

ORIGINAL



PINNACLE WEST
CAPITAL CORPORATION



0000118745

RECEIVED LAW DEPARTMENT

LINDA J. ARNOLD, ESQ.
Direct Line: (602) 250-3633

2010 OCT 12 P 4: 46

CORP COMMISSION
DOCKET CONTROL
October 12, 2010

Arizona Corporation Commission

DOCKETED

OCT 12 2010

Paul Newman, Commissioner
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

DOCKETED BY

RE: In the Matter of Arizona Public Service Company's Application
for a Solar Electrical Supply Agreement
Docket No. E-01345A-10-0113

Dear Commissioner Newman:

This letter is in response to your letter dated September 29, 2010. Arizona Public Service Company ("APS" or "Company") appreciates this opportunity to provide additional information in clarification of the Company's Application for the approval of the Solar Electrical Supply Agreement ("Solar Agreement") and the Solar Energy Charge. In its Application, APS is seeking approval of the Solar Agreement, under which Freeport-McMoRan Bagdad Inc. ("Freeport-McMoRan") would pay APS a fixed rate ("Solar Energy Charge") for a period of 25 years for the renewable energy from the 15 megawatt photovoltaic plant that will be constructed at Freeport-McMoRan's Bagdad Mine ("Solar Facility"). The Solar Facility will be owned and operated by RE Bagdad Solar 1 LLC, a subsidiary of Recurrent Energy.

In the introductory part of your letter, you stated that, based on your understanding of the proposed Solar Agreement, the energy generated by the Solar Facility would be counted toward the non-residential distributed energy ("DE") component of the Renewable Energy Standard ("RES"), and would meet up to 22% of APS's non-residential DE requirement. While this statement is in fact accurate, it does not reflect the DE programs currently approved by the Commission, and currently deployed by APS which exceed that requirement. In fact, the Commission through APS's 2010 RES Implementation Plan authorized the Company to commit up to \$320 million in lifetime contract value to non-residential customers through its Production Based Incentive ("PBI") program. This budget was approved above and beyond the \$250 million in lifetime contract value for APS's 2008 DE request for proposal projects. The PBI budget, in addition to all of APS's other non-residential DE programs, is anticipated to result in 175,000 megawatt hours ("MWh") in 2011. Using this measure, the Solar Facility only reflects 3.3% of the non-residential DE budget APS anticipates will result from its non-residential DE programs in total. Further, by 2025 the Solar Facility will reflect only 4% of the Company's projected non-residential compliance requirement.

APS • APS Energy Services • SunCor • El Dorado

In your letter, you also asked APS to respond to Chairman Mayes' Proposed Amendment 1, in light of your assumption that there would be other bidders for the non-residential DE allocation over the next 25 years. On October 12, 2010, the Company filed its comments in response to new issues raised at the Commission's Open Meeting held on September 22, 2010, where initial discussions regarding the Company's Application in the above-referenced docket were heard. In that filing, APS provided comments regarding Chairman Mayes' Proposed Amendment 1. Please refer to APS's filed comments (*see* pages 11-12), which will serve as APS's response to your question number 2.

A number of your questions pertained to Freeport-McMoRan in their capacity as a customer of APS. Because Freeport-McMoRan is best suited to answer several of your questions, APS has provided a copy of your letter to a representative of Freeport-McMoRan.

Your questions 1, 3, and 5(b) requested Freeport-McMoRan's customer-specific information. Because APS's responses to these questions include documents that contain customer-specific information that are proprietary and confidential, these documents must be protected from public disclosure pursuant to A.C.C. R14-2-203(A)(2). APS will be providing you Freeport-McMoRan's information as confidential documents, under separate cover, pursuant to an executed Protective Agreement.

Finally, your two remaining inquiries are restated below with the Company's response following each question.

1. You inquired about how Bagdad's Solar Energy Charge (in the Solar Agreement) would benefit ratepayers based on the amount of money paid by Bagdad Mine into the RES relative to Bagdad Mine's energy consumption.

APS believes that the RES rules were carefully crafted to include a DE requirement because the Commission identified both specific and potential benefits associated with non-central station renewable generation. APS believes that all stakeholders recognized that the recipients of DE incentives obtain a benefit greater than they are likely to contribute over a reasonable time period through the RES. For example, a residential customer installing an average sized photovoltaic system today would repay the incentive amount they had received through the RES in approximately 300 years. Through the logic employed in the RES rules, all customers receive an environmental benefit from any other customer's installation of a DE system and, therefore, the magnitude of benefits of the installing customer are counterbalanced by the benefit of adding DE resources to the electric system for all customers.

Specifically, in the case of the Solar Facility and the associated Solar Agreement, APS has worked to return an increased value to the RES beyond that which is received from the installation of any other DE system. The solar premium

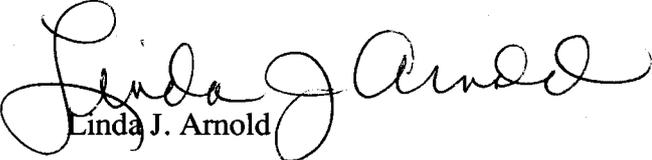
reflected in the Solar Agreement and designed through the REC and Energy model is credited back to the RES and, therefore, generates revenue towards the RES that can work to offset costs for all customers. This is not the case with any other DE transaction.

- 2. In the first part of question 5, you asked APS to provide an explanation of how the energy produced from the Solar Facility counted only towards 'energy' charges rather than 'demand' charges.**

Through the Solar Agreement, Freeport-McMoRan effectively is acquiring an energy hedge for the amount of energy that will be produced by the Solar Facility. Freeport-McMoRan's load characteristics are very different compared to most of APS's customers in that it is a very high load factor user of electricity, i.e., the load operates at high levels of demand for most of the day, including night time hours. Because of the intermittent nature of solar facilities, the Solar Facility will not provide a firm capacity source that will offset demand during all hours of Freeport McMoRan's Bagdad Mine operation. Therefore, there will be no reduction in the levels of demand, and APS must be ready and able to serve the peak demands of Freeport-McMoRan that will not be offset by the Solar Facility.

I hope that the information provided is responsive to your inquiry. Company representatives will be prepared to answer further questions you might have on this topic at the next open meeting.

Sincerely,


Linda J. Arnold

LJA/jlj

cc: Kristin K. Mayes, Chairman
Commissioner Gary Pierce
Commissioner Sandra Kennedy
Commissioner Bob Stump
Lyn Farmer
Steven M. Olea
Janice M. Alward
C. Webb Crockett