

ORIGINAL

EXCEPTION



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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission
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IN THE MATTER OF THE COMPETITION
IN THE PROVISIONS OF ELECTRIC
SERVICES THROUGHOUT THE STATE OF
ARIZONA.

DOCKET NO. RE-00000C-94-0165

**CITIZENS UTILITIES COMPANY
EXCEPTIONS TO PROPOSED RULES**

On February 5, 1999, the Hearing Officer submitted a Proposed Order in Docket No. RE-00000C-94-0165 in the matter of Electric Competition Rulemaking ("Proposed Order"). The following are Citizens Utilities Company's ("Citizens") exceptions to the Proposed Order filed pursuant to A.A.C. R14-3-110(B).

Citizens applauds the Hearing Officer for the extensive work effort of sifting through the substantial filed comments and is pleased that a number of its suggested revisions to the Electric Competition Rules ("Rules") were, in fact, adopted. In the interest of focusing on the most important remaining issues, Citizens is not excepting to every issue that it raised that the Hearing Officer did not adopt in the Proposed Order. Rather, Citizens is submitting exceptions to the Proposed Order in two categories: 1) substantive policy matters that have significant impact on electric competition; and 2) additional matters that can materially improve the functioning of the new industry.

Substantive Policy Matters

The following three exceptions to the Proposed Order address matters that would substantively impact the future competitive electric industry.

1 **Citizens Exception No. 1: The Rules Should Allow All Utility Distribution**
2 **Companies to Offer Metering, Meter Reading, Billing, and Collection**
3 **Services at Tariffed Rates Within Their Certificated Service Areas to**
4 **Competitive Providers.**

4 Under R14-2-1616(B) of the proposed new Rules, Utility Distribution
5 Companies ("UDCs")¹ are prohibited, after January 1, 2001, from providing
6 Competitive Services, which include: aspects of metering, meter reading, billing
7 and collection services within their service areas ("Metering and Billing").
8 Consequently, UDCs cannot provide these services either directly to customers
9 taking competitive generation or indirectly through their competitive providers.
10 Unfortunately, this will likely mean higher costs for customers within their service
11 areas who take competitive services.

12 If this prohibition stands, neither the scale economies inherent in UDC
13 Metering and Billing infrastructure, nor the "yardstick," cost-controlling influence
14 of tariffed rates, will be available to competitive customers. Critics may opine
15 that UDCs will cross-subsidize their Metering and Billing operations to undercut
16 competition. However, because cross-subsidization is not allowed under the
17 Affiliate Rules and this UDC service will still be subject to regulation and rate
18 review by the Commission, this opinion carries no weight. Nor will UDC provision
19 of Metering and Billing limit innovation. Under Citizens' proposal, UDCs would be
20 allowed to offer Metering and Billing services to Energy Service Providers ("ESP")
21 at tariffed rates for customers within their certificated service areas. ESPs will
22 likely seek to differentiate themselves from the competition through value-added
23 features and services within the Metering and Billing arena. If UDCs do not offer
24 the value-added services that ESPs wish to offer customers at prices they deem
25 reasonable then UDCs will simply not get the business.

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¹ Except Electric Distribution Cooperatives.

1 Limited competition results in higher prices and limited service quality.
2 Citizens urges the Commission to modify R14-2-1616 and allow UDCs to be part
3 of the competitive Metering and Billing marketplace within their service areas,
4 through tariffed rates filed with and approved by the Commission.

5 **Citizens' Exception No. 2: The Definition of Stranded Costs Should be**
6 **Modified to Include Those Associated With Opening Metering, Meter**
7 **Reading, Billing, and Collection Services to Competition.**

8 Through its limited definition of stranded costs and its prohibition on UDCs
9 from offering Metering and Billing services, the Proposed Order effectively
10 guarantees that Affected Utilities will incur stranded costs associated with these
11 services without any reasonable means for recovery.

12 Affected Utilities under regulation have invested substantial resources to
13 carry out Metering and Billing functions that are essential to supplying electricity.
14 The opening of these services to competition can render these investments
15 stranded in the same way as above-market generation assets can be stranded by
16 the introduction of competition. Recovery of stranded metering and billing costs
17 is no less appropriate than recovery for stranded generation assets; the same
18 constitutional protections apply. Further, as with generation-related stranded
19 costs, the lack of specific assurance of stranded cost recovery for Metering and
20 Billing assets may well lead to unintended and immediate write-offs under
21 Statement of Financial Accounting Standards ("SFAS") No. 71, because rates
22 would not fully recover the costs of providing service. To reach the stated goal of
23 providing reasonable opportunity for recovery of 100% of stranded costs, the
24 Commission should modify its definition of Stranded Costs to include Metering
25 and Billing assets.

1 **Citizens' Exception No. 3: The Rules Should Allow Purchased Power**
2 **Adjustment Mechanisms for Standard Offer Generation Services Obtained**
3 **Through Competitive Bid.**

4 The Proposed Order's discussion of the provision of Standard Offer
5 generation services suggests that the alternative of providing power based on
6 competitive bids and instituting a Purchased Power Adjustor ("PPA") mechanism
7 is an undesirable option because it "would be expensive and would not lead to a
8 competitive generation market in Arizona within the foreseeable future."²

9 Citizens disagrees.

10 The electric power that Citizens' customers purchase is currently supplied
11 through Citizens' contract with Arizona Public Service ("APS"). Citizens' PPA
12 clause passes the fluctuations in costs onto customers. The pricing and terms of
13 the APS contract were established within an environment in which Citizens had
14 (and did elect from time-to-time) competitive alternatives. Both the purchased
15 power contract and PPA clause were reviewed and approved by the Commission.

16 There is no basis to now suggest that such an arrangement for serving
17 Standard Offer customers does not continue to be a desirable option. In fact, the
18 use of competitive bids in conjunction with a PPA would result in the lowest-cost
19 generation supplies for Standard Offer customers. This is so because:

- 20 1. the competitive bidding process will naturally identify the lowest-cost
21 available sources, and
- 22 2. the ability to pass on variable fuel costs would have the effect of
23 reducing price bids because the suppliers would not be required to
24 shoulder the fuel-cost risk.

25 If UDCs are not allowed to pass on fuel-cost fluctuations, they will naturally tend
26 to seek fixed-price bids that pass the fuel-cost risk onto suppliers, which will
27 result in higher bid prices.

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² Proposed Order, App. C, p. 23.

1 To be clear, the requirement to serve Standard Offer customers "through
2 the open market" after January 1, 2001 would require Citizens to abrogate its
3 existing contract with APS and incur additional stranded costs. Citizens is
4 endeavoring to remedy this situation through contract renegotiations, but these
5 matters are yet resolved. Despite these concerns, Citizens believes that, on
6 balance, the provision of Standard Offer service through competitive bids linked
7 to a PPA is a superior alternative that the Commission should make available.

8 **Additional Matters**

9 In addition to the above substantive policy issues, Citizens urges the
10 Commission to consider the following exceptions to the Proposed Order that it
11 believes will materially improve the functioning of the new competitive industry.

12 **Citizens' Exception No. 4: The Rules should allow UDCs to Read Meters**
13 **for Customers Using Load Profiling.**

14 In the re-writing of R14-2-1616, a key provision was removed which
15 allowed UDCs to use load profiling techniques to read the energy meters of those
16 customers with small loads (less than 20 kW) who are taking competitive
17 services. This provision was established during previous iterations of the Rules to
18 reduce meter-reading costs for these customers. Without this provision, ESPs
19 that acquire small-load customers (e.g. residential customers) would be forced to
20 make special arrangements to have load-profiled meters read, or install
21 expensive metering. Since UDCs must read all meters to bill distribution
22 services, it is sensible to allow UDCs to read load-profiled meters as part of their
23 normal reading cycles. The current provisions of R14-2-1616 would prohibit
24 UDCs from doing so after January 1, 2001. Clearly, this should be changed.

1 **Citizens' Exception No. 5: The Affiliate Transaction Rules Should Allow**
2 **Participation by Affiliates in Joint Marketing, Sales, and Promotional**
3 **Activities as Long as Participation is Based on a Fair and Open Bid**
4 **Process.**

5 In its comments on the Rules, Citizens suggested, in relation to Affiliate
6 Transaction provisions R14-2-1617A4 and 5 and R14-2-1617C.3 (of the prior
7 Rule), that joint activities should be allowed if based on "services governed by a
8 contract resulting from an open competitive bidding process." It would be
9 reasonable for a UDC to consider teaming with a competitive supplier and
10 pursuing various joint activities to assist customers to take full advantage of the
11 competitive marketplace. As long as UDCs use a fair and open bid process to
12 select a competitive supplier to work with, there is no reason to effectively
13 prohibit participation by a competitive electric affiliate. Citizens urges the
14 Commission to adopt its suggested wording for the above-cited sections in the
15 Rules to make this possible.

16 **Citizens' Exception No. 6: The Rules Should Include Specific Deadlines**
17 **for the Director, Utilities Division to Issue of Procedures, Specifications,**
18 **and Standards for Key Factors Impacting the Transition to Competition.**

19 In its filed comments on the Rules, Citizens suggested that key subsections
20 of R14-2-1613, which provide for the Director, Utilities Division to issue certain
21 procedures, specifications and/or standards affecting key aspects of the
22 competitive industry, need specific deadline to allow for an orderly transition.
23 Until many of these key procedures are established, it will not be possible for the
24 various parties to the restructured industry to finalize their own systems and
25 procedures. To remove this uncertainty, subsections K13, K14, K15 and P should
26 include dates-certain by when the various rules and procedures will be
27 established. Citizens suggested April 1, 1999; certainly the date needs to be a
28 soon as possible to allow the maximum period possible for final preparations.
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1 **Miscellaneous Exceptions**

2 Citizens suggests the following changes to the definition of "Must-Run
3 Generating Units" in R14-2-1601(26):

4 "Must-Run Generating Units" are those units that are required to run
5 to maintain transmission and distribution system reliability and to meet load
6 requirements on times of congestion on certain portions of the
7 interconnected transmission grid, ~~as may be determined by the Federal~~
8 ~~Energy Regulatory Commission.~~

9 Must-Run Generating Units may be required to support transmission reliability,
10 even though the grid may not technically be congested. Also, the Control Area
11 Coordinator and/or the Security Coordinator of the Western States Coordinating
12 Council will determine when generating assets must be run for area protection,
13 not the Federal Energy Regulatory Commission.

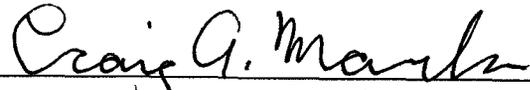
14 In R14-2-1610(A) Citizens notes that FERC Orders 888 and 889 do not
15 speak to retail customer requirements. Therefore, the last sentence of this
16 subsection should be modified by placing a period after "basis" and striking the
17 remainder of the sentence.

18 In R14-2-206(E)3.e. and R14-2-208(F)1., Citizens notes that the
19 references to codes (ANSI C2 and ANSIB31.1) have parenthetical statements:
20 "and no future editions." Unless there are specific requirements in place that
21 would update these subsections in the event of update of the referenced codes,
22 these subsections should be modified to indicate that the "then-current" version
23 of the code is applicable.

24 Finally, Citizens notes that its suggestions for R14-2-1610 concerning
25 obligations for transmission capacity and future transmission planning, which
26 were accepted by the Hearing Officer in Appendix C, Concise Explanatory
27 Statement, were not included in the final text of the proposed Rule. This needs
28 to be remedied.

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1 RESPECTFULLY SUBMITTED this 17th day of February, 1999.
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