direct Access should also be revisited.

¹¹Decision No. 61969 (September 29, 1999). The PSWG is a stakeholder group that was established to develop transaction process necessary to facilitate retail competition.