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Barbara A. Klemstine  
Manager  
Regulatory Affairs

Tel 602/250-2031  
Fax 602/250-3399  
e-mail: [bklemsti@apsc.com](mailto:bklemsti@apsc.com)  
<http://www.apsc.com>

Mail Station 9909  
P.O. Box 53999  
Phoenix, AZ 85072-3999

February 17, 1999

Jerry Rudibaugh  
Chief Hearing Officer  
Arizona Corporation Commission  
1200 West Washington  
Phoenix, Arizona 85007

Arizona Corporation Commission  
**DOCKETED**

FEB 17 1999

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RE: Docket No. RE-00000C-94-0165, Procedural Order of February 12, 1999

Dear Mr. Rudibaugh:

Pursuant to your Procedural Order dated February 12, 1999, attached are the comments of Arizona Public Service Company regarding the Electric Competition Rules (Amend Decision No. 60977) and the Electric Competition Rulemaking of February 5, 1999.

If you have any questions, please call me at (602)250-2031.

Sincerely,

Barbara A. Klemstine  
Manager  
Regulatory Affairs

BAK:srm

Cc: Docket Control (Original, plus 10 copies)  
Service List as attached

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 JIM IRVIN  
3 Commissioner-Chairman  
4 TONY WEST  
5 Commissioner  
6 CARL J. KUNASEK  
7 Commissioner

8 IN THE MATTER OF THE )  
9 COMPETITION IN THE PROVISION )  
10 OF ELECTRIC SERVICES THROUGHOUT ) DOCKET NO. RE-00000C-94-0165  
11 THE STATE OF ARIZONA )  
12 \_\_\_\_\_ )

13 **EXCEPTIONS OF ARIZONA PUBLIC SERVICE COMPANY**  
14 **TO RECOMMENDED ORDER AMENDING DECISION NO. 60977**

15 Arizona Public Service Company ("APS" or "Company") appreciates the Chief Hearing  
16 Officer's attempt to improve upon the seriously flawed provisions of Decision No. 60977  
17 (June 22, 1998)<sup>1</sup> in his Recommended Order of February 5, 1999 ("Recommended Order").  
18 However, even with the two proposed additional options for the recovery of stranded costs, the  
19 amended decision would still undermine perhaps the only heretofore clearly established principle  
20 of electric restructuring in Arizona: that the Commission would "guarantee" all Affected Utilities  
21 an opportunity for full stranded cost recovery [see Decision No. 59943 (December 6, 1996) at 47] -  
22 a principle that is expressly reiterated in Decision No. 60977 (p. 22): "Affected Utilities should  
23 have a reasonable opportunity to collect 100 percent of their unmitigated stranded costs."  
24 Accordingly, the Company urges the Commission to modify the Recommended Order and adopt  
25 reasonable stranded cost recovery provisions as set forth below.  
26

<sup>1</sup> APS has appealed Decision No. 60977 on the grounds, *inter alia*, that the order was arbitrary, capricious, not based on substantial evidence and that the denial of an opportunity for full stranded cost recovery was an unconstitutional taking of private property in violation of the United States and Arizona Constitutions. That appeal is still pending.

Snell & Wilmer  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

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1  
2 Even as modified by the Recommended Order, none of the four options for stranded cost  
3 recovery would provide APS with a reasonable opportunity to fully recover its stranded costs as  
4 required by law and as recognized in every version of the Electric Competition Rules adopted by  
5 the Commission. APS has previously commented on Option No. 2 (Divestiture/Auction) and  
6 Option No. 3 (Financial Integrity Methodology)<sup>2</sup> and will not repeat its analysis of how those  
7 options are either patently unlawful or systematically, deliberately and arbitrarily prevent the full  
8 recovery of stranded costs.

9 The Recommended Order proposes a new Option No. 1 which is similar, but not identical,  
10 to that advanced by the Chief Hearing Officer in the Recommended Opinion and Order dated  
11 May 6, 1998, in this docket. Unfortunately, this option contains several material defects, some of  
12 which are new to this version of Option No. 1.

13 Option No. 1 would apparently prohibit stranded cost recovery after 2003. As APS  
14 indicated during last year's stranded cost hearing (a contention which was not refuted by any  
15 witness), APS would in fact incur stranded costs through 2006 and well beyond. Without  
16 explanation, the Recommended Order allows no opportunity to recover so much as a dime of these  
17 post-2003 stranded costs. At the very least, this five-year "window" should not start until approval  
18 of a stranded cost recovery plan and the implementation of rates to implement such recovery.

19 Even with the five (5) year recovery "window" allowed by Option No. 1 in the  
20 Recommended Order, APS is given a reasonable opportunity for stranded cost recovery only  
21 during the first year. Thereafter, its stranded cost recovery is reduced 20% for the second year,  
22 40% for the third year, 60% for the fourth, and then by 80% in year five. This averages just 60%  
23 for the five-year period and will be an even smaller percentage of total stranded costs when the  
24

25  
26 <sup>2</sup> See APS' July 10, 1998, Application for Rehearing of Decision No. 60977 and also its Exceptions dated  
May 29, 1998, to the Hearing Officer's then Recommended Opinion and Order.

1 post-2003 years are factored into the total.<sup>3</sup> APS is unaware of any regulatory agency or state  
2 legislature that has attempted to so summarily confiscate such a large percentage of utility equity.  
3 Although APS does not oppose in principle establishing reasonable pre-set goals for mitigation of  
4 stranded costs (in lieu of endless quarreling over this or that specific mitigation measure), what is a  
5 “reasonable” target may well vary from utility to utility, and therefore each Affected Utility should  
6 be allowed to make some specific proposal in that regard as part of its stranded cost filing. The  
7 Company finds this a far better approach than using some arbitrary percentage of disallowance.  
8 Moreover, there is certainly no evidence (and none is cited) that would support the apparent  
9 assumption that Affected Utilities could mitigate (through customer growth or otherwise) almost  
10 50% of their stranded costs during the period 1999-2003 and 100% thereafter.

11 The Recommended Order attempts to justify this confiscation of the Company’s property as  
12 a mere “modification” of the APS proposal that is apparently intended to rectify a perceived  
13 “major flaw” in such proposal. This so called “major flaw” is that there is allegedly little incentive  
14 for APS customers to switch to alternative suppliers unless they can “purchase generation at below  
15 market price.” Recommended Order at 2. Aside from the fact that thousands of customers in  
16 California do precisely that every day and that the market price contemplated in the referenced  
17 APS proposal is an annual weighted average market price, clearly an easier target to beat than a  
18 spot price, APS would ask this more fundamental question. If a customer cannot, in fact, purchase  
19 generation for a lower cost than APS can purchase or generate that same power, why should such a  
20 customer expect or deserve “to reap any savings”? Far from being a “major flaw,” the Company’s  
21 proposal both promotes and reflects fundamental principles of economic efficiency.

22 **II**

23 To remedy the problems identified above, APS recommends that the Commission consider  
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25 <sup>3</sup> The Chief Hearing Officer’s original May 6, 1998, Recommended Opinion and Order proposed a less  
26 draconian “reduction schedule” that would have provided slightly greater stranded cost recovery. No explanation for  
this change is offered.

1 adopting the Recommended Order with several changes.

2 First, the Commission should add a finding of fact and conclusion of law, both of which  
3 would state that "Affected Utilities are entitled to a reasonable opportunity to fully recover their  
4 stranded costs." Such statements would be fully consistent with the Electric Competition Rules  
5 and are required by applicable legal standards.

6 Second, the sentence appearing at Page 2, lines 5-6 of the Recommended Order should be  
7 modified to read as follows:

8 Accordingly, we shall modify Decision No. 60977  
9 to allow each Affected Utility to file a stranded  
10 cost recovery plan of its choice that will allow it a  
11 reasonable opportunity to recover its stranded  
12 costs. Among the options available to each  
13 Affected Utility are the following:

14 This language will make it clear that Affected Utilities are not unreasonably restricted to a specific  
15 method of stranded cost recovery, but rather retain the flexibility to propose a plan for  
16 Commission consideration, and intervenor review, that is tailored to the conditions on their  
17 systems and their particular operational and financial circumstances.

18 Third, the description of Option No. 1 (Net Revenues Loss Methodology) should be  
19 modified to eliminate arbitrary stranded cost disallowance percentages and cut-off dates and  
20 instead encourage a filing Affected Utility to propose its own mitigation plan (such a proposal  
21 could include a specific mitigation factor, a hearing on mitigation measures or some other  
22 alternative). Proposed language amending Option 1 is attached hereto as Exhibit A.

## 23 CONCLUSION

24 APS urges the Commission to take this opportunity to clearly and unequivocally reaffirm its  
25 commitment to allow Affected Utilities a reasonable opportunity to fully recover their stranded  
26 costs.<sup>4</sup> Such a reaffirmation would go a long way toward a final resolution of this contentious

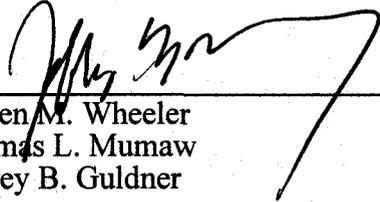
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<sup>4</sup> The Commission has already specifically and expressly authorized 100% recovery of APS' regulatory assets over an eight-year period ending July 1, 2004. See Decision No. 59601 (April 24, 1996). Therefore, APS does not

1 issue in a manner that is consistent with: (1) the Commission's prior regulatory promises, not the  
2 least of which was that made in the original stranded cost regulation concerning recovery of  
3 prudently incurred costs; (2) sound regulatory and economic principles; and (3) well-settled legal  
4 standards regarding regulatory confiscation of utility property.

5  
6 **RESPECTFULLY SUBMITTED** this 17th day of February, 1999.

7  
8 **SNELL & WILMER L.L.P.**

9  
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11 \_\_\_\_\_  
12 Steven M. Wheeler  
13 Thomas L. Mumaw  
14 Jeffrey B. Guldner

15 Attorneys for Arizona Public Service Company

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Snell & Wilmer  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

\_\_\_\_\_ believe the Recommended Order or Decision No. 60977 intended to, or indeed could, alter that recovery.

**CERTIFICATE OF SERVICE**

The original and ten (10) copies of the foregoing document were filed with the Arizona Corporation Commission on this 17th day of February, 1999, and service was completed by mailing or hand-delivering a copy of the foregoing document this 17th day of February, 1999 to all parties of record herein.

  
\_\_\_\_\_  
Sharon Madden

621340.02

**Snell & Wilmer**  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

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## EXHIBIT A

### Option 1 - Net Revenues Lost Methodology

Utilize a Net Revenues Lost Methodology similar to that set forth by APS witness Davis. In general, the APS proposal compares generation revenues with competition versus revenues without competition. The difference, if any, is considered as potential stranded costs. That amount is then allocated among rate classes utilizing traditional cost allocation and rate design principles. Those customers taking service on the standard offer tariff would already be paying their portion of stranded costs. Customers taking competitive generation service would be charged for their portion of stranded costs through a competitive transition charge ("CTC"). ~~That amount will also be separated out in the standard offer to insure that standard offer customers do not pay twice. Under the APS proposal, the potential stranded costs would be spread over all customers including customers added during the year. If there is enough growth relative to customers taking competitive service, all customers could end up with a decrease in rates. However, there would be little incentive for customers to utilize another competitive service as they would have to purchase generation at below market price in order reap any savings. We believe such a result is a major flaw in the APS proposal. As a result we will modify the APS proposal to place the risk/reward of mitigation more directly on the Affected Utilities.~~

We will clearly separate stranded costs into generation related assets and regulatory assets. Any growth in customers will not be part of the customer base used in calculating the generation related asset stranded costs. Any such growth would be considered as mitigation which the Affected Utilities can retain. In turn, the percentage of stranded costs that the Affected Utilities will be permitted collect via the CTC charge will could be reduced each year. ~~We will utilize the customer base of the Affected Utility as of December 31, 1998 to calculate stranded costs for each year. Any Affected Utility choosing this method will be permitted to collect 100 percent of its stranded costs in Year No. 1, from all distribution customers either through a CTC charge to any customer who elects to purchase from competitors; in year No. 2, the Affected Utility will be permitted to calculate its stranded costs over the same December 31, 1998 customer base. However, only 80 percent of the proportionate amount can be recovered in a CTC charge to any customer who elects to purchase from competition. Those remaining on the standard offer will still be paying 100 percent of their proportionate share of stranded costs. Any shortfall the Affected Utility may have from the December 1998 customer base could be more than made up from post 1998 customer growth. In Years Nos. 3, 4, and 5, the Affected Utility will utilize the same methodology only the percentages to be collected via the CTC charge will be 60, 40 and 20 percent respectively in a manner to be determined after a hearing and based on substantial evidence.~~

Because regulatory assets are ~~more difficult for an~~ of Affected Utilities to mitigate cannot be effectively mitigated and as such need to have different treatment, we will permit an Affected Utility to collect 100 percent of the appropriate regulatory assets over its existing amortization period. Further, all existing and future customers should bear their portion of the regulatory assets either as part of the standard offer or as part of the ~~CTC charge. In order to encourage Affected Utilities to make the maximum effort to mitigate regulatory assets, we will~~

begin phasing out any return on such assets after a five year period. For regulatory assets which are receiving a rate of return, such rate of return should be reduced by 20 percent per year so that after five years there would be no return allowed on such assets. As the rate of return is reduced, all rates including those customers on standard offer rates should be reduced accordingly **unbundled rates**. Upon expiration of the amortization period for regulatory assets, standard offer rates ~~should~~ **could** be reduced to reflect the removal of the regulatory assets. ~~If an Affected Utility believes~~ **unless** other costs have increased to offset the removal of the regulatory assets. ~~it shall file a rate case at least a year before regulatory assets are extinguished.~~

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 JIM IRVIN  
3 Commissioner-Chairman  
4 TONY WEST  
5 Commissioner  
6 CARL J. KUNASEK  
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8 IN THE MATTER OF THE )  
9 COMPETITION IN THE PROVISION )  
10 OF ELECTRIC SERVICES THROUGHOUT ) DOCKET NO. RE-00000C-94-0165  
11 THE STATE OF ARIZONA )  
12 \_\_\_\_\_ )

13 **EXCEPTIONS OF ARIZONA PUBLIC SERVICE COMPANY**  
14 **TO RECOMMENDED ORDER AMENDING THE ELECTRIC COMPETITION**  
15 **RULES, A.A.C. R14-2-1600 ET SEQ.**

16 Arizona Public Service Company (“APS” or “Company”) commends the Hearing Division  
17 for undertaking the complex and daunting task of revising the Electric Competition Rules  
18 (“Rules”). APS notes significant improvement in a number of the Rules, both substantively and  
19 from the standpoints of internal consistency and clarity.

20 Although APS has comments or suggestions—often relatively minor points or interpretive  
21 clarifications—on many of the revisions to the Rules, APS will generally reserve such matters for  
22 the forthcoming rulemaking proceeding. APS does, however, believe that the Recommended  
23 Order and proposed revisions to the Rules do not adequately consider several critical arguments  
24 raised in APS’ previous submissions. Additionally, APS has noted certain instances where a rule  
25 revision appears to have broader consequences than apparently intended—some confirmed by the  
26 analysis provided in the Concise Explanatory Statement (“CES”)—or did not fully implement a  
proposed change otherwise accepted in the analysis of the Rules. Some of these latter deficiencies  
require substantive changes to the Rules, which if not made as part of the proposed amendments,  
will be difficult to adopt later without delaying the advent of competition.

Snell & Wilmer  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

1 The Company therefore urges the Commission to modify the Recommended Order and  
2 proposed revisions to the Rules to adopt the Company's comments set forth below and in Exhibit  
3 A, attached hereto.

4  
5 **I. DEFINITION OF "COMPETITIVE SERVICES"**

6 The Hearing Division's reliance on the initially defined term "Competitive Services" [R14-  
7 2-1601(5)] in a number of the proposed revisions to the Rules, rather than having the term  
8 redefined in different parts of the Rules, is certainly appropriate. However, there is an unnecessary  
9 ambiguity caused by defining this essential term solely by a negative reference to another defined  
10 term. Specifically, defining "Competitive Service" as encompassing *all* aspects of retail electric  
11 service that are not "Noncompetitive Services" is impermissibly vague and almost certainly  
12 overbroad, particularly if the finally-adopted Rules include a blanket prohibition on Utility  
13 Distribution Companies ("UDCs") providing any "Competitive Services" after 2000. So defined,  
14 "Competitive Services" arguably includes services never before regulated by the Commission as a  
15 public utility service.

16 APS suggests that the Commission adopt a more precise definition of the term  
17 "Competitive Services" that is both self-sustaining and limited to those formerly-regulated aspects  
18 of retail electric service that may now be provided by an ESP. APS would propose the following  
19 language:

20 "Competitive Services" means the provision of retail electric Generation, Meter  
21 Service (other than those aspects of Meter Service described in R14-2-1613(K)),  
22 Meter Reading Service, or electric billing and collection services (other than joint  
23 or consolidated billing provided by an Affected Utility or Utility Distribution  
Company pursuant to a tariff). It does not include Standard Offer Service or any  
other electric service defined by this article as noncompetitive.

24 This language recognizes the formerly-regulated retail electric services, which are also specifically  
25  
26

1 identified in R14-2-1613(O),<sup>1</sup> while not overly restricting *any* party from offering unregulated  
2 services that may emerge to the benefit of consumers.

3 The Recommended Order itself recognizes that mitigation of stranded cost may be  
4 accomplished by offering a “wider scope of permitted regulated utility services for profit.” R14-2-  
5 1607(A). The proposed definition of “Competitive Services,” however, would all but eliminate  
6 the possibility of an Affected Utility offering such additional services. Further, the separation  
7 requirements and subsequent prohibition on UDCs offering these vaguely-defined “Competitive  
8 Services” after 2000, if adopted, could severely limit otherwise lawful and appropriate business  
9 activities of a UDC, such as home security systems or certain energy efficiency programs. Such  
10 services and programs may be completely unrelated to the regulated utility services intended to be  
11 addressed by the proposed Rules.

## 12 **II. DEFINITION OF “STANDARD OFFER SERVICE”**

13 APS agrees with AEPCO’s prior comments that the Provider of Last Resort requirement  
14 should be limited to customers below a defined annual load. This limitation helps to prevent  
15 “gaming” of the system by larger customers. Thus, APS supports the revision of R14-2-1606(A)  
16 proposed by AEPCO, specifically limiting the obligation of an Affected Utility or UDC to act a  
17 Provider of Last Resort only to customers whose annual usage is 100,000 kWh or less. As  
18 proposed by AEPCO, such a revision confirms that UDCs have the right, but not the obligation, to  
19 provide Standard Offer Service to customers with annual usage of over 100,000 kWh.  
20

21 APS does not believe, however, that the proposed amendment to the definition of Standard  
22 Offer Service in R14-2-1601(34) clearly embodies such a policy. That provision now appears to  
23 define “Standard Offer Service” to categorically exclude customers whose annual usage is more  
24

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25 <sup>1</sup> The strikethrough version of the proposed rules distributed on February 11, 1999 deleted  
26 R14-2-1609 and renumbered the following sections. In these exceptions, APS will reference the  
rules as numbered in the original version of Appendix A.

1 than 100,000 kWh. Such wording could arguably require *all* such customers (presumably after the  
2 phase-in period ends) to switch *en masse* to Competitive Service—an undesirable and perhaps  
3 impossible scenario. This result does not appear to be contemplated by the discussion of the  
4 proposed revision in the CES. Moreover, this result does not reflect the amendments to A.R.S. §  
5 40-202(B)(5) in H.B. 2663, which merely limited the Provider of Last Resort *obligation* to  
6 customers with annual usage of 100,000 kWh or less, and did not otherwise restrict the availability  
7 of Standard Offer Service.

8 APS believes that the decision to remain on an otherwise available Standard Offer Service  
9 or opt for Competitive Service should generally lie with the customer, and not be dictated by the  
10 Rules. Accordingly, APS urges the Commission to delete the phrase “whose annual usage is  
11 100,000 kWh or less” from R14-2-1601(34), but incorporate the limitation into R14-2-1606(A) as  
12 provided in Exhibit A hereto.

### 13 **III. SEPARATION OF COMPETITIVE SERVICES**

14 Rule R14-2-1616 requires Affected Utilities to “spin off” to affiliates not just competitive  
15 generation assets, but *all* Competitive Services. APS previously urged the Commission to limit the  
16 required separation of services from an Affected Utility or UDC to competitive generation only.  
17 There has never been any evidence or testimony presented to the Commission that the compelled  
18 separation of distribution-related activities such as metering and billing from a UDC is necessary,  
19 appropriate, or in any way benefits consumers or the competitive marketplace (as opposed to  
20 metering vendors and independent billing service providers). In fact, such mandated “spin offs”  
21 would reduce permissible economies of scale and increase the cost of service for customers of both  
22 Competitive Services and Noncompetitive Services. For example, the proposed rules would  
23 prohibit UDCs or Affected Utilities from directly providing meter-related services to load profiled  
24 residential customers choosing competitive access after 2000 because metering and billing must be  
25 “spun off” to an affiliate. There is no justification for forcing load profiled customers to change  
26

1 meters, which is not required for such customers to participate in the competitive market. Without  
2 sufficient economies of scale for metering and meter reading for residential customers, such  
3 customers may be foreclosed from the benefits of competition.

4 The CES in the Recommended Order does not evaluate APS' comments of the  
5 inappropriate and unnecessary burdens and limitations imposed by requiring separation of all  
6 Competitive Services. Indeed, such compelled separation of non-generation services is,  
7 understandably, unprecedented anywhere in the country and cannot be rationally justified. APS  
8 thus requests that the Commission consider APS' analysis and adopt the proposed changes to Rule  
9 R14-2-1616 set forth in Exhibit A hereto.

#### 11 IV. AFFILIATE TRANSACTION RULES

12 The affiliate transaction provisions in R14-2-1617 are still confusing, contradictory, and  
13 overly burdensome. Rule R14-2-1617(A)(2) provides that a UDC "may share with its affiliates  
14 joint corporate oversight, governance, support systems and personnel." Section 1617(A)(6) states  
15 that, *except as provided by Section 1617(A)(2)*, a UDC and its affiliate cannot jointly share  
16 directors and officers. However, because directors and officers are, by definition, providing  
17 governance and joint corporate oversight, the express prohibition in Section 1617(A)(6) is either  
18 meaningless or completely negates the intended exception. Indeed, few American corporations,  
19 competitive or regulated, would make significant investments in a subsidiary and not also seek to  
20 control the strategic direction of the subsidiary and ensure that the parent's investment is being  
21 appropriately utilized. Moreover, no party has presented evidence that improper cross-  
22 subsidization or sharing of customer-specific confidential information would reasonably result  
23 from the sharing of such *senior* personnel—the only realistic threat of such conduct is presented by  
24 lower-level staff that actually access such information and are involved in day-to-day transactions,  
25 not those responsible for policy and oversight.

26 Additionally, APS previously recommended that the affiliate transaction pricing provisions

1 in R14-2-1617(A)(7) provide that non-tariffed items regularly sold by a UDC should be transferred  
2 at the market price. The proposed revisions to this rule still provide that the transfer price shall be  
3 the *higher* of market price or fully allocated cost. For goods and services that are regularly and  
4 routinely sold by a UDC, requiring cost allocation determinations each time that a transfer to an  
5 affiliate occurs is overly burdensome and unnecessary. Such a provision could result in the  
6 anomolous situation that other ESPs may purchase the good or service at a *lower* price than a UDC  
7 is allowed to charge its competitive electric affiliate. If the objective of the rule is to prevent a  
8 UDC from unfairly dealing with a competitive affiliate, transferring a good or service at the same  
9 price to all comers satisfies that objective. Raising additional regulatory hurdles when the transfer  
10 involves a UDC's competitive affiliate simply places the affiliate at a competitive disadvantage to  
11 other ESPs. Accordingly, APS requests that the Commission revise proposed rule R14-2-1617 as  
12 suggested in Exhibit A.

#### 13 14 **V. REQUIRED RATE DECREASES**

15 APS previously recommended deleting as moot R14-2-1604(C), which required Affected  
16 Utilities to file a report by September 1, 1998 to detail "possible" mechanisms to provide benefits  
17 "such as rate reductions of 3% to 5%, to all Standard Offer customers." Although APS agrees that  
18 the revision in the Recommended Order of the September 1, 1998 date to November 1, 1999  
19 addressed the mootness issue, APS would ask the Commission to clarify that the replacement of  
20 the words "such as" with "including" was not intended to impose an unlawful *requirement* for a  
21 3% to 5% rate reduction. Arizona law and the Due Process Clause of the Arizona and federal  
22 Constitutions prohibit the Commission from ordering a rate reduction (or that a utility file for a  
23 rate reduction) without conducting a rate case. *See, e.g., Simms v. Round Valley Light & Power*  
24 *Co.*, 80 Ariz. 145, 150-51, 294 P.2d 378, 381-82 (1956). Accordingly, APS proposes that the  
25 Commission delete R14-2-1604(C) or at least clarify R14-2-1604(C) by reverting to the "such as"  
26 language or otherwise indicating through similar language that the reference to rate reductions is

1 intended as an example, rather than a requirement.

## 3 VI. UNBUNDLED TARIFFS AND SPECIAL CONTRACTS

4 The revisions to Rule R14-2-1606(C) and (D) are ambiguous, and at least appear to  
5 contemplate “rate cases” for each of the unbundled billing cost elements. APS understands that  
6 the unbundling will involve the filing of two types of unbundled tariffs: tariffs for Noncompetitive  
7 Services provided to customers receiving Competitive Services from ESPs, and tariffs for  
8 Standard Offer Service, which are “unbundled” solely to provide general information to Standard  
9 Offer customers on the “cost” of each service they receive from a UDC.

10 Rule R14-2-1606(C) discusses Standard Offer unbundling. Under APS’ understanding of  
11 the previous rule for Standard Offer Service, separate tariffs for each “billing cost element” were  
12 not required to meet the unbundled tariff filing requirements. The CES explains the proposed  
13 amendments to the rules as needed guidance and indicates that new tariffs are necessary so that the  
14 Commission can examine the cost elements. APS would urge the Commission to clarify that this  
15 revision is not intended to dictate a “bottom up” rate redesign proceeding for all Standard Offer  
16 tariffs. If the Commission were to require such a bottom up redesign of Standard Offer rates, there  
17 would be significant customer dislocation (all of which would likely be attributed by the customer  
18 to “competition”) and, rather than a three week unbundling hearing, would require a process  
19 spanning several months for each Affected Utility. Further, a bottom up redesign of every “billing  
20 cost element” across each customer class will not provide consumers with any more useful  
21 information.

22 Further, the CES does not explain why such a revision would be at all prudent. The  
23 Commission will already have the authority to examine the “cost elements” in the Affected  
24 Utilities’ unbundled tariffs during hearings later this year. Additionally, as was proposed in APS’  
25 settlement last November, a more workable alternative, should the Commission determine that a  
26 bottom up redesign of all Standard Offer rates is necessary, would be to provide for a revenue

1 neutral rate design proceeding at some point after competition has begun. Such a deferred  
2 proceeding will not bog down competition while each Affected Utility puts on a full blown rate  
3 case. Accordingly, APS requests that the Commission return to the original language in R14-2-  
4 1606(C)(2), or to rephrase the proposed rule to clarify that separate, fully-cost allocated unbundled  
5 Standard Offer tariffs are not required for each billing cost element for each customer class.

6 Rule R14-2-1606(D) then provides that Affected Utilities and UDCs shall file “an  
7 Unbundled Service tariff which shall include a Noncompetitive Services tariff.” Again, this  
8 revision does not appear to distinguish between unbundled tariffs for Standard Offer Service and  
9 unbundled tariffs for Noncompetitive Services, which APS anticipates will necessarily be  
10 somewhat different. For the reasons stated above, APS would suggest that the Commission revise  
11 the language in R14-2-1606(D) to conform with APS’ previously proposed revision (which the  
12 Hearing Officers appear to accept in the CES), and as is set forth in Exhibit A.

13 With regard to the rejection of a Purchase Power Adjustment mechanism in Section  
14 1606(B) of the proposed rule, the CES cites only the supposed diminution in incentives for “least  
15 cost” purchases attributable to such a mechanism. This argument ignores the fact that all electric  
16 and gas distribution utilities presently regulated by the Commission (including every Affected  
17 Utility except APS and TEP) have this sort of mechanism. The two Affected Utilities without  
18 such mechanisms are essentially forced by the Rules to become UDCs but without the rate  
19 mechanisms enjoyed by other UDCs. Moreover, requiring UDCs to be providers of last resort  
20 without the ability to adjust their rates for an increasingly volatile bulk power market will not  
21 necessarily incent them to pick the “least” cost source, rather than the “most stable” cost source.

22 APS also objects to the newly-added prohibition of any special discounts or “contracts with  
23 term” being made available by a UDC. First, there has been no evidentiary showing of why such a  
24 prohibition is either necessary or appropriate. Second, restricting UDCs from negotiating such  
25 contracts removes an important stranded cost mitigation measure and results in *diminished*  
26 competition. The amended rule simply adds an additional burden on a UDC to design more tariffs

1 for narrower customer classes, rather than dealing on a case-by-case basis with such sophisticated,  
2 economically-powerful customers—a manner recognized as appropriate by the Commission for  
3 many years. These large consumers, more than anyone, are able to take advantage of competition  
4 in the marketplace. Contrary to NEV’s assertion, such contracts in no way “prevent consumers  
5 from accessing a competitive option.”  
6

### 7 **VII. CTC ASSESSMENT FROM “DISTRIBUTION” CUSTOMERS**

8 In implementing a change proposed by RUCO to Rule R14-2-1607(F), the proposed rule  
9 now permits the collection of a Competitive Transition Charge (“CTC”) from customers using the  
10 “distribution system.” APS understands the intent of this revision, and does not believe that the  
11 Hearing Officers intended to exclude APS customers that receive electric service at transmission-  
12 level voltage, such as mines and other very large industrial customers. APS recommends revising  
13 the language in R14-2-1607(F) to provide that “A Competitive Transition Charge (CTC) may be  
14 assessed on all customers of an Affected Utility receiving any Noncompetitive Service, and shall  
15 be based on the total amount of generation purchased by such customer from any supplier.”  
16 Because customers receiving transmission-level voltage service will, at a minimum, receive some  
17 metering services (set forth in proposed rule R14-2-1613(K)) that are defined as Noncompetitive  
18 Services, these customers will not evade the CTC under APS’ proposed revision.  
19

### 20 **VIII. TREATMENT OF MARKET DETERMINED RATES**

21 Rule R14-2-1612(A) formerly provided that market determined rates were “deemed” just  
22 and reasonable. The revisions to this rule now provide that market determined rates are  
23 “presumed” just and reasonable. The word “presumed” appears to expose a market determined  
24 rate to attack for not meeting the “just and reasonable” requirement for the rates of public service  
25 corporations. If the intent of such a change was to “hedge” against the competitive market perhaps  
26 causing higher electric rates than current regulated rates, such manipulation of the market is

1 anathema to the “deregulation” process that has been underway for the past four years. Put simply,  
2 the maximum rates set forth in an ESP’s tariff should be the only “limits” on market determined  
3 rates.

4       Additionally, APS proposed adding a sentence at the end of Rule R14-2-1612 stating:  
5 “Such tariffs may combine one or more competitive services within the rate(s) for any other  
6 competitive service.” Such a provision incorporates Commission Staff’s position on combining  
7 services for tariff purposes that was proposed and adopted by the Commission in the PG&E  
8 Energy Services CC&N proceeding, Docket No. E-03595A-98-0389. Incorporating such a  
9 provision in the rules, rather than at each CC&N proceeding, adds clarity and consistency to the  
10 tariff requirements in Rule R14-2-1612.

#### 11 12                   **IX. FILING INFORMATION FOR THE CONSTRUCTION OF NEW 13                   GENERATION FACILITIES**

14       Although not raised in APS’ original comments filed pursuant to the Chief Hearing  
15 Officer’s Procedural Order of January 26, 1999, APS recommends that the Commission use this  
16 rulemaking opportunity to conform rule R14-2-202(B) to the amendments adopted last year in  
17 House Bill 2663. That law amended A.R.S. § 40-360.02 to delete the requirement that persons  
18 contemplating the construction of generating plants file plans with the Commission providing the  
19 information currently set forth in R14-2-202(B). A.R.S. § 40-360.02 now requires plans only for  
20 transmission facilities, which are not addressed in R14-2-202(B). To conform the rules to the  
21 amendments in HB 2663, APS thus recommends deleting R14-2-202(B) in its entirety.

#### 22                   **X. FERC JURISDICTIONAL AND TRANSMISSION ISSUES**

23       In R14-2-1606(F), the Commission identifies the “transmission, distribution and ancillary  
24 service” requirements for Affected Utilities and UDCs. Although the word “distribution” was  
25 added to the prefatory language in the rule, no distribution services are then identified in the rule.  
26

1 Rather, the rule continues to provide what and how transmission service, subject to exclusive  
2 FERC jurisdiction, is to be provided in Arizona. If the Commission, through its revisions, is  
3 merely attempting to “tread lightly” along jurisdictional boundaries, it has nonetheless invaded  
4 FERC’s exclusive territory. For example, the rule outlines certain obligations relating to  
5 transmission service with the caveat, “[u]nless otherwise required by federal regulation.” Because  
6 FERC has exclusive jurisdiction over transmission-related issues, the correct wording could only  
7 be “If provided by federal regulation....” Rather than risk intruding into FERC’s jurisdiction, APS  
8 continues to recommend that this paragraph be deleted.

9 Additionally, APS suggests several revisions to R14-2-1610 relating to the Arizona  
10 Independent Scheduling Administrator (“AISA”). First, APS believes that language should be  
11 revised in R14-2-1610(C)(1) to allow the AISA certain flexibility in connection with an OASIS  
12 system. The proposed rule requires the AISA to develop an “overarching” statewide OASIS  
13 program, which unnecessarily limits the AISA to this type of OASIS program. Also, APS believes  
14 that the AISA should have the flexibility to either operate the system itself or designate another  
15 entity to operate the system. Such an option is currently foreclosed by the proposed rules.

16 Also, R14-2-1610(C)(4) appears to require that all wholesale scheduling requests, in  
17 addition to retail and Standard Offer requests, be made through AISA. APS has a number of  
18 existing wholesale transmission contracts which are under FERC jurisdiction. The parties to these  
19 contracts are not affiliated with AISA, and could not be made subject to AISA protocols without  
20 FERC intervention. APS recommends deleting the word “wholesale” from R14-2-1610(C)(4).  
21 APS’ proposed revisions are set forth in Exhibit A.<sup>2</sup>  
22

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23  
24 <sup>2</sup> APS also has several concerns about language in R14-2-1610 regarding the recovery of the  
25 costs of establishing the AISA and the treatment of must-run generation at the federal level.  
26 Essentially, FERC has determined that costs associated with ISA formation and must-run  
generation are appropriately addressed at the distribution level. Although APS will reserve  
additional comment on these matters until the rulemaking proceeding, APS’ proposed revisions  
are indicated on Exhibit A.

**XI. MISCELLANEOUS**

1  
2 There are several additional comments to the Recommended Order and proposed revisions  
3 to the Rules that APS believes should be accepted:

4 1. The provision of "customer demand and energy data" to ESPs has been newly-classified  
5 as a "Noncompetitive Service." If this change is to prevent the "spin off" requirement in Section  
6 1616(A) from effectively prohibiting a UDC from providing such services, APS' proposed change  
7 to the definition of "Competitive Services" would eliminate that concern. Moreover, the provision  
8 of this customer data is only a "Noncompetitive Service" when the customer is a Standard Offer  
9 customer. Otherwise, a competitive MSP or MRSP is just as likely to have this data as the UDC.

10 2. Rule R14-2-1606(G)(4) provides that Load Serving Entities may charge a tariffed rate  
11 for customer demand and energy data only for the second customer request in a twelve month  
12 period. The cost of tracking and administering such a requirement, however, will likely exceed the  
13 cost of producing the data. Depending on the specific UDC, it may be more appropriate to apply a  
14 single nominal charge for all customer data requests. Accordingly, APS proposes deleting R14-2-  
15 1606(G) and addressing the issue in the appropriate tariff filings.

16 3. Proposed rule R14-2-1606(D) requires Affected Utilities to file stranded cost recovery  
17 mechanism proposals by March 19, 1999. However, providing a date certain for any filing should  
18 be done by issuing a procedural order, rather than imposing the date in a rulemaking proceeding.  
19 In this case, the March 19, 1999 date appearing in the proposed rule will be moot by the time the  
20 rule is final. This date also appears, and should be removed, in R14-2-1607.

21 4. In proposed rule R14-2-1618, the Hearing Officers adopted APS' suggestion that  
22 information disclosures be limited to residential customers. The residential customer limitation  
23 was inserted into Section 1618(A), but appears to have been inadvertently omitted from Section  
24 1618(E) and (F)(1). The specific locations of these omissions are identified on APS' Exhibit A  
25 hereto.

26 5. In R14-2-1615(A), the proposed rule deletes the requirement that the Commission

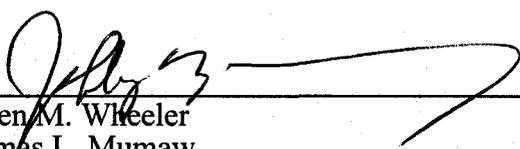
1 affirmatively approve an ESP's tariff prior to the ESP providing the service. The CES  
2 acknowledges that this proposal is reasonable. The same affirmative approval requirement,  
3 however, is still present in rule R14-2-1612(B).<sup>3</sup> To correct this contradiction, the Commission  
4 should delete everything after the comma in R14-2-1612(B).

5  
6 **CONCLUSION**

7 APS urges the Commission to take this opportunity, prior to the commencement of the  
8 formal rulemaking proceeding, to carefully consider the proposed changes and clarifications  
9 suggested by APS. The Company believes that these revisions are fair, practical and proportional,  
10 and will send a strong signal that the Commission intends to adopt effective rules to implement  
11 retail electric competition.

12 **RESPECTFULLY SUBMITTED** this 17<sup>th</sup> day of February, 1999.

13 **SNELL & WILMER L.L.P.**

14  
15   
16 \_\_\_\_\_  
17 Steven M. Wheeler  
18 Thomas L. Mumaw  
19 Jeffrey B. Guldner

20 Attorneys for Arizona Public Service Company

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26 <sup>3</sup> APS admits that its comments of January 29, 1999, also overlooked the fact that this "prior approval" requirement, which is more onerous than that presently in effect for Noncompetitive Services, appeared in two sections of the Rules.

Snell & Wilmer  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

## EXHIBIT A

### APS' SUGGESTED CHANGES TO PROPOSED ELECTRIC COMPETITION RULES

#### R14-2-1601

5. "Competitive Services" means the provision of retail electric Generation, Meter Service (other than those aspects of Meter Service described in R14-2-1613(K)), Meter Reading Service, or electric billing and collection services (other than joint or consolidated billing provided by an Affected Utility or Utility Distribution Company pursuant to a tariff). It does not include Standard Offer Service or any other electric service defined in this article as noncompetitive. ~~all aspects of retail electric service except those services specifically defined as "Noncompetitive Services" pursuant to R14-2-1601(27) or noncompetitive services as defined by the Federal Energy Regulatory Commission.~~
34. "Standard Offer Service" means Bundled Service offered by the Affected Utility or Utility Distribution Company to ~~all~~ consumers in the Affected Utility's or Utility Distribution Company's service territory ~~whose annual usage is 100,000 kWh or less~~ at regulated rates, including metering, meter reading, billing, collection services, demand side management services including but not limited to time-of-use, and consumer information services. All components of Standard Offer Service shall be deemed noncompetitive as long as those components are provided in a bundled transaction pursuant to R14-2-1606(A).

**R14-2-1606**

- A. On the date its service area is open to competition pursuant to R14-2-1602, each Affected Utility or Utility Distribution Company shall make available Standard Offer Service and Noncompetitive Services at regulated rates. After January 1, 2001, Standard Offer Service and Noncompetitive Services shall be provided by Utility Distribution Companies who shall also act as Providers of Last Resort for any customer whose annual usage is 100,000 kWh or less.
- B. After January 1, 2001, power purchased by a Utility Distribution Company to provide Standard Offer Service shall be acquired through the open market. All purchased power costs shall be recovered through a purchased power adjustment mechanism, which the Commission shall approve prior to January 1, 2001.
- C. Standard Offer Tariffs
1. By the date indicated in R14-2-1602, each Affected Utility shall file proposed tariffs to provide Standard Offer Service. Such rates shall not become effective until approved by the Commission. ~~Standard Offer tariffs shall include the billing cost elements required by R14-2-1613(O).~~
  2. Affected Utilities and Utility Distribution Companies may file proposed revisions to such rates. Any rate increase proposed by an Affected Utility or Utility Distribution Company for Standard Offer Service must be fully justified through a rate case proceeding, which may be expedited at the discretion of the Utilities Division Director.
  3. Such rates shall reflect the costs of providing the service.
  4. Consumers receiving Standard Offer service are eligible for potential future rate reductions as authorized by the Commission.
  5. ~~After January 1, 2001, tariffs for Standard Offer Service shall not include~~

~~any special discounts or contracts with term, or any tariff which prevents the customer from accessing a competitive option.~~

- D. ~~By March 19, 1999, e~~Each Affected Utility or Utility Distribution Company shall file ~~an~~ Unbundled Service tariffs to provide ~~which shall include a~~ Noncompetitive Services to all eligible purchasers on a nondiscriminatory basis. ~~tariff.~~

**R14-2-1607**

- F.** A Competitive Transition Charge (CTC) may be assessed on all customers of an Affected Utility receiving any Noncompetitive Service, and shall be ~~continuing to use the distribution system~~ based on the amount of generation purchased by such customer from any supplier. Any reduction in electricity purchases from an Affected Utility resulting from self-generation, demand side management, or other demand reduction attributable to any cause other than the retail access provisions of this Article shall not be used to calculate or recover any Stranded Cost from a consumer.

**R14-2-1610**

C. The Commission believes that an Independent Scheduling Administrator is necessary in order to provide non-discriminatory retail access and to facilitate a robust and efficient electricity market. Therefore, those Affected Utilities that own or operate Arizona transmission facilities shall form an Arizona Independent Scheduling Administrator which shall file with the Federal Energy Regulatory Commission within 60 days of this Commission's adoption of final rules herein, for approval of an Independent Scheduling Administrator having the following characteristics:

1. The Arizona Independent Scheduling Administrator shall calculate Available Transmission Capacity (ATC) for Arizona transmission facilities that belong to the Affected Utilities or other Arizona Independent Scheduling Administrator participants, and shall develop ~~and operate an overarching a~~ statewide OASIS.

...

4. All requests (~~wholesale, Standard Offer retail,~~ and competitive retail) for reservation and scheduling of the use of Arizona transmission facilities that belong to the Affected Utilities or other Arizona Independent Scheduling Administrator participants shall be made to, or through, the Arizona Independent Scheduling Administrator using a single, standardized procedure.

D. ~~The Affected Utilities that own or operate Arizona transmission facilities shall file a proposed Arizona Independent Scheduling Administrator~~ shall file an implementation plan with the Commission within thirty days of the Commission's adoption of final rules herein. The implementation plan shall address Arizona Independent Scheduling Administrator governance, incorporation, financing and staffing; the acquisition of physical facilities and staff by the Arizona Independent

Scheduling Administrator; the schedule for the phased development of Arizona Independent Scheduling Administrator functionality; contingency plans to ensure that critical functionality is in place no later than three months following adoption of final rules by the Commission; and any other significant issues related to the timely and successful implementation of the Arizona Independent Scheduling Administrator.

...

- F.** It is the intent of the Commission that prudently-incurred costs incurred by the Affected Utilities in the establishment and operation of the Arizona Independent Scheduling Administrator, and subsequently the Independent System Operator, should be recovered from customers using the ~~transmission-distribution~~ system, including the Affected Utilities' ~~wholesale customers~~, Standard Offer retail customers, and competitive retail customers on a non-discriminatory basis through ~~Federal Energy Regulatory Commission-regulated prices~~Commission-regulated distribution rates. ~~Proposed rates for the recovery of such costs shall be filed with the Federal Energy Regulatory Commission and this Commission. In the event that the Federal Energy Regulatory Commission does not permit recovery of prudently incurred Independent Scheduling Administrator costs within 90 days of the date of making an application with the Federal Energy Regulatory Commission, the Commission may authorize Affected Utilities to recover such costs through a distribution surcharge.~~

...

- I.** The Affected Utilities and Utility Distribution Companies shall provide services from the Must-Run Generating Units to Standard Offer retail customers and competitive retail customers on a comparable, non-discriminatory basis at regulated prices. The Affected Utilities shall specify the obligations of the Must-Run Generating Units in appropriate sales contracts prior to any divestiture.

Under auspices of the Arizona Independent Scheduling Coordinator, the Affected Utilities and other stakeholders shall develop statewide protocols for pricing and availability of services from Must-Run Generating Units with input from other stakeholders. These protocols shall be presented to the Commission for review ~~and filed with the Federal Energy Regulatory Commission in conjunction with the Arizona Independent Schedule Administrator tariff filing.~~

**R14-2-1612**

- A. Market determined rates for Competitive Services as defined in R14-2-1601(5) shall be ~~presumed~~ deemed to be just and reasonable.
- B. Each Electric Service Provider selling services under this Article shall have on file with the Commission tariffs describing such services and maximum rates for those services, ~~but the services may not be provided until the Commission has approved the tariffs.~~ Such tariffs may combine one or more Competitive Services within the rate(s) for any other Competitive Service.

**R14-2-1616**

A. All competitive generation assets ~~and competitive services~~ shall be separated from an Affected Utility prior to January 1, 2001. Such separation shall either be to an unaffiliated party or to a separate corporate affiliate or affiliates.

B. Affected Utilities or Utility Distribution Companies may provide other (non-generation Competitive Services through an affiliate, but are not required to do so. If an Affected Utility or Utility Distribution Company chooses not to provide non-generation Competitive Services through a separate affiliate, the Affected Utility or Utility Distribution Company shall separately account for such Competitive Services.

**BC.** After January 1, 2001, an Affected Utility or Utility Distribution Company shall not provide competitive retail Generation Competitive Services as defined in R14-2-1601(16), except as otherwise authorized by these rules or by the Commission.

**R14-2-1617**

**A. Separation**

An Affected Utility or Utility Distribution Company and its affiliates shall operate as separate corporate entities. For the purposes of this Rule, Utility Distribution Company also includes any affiliate of an electric Service Provider that would be deemed a Utility Distribution Company if operating in Arizona and subject to the Commission's jurisdiction. Books and records shall be kept separate, in accordance with applicable Uniform System of Accounts (USOA) and Generally Accepted Accounting Principles (GAAP). The books and records of any Electric Service Provider that is an affiliate of an Affected Utility or Utility Distribution Company shall be open for examination by the Commission and its staff consistent with the provisions set forth in R14-2-1614. All proprietary information shall remain confidential.

...

6. Except as provided in subsection A(2), an Utility Distribution Company and its competitive electric affiliate shall not jointly employ the same employees. This rule does not apply to Boards of Directors and corporate officers. ~~However, any board member or corporate officer of a holding company may also serve in the same capacity with the Affected Utility or Utility Distribution Company, or its competitive electric affiliates, but not both.~~ Where the Affected Utility is a multi-state utility, is not a member of a holding company structure, and assumes the corporate governance functions for its competitive electric affiliates, the prohibition outlined in this section shall only apply to competitive electric affiliates that operate within Arizona.
7. Transfer of Goods and Services: To the extent that these rules do not prohibit transfer of goods and services between an Utility Distribution

Company and its competitive electric affiliates, all such transfers shall be subject to the following price provisions:

- a. Goods and services provided by an Utility Distribution Company to a competitive electric affiliate shall be transferred at the price and under the terms and conditions specified in its tariff. If the goods or service to be transferred is a non-tariffed item and is regularly sold by the Utility Distribution Company to unaffiliated third parties, the transfer price shall be the ~~higher of fully allocated cost or the fair~~ market price. If market price cannot be easily determined by the Utility Distribution Company or if a good or service is not regularly offered to third parties (e.g., shared service), the transfer price should not be less than the fully allocated cost of the good or service.
- b. Goods and services produced, purchased or developed for sale on the open market by the Utility Distribution Company will be provided to its competitive electric affiliates and unaffiliated companies on a nondiscriminatory basis, except as otherwise permitted by these rules or applicable law.

**R14-2-1618**

**E.** Each Load-Serving Entity shall prepare a statement of its terms of service that sets forth the following information:

1. Actual pricing structure or rate design according to which the residential customer with a load of less than 1 MW will be billed, including an explanation of price variability and price level adjustments that may cause the price to vary;
2. Length and description of the applicable contract and provisions and conditions for early termination by either party;
3. Due date of bills and consequences of late payment;
4. Conditions under which a credit agency is contacted;
5. Deposit requirements and interest on deposits;
6. Limits on warranties and damages;
7. All charges, fees, and penalties;
8. Information on consumer rights pertaining to estimated bills, 3<sup>rd</sup> party billing, deferred payments, and recission of supplier switches within 3 days of receipt of confirmation;
9. A toll-free telephone number for service complaints;
10. Low income programs and low income rate eligibility;
11. Provisions for default service;
12. Applicable provisions of state utility laws; and
13. Method whereby customers will be notified of changes to the terms of service.

**F.** The consumer information label, the disclosure report, and the terms of service shall be distributed in accordance with the following requirements:

1. Prior to the initiation of service for any retail residential customer,

2. Prior to processing written authorization from a retail residential customer with a load of less than 1 MW to change Electric Service Providers,
3. To any person upon request,
4. Made a part of the annual report required to be filed with the Commission pursuant to law.
5. The information described in this subsection shall be posted on any electronic information medium of the Load-Serving Entities.

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**CERTIFICATE OF SERVICE**

The original and ten (10) copies of the foregoing document were filed with the Arizona Corporation Commission on this 17th day of February, 1999, and service was completed by mailing or hand-delivering a copy of the foregoing document this 17th day of February, 1999 to the accompanying service list.

  
\_\_\_\_\_  
Sharon Madden

**Snell & Wilmer**  
L.L.P.  
LAW OFFICES  
One Arizona Center  
Phoenix, AZ 85004-0001  
(602) 382-6000

Greg Patterson  
RUCO  
2828 North Central Avenue  
Suite 1200  
Phoenix, Arizona 85004

200 Stovall St., Rm. 10S12  
Alexandria, VA 22332-2300

Ajo Improvement Company  
P.O. Drawer 9  
Ajo, Arizona 85321

Michael A. Curtis  
Martinez & Curtis, P.C.  
2712 N. Seventh Street  
Phoenix, Arizona 85006

Mohave Electric Cooperative, Inc.  
P.O. Box 1045  
Bullhead City, Arizona 86430

Walter W. Meek, President  
Arizona Utility Investors Association  
2100 N. Central Avenue  
Suite 210  
Phoenix, Arizona 85004

Morenci Water & Electric Co.  
P.O. Box 68  
Morenci, Arizona 85540

Rick Gilliam  
Land & Water Fund of the Rockies  
2260 Baseline Road  
Suite 200  
Boulder, Colorado 80302

Betty Pruitt  
Arizona Community Action Assoc.  
2627 N. Third St., Ste. 2  
Phoenix, Arizona 85004

Terry Frothun, President  
Charles R. Huggins, Sec/Treasurer  
Arizona State AFL-CIO  
5818 N. 7<sup>th</sup> St., Ste. 200  
Phoenix, Arizona 85014-5811

Jay I. Moyes  
Meyer Hendricks Bivens & Moyes PA  
3003 N. Central Ave., Ste. 1200  
Phoenix, Arizona 85001-2199

Norman J. Furuta  
Department of the Navy  
900 Commodore Drive, Bldg. 107  
P.O. Box 272 (Attn. Code 90C)  
San Bruno, CA 94066-5006

Bradley Carroll  
Legal Dept.-DB203  
Tucson Electric Power Company  
P.O. Box 711  
Tucson, Arizona 85702

Sam Defraw (Attn. Code 16R)  
Rate Intervention Division  
Naval Facilities Engineering Command

Creden Huber  
Sulphur Springs Valley Electric  
Cooperative  
P.O. Box 820  
Willcox, Arizona 85644  
Mick McElrath  
Cyprus Climax Metals Company  
P.O. Box 22015  
Tempe, Arizona 85285-2015

Wayne Retzlaff  
Navopache Electric Co-Op, Inc.  
P.O. Box 308  
Lakeside, Arizona 85929

Craig Marks  
Citizens Utilities Company  
2901 N. Central Ave., Suite 1660  
Phoenix, Arizona 85012

Stephen L. Teicher  
Duane Morris & Heckscher LLP  
1667 K Street N.W., Ste. 700  
Washington, D.C. 20006

Steve Kean  
ENRON  
P.O. Box 1188  
Houston, TX 77251-1188

Jessica Youle  
PAB 300  
Salt River Project  
P.O. Box 52025  
Phoenix, Arizona 85072-2025

Jack Shilling  
Duncan Valley Electric Cooperatiave  
P.O. Box 440  
Duncan, Arizona 85534

Patricia Cooper  
AEP  
P.O. Box 670  
Benson, Arizona 85602-0670

Ken Saline  
K.R. Saline & Associates  
160 N. Pasadena, Ste. 101  
Mesa, Arizona 85021-6764

Clifford Cauthen  
Graham County Electric Co-Op  
P.O. Drawer B  
Pima, Arizona 85543

Phyllis Rowe  
Arizona Consumers Council  
6841 North 15<sup>th</sup> Place  
Phoenix, Arizona 85014

Marv Athey  
Trico Electric Cooperative  
P.O. Box 35970  
Tucson, Arizona 85740

C. Webb Crockett  
Fennemore Craig  
3003 N. Central Avenue  
Suite 2600

Phoenix, Arizona 85012-2813

6900 E. Camelback Rd. #800  
Scottsdale, Arizona 85251

Kathy T. Puckett  
Shell Oil Company  
200 N. Dairy Ashford  
Houston, Texas 77079

Michael Grant  
Gallagher & Kennedy  
2600 North Central Avenue  
Phoenix, Arizona 85004

Robert S. Lynch  
340 E. Palm Lane  
Suite 140  
Phoenix, Arizona 85004-4529

Albert Sterman  
Arizona Consumers Council  
2849 East 8<sup>th</sup> Street  
Tucson, Arizona 85716

Michael Block  
Goldwater Institute  
Bank One Center  
201 N. Central, Concourse Level  
Phoenix, Arizona 85004

Lex Smith  
Michael Patten  
Brown & Bain, P.C.  
2901 N. Central Avenue  
Phoenix, Arizona 85001-0400

John Branch  
City of Mesa Electric Utility  
P.O. Box 1466  
Mesa, Arizona 85211-1466

Vinnie Hunt  
Tucson Department Of Operations  
4004 South Park Avenue, Building 2  
Tucson, Arizona 85714

Douglas C. Nelson, P.C.  
7000 N. 16<sup>th</sup> Street  
Suite 120-307  
Phoenix, Arizona 85020-5547

William Sullivan  
Martinez & Curtis, P.C.  
2716 North Seventh Street  
Phoenix, Arizona 85006

Lawrence V. Robertson, Jr.  
Munger Chadwick, P.L.C.  
333 North Wilmot, Suite 300  
Tucson, Arizona 85711-2634

Elizabeth S. Firkins  
International Brotherhood of  
Electrical Workers L.U. #1116  
750 South Tucson Blvd.  
Tucson, Arizona 85716-5698

Charles Post  
PG&E Energy Services

Paul Bullis, Chief Counsel, Legal Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Peter Q. Nyce, Jr.  
Department of the Army  
JALIS-RS Suite 713  
901 N. Stuart Street  
Arlington, Virginia 22203-1837

Arizona Reporting Service, Inc.  
2627 North Third Street, Suite #3  
Phoenix, Arizona 85004-1104

Russell E. Jones  
O'Connor Cavanagh Molly Jones  
33 N. Stone Avenue, Suite 2100  
P.O. Box 2268  
Tucson, Arizona 85702  
Christopher Hitchcock  
Hitchcock Hicks & Conlogue  
P.O. Box 87  
Bisbee, Arizona 85603-0087

Jerry Rudibaugh  
Chief Hearing Officer  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Ray Williamson  
Acting Director, Utilities Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Suzanne M. Dallimore  
Antitrust Unit Chief  
Department of Law Building  
1275 West Washington Street  
Phoenix, Arizona 85007

Carl Dabelstein  
2211 E. Edna Avenue  
Phoenix, Arizona 85022

Andrew W. Bettwy  
Debra Jacobson  
Southwest Gas Corporation  
5241 Spring Mountain Road  
Las Vegas, Nevada 89102

Barabara S. Bush  
Coalition For Responsible  
Energy Education  
315 W. Rivera Drive  
Tempe, Arizona 85282

Andrew N. Chau  
Shell Energy Services Co. LLC  
1221 Lamar, Suite 1000  
Houston, Texas 77010

Myron Scott  
Arizonians for Better Environment  
1628 E. Southern No. 9-328

Roderick G. McDougall  
City Attorney  
200 West Washington St.  
Suite 1300  
Phoenix, Arizona 85003-1611

Tempe, Arizona 85282-2179

Barbara R. Goldberg  
Office of the City Attorney  
3939 Civic Center Blvd.  
Scottsdale, Arizona 85251

Phyllis Rowe  
Arizona Consumers Council  
P.O. Box 1288  
Phoenix, Arizona 85001

Donald R. Allen, Esq.  
John P. Coyle, Esq.  
Duncan & Allen  
1575 Eye St., NW, Ste. 300  
Washington, DC 20005

Porter Simon  
Steven C. Gross  
40200 Truckee, Airport Rd.  
Truckee, CA 96161

Timothy Hogan  
AZ Center for law in the Public Interest  
202 E. McDowell Rd., Ste. 153  
Phoenix, AZ 85004

Mick McElrath  
Cyprus Climax Metals Company  
P.O. Box 22015  
Tempe, Arizona 85285-2015

Patricia Cooper

AEPCO  
P.O. Box 670  
Benson, Arizona 85602-0670

Clifford Cauthen  
Graham County Electric Co-Op  
P.O. Drawer B  
Pima, Arizona 85543

Marv Athey  
Trico Electric Cooperative  
P.O. Box 35970  
Tucson, Arizona 85740

Wayne Retzlaff  
Navopache Electric Co-Op, Inc.  
P.O. Box 308  
Lakeside, Arizona 85929

Libby Brydolf  
California Energy Markets Newsletter  
2419 Bancroft Street  
San Diego, California 92104

Jack Shilling  
Duncan Valley Electric Cooperative  
P.O. Box 440  
Duncan, Arizona 85534

Ken Saline  
K.R. Saline & Associates  
160 N. Pasadena, Ste. 101  
Mesa, Arizona 85021-6764

John Branch  
City of Mesa Electric Utility  
P.O. Box 1466  
Mesa, Arizona 85211-1466

Continental Divide Electric Cooperative  
P.O. Box 1087  
Grants, New Mexico 87020

James P. Barlett  
5333 North 7<sup>th</sup> Street  
Buite B-215  
Phoenix, Arizona 85014

Dixie Escalante Rural  
Electric Association  
CR Box 95  
Beryl, Utah 84714

Paul W. Taylor  
R. W. Beck  
2201 E. Camelback Road  
Suite 115-B  
Phoenix, Arizona 85016-3433  
Rick Lavis  
Arizona Cotton Growers Association  
4139 E. Broadway Road  
Phoenix, Arizona 85040

Garkane Power Association, Inc.  
P.O. Box 790  
Richfield, Utah 84701

Arizona Department of Commerce  
Energy Office  
3800 N. Central Ave., 12<sup>th</sup> Floor  
Phoenix, Arizona 85012

Steve Brittle  
Don't Waste Arizona, Inc.  
6205 South 12<sup>th</sup> Street  
Phoenix, Arizona 85040

Betty Pruitt  
Arizona Community Action Assoc.  
2627 North 3<sup>rd</sup> Street, Ste. 2  
Phoenix, Arizona 85004

Karen Glennon  
19037 N. 44<sup>th</sup> Avenue  
Glendale, Arizona 85308

B. Baardson  
Nordic Power  
4281 north Summerset  
Tucson, Arizona 85715

Columbus Electric Cooperative, Inc.  
P.O. Box 631  
Deming, New Mexico 88031

Joe Eichelberger  
Magma Copper Company  
P.O. Box 37

Superior, Arizona 85273

USDA-RUS  
6266 Weeping Willow  
Rio Rancho, New Mexico 87124

Barry Huddleston  
Destec Energy  
P.O. Box 4411  
Houston, Texas 77210-4411

Jim Driscoll  
Arizona Citizen Action  
2430 S. Mill, Ste 237  
Tempe, Arizona 85282

Steve Montgomery  
Johnson Controls  
2032 West 4<sup>th</sup> Street  
Tempe, Arizona 85281

William Baker  
Electrical District No. 6  
P.O. Box 16450  
Phoenix, Arizona 85011

Terry Ross  
Center for Energy and  
Economic Development  
P.O. Box 288  
Franktown, Colorado 80116-0288  
Kimberly Knox  
Streich Lang  
Two North Central Avenue  
Phoenix, Arizona

John Jay List, General Counsel  
National Rural Utilities Cooperative  
Finance Corporation  
2201 Cooperative Way  
Herndon, Virginia 21071  
Wallace Tillman, Chief Counsel  
National Rural Electric Cooperative Assn.  
4301 Wilson Boulevard  
Arlington, Virginia 22203-1860

Clara Peterson  
AARP  
HC 31, Box 977  
Happy Jack, Arizona 86024

Robert Julian  
PPG  
1500 Merrell lane  
Belgrade, Montana 59714

Barbara Sherman  
Utility Watchdog Committee  
120 E. McKellips Road  
Tempe, Arizona 85281-1118

Stan Barnes  
Copper State Consulting Group  
100 W. Washington St., Ste. 1415  
Phoenix, Arizona 85003

Larry McGraw

Carl Robert Aron  
Executive Vice President and COO  
Itron, Inc.  
2818 N. Sullivan Road  
Spokane, Washington 99216

Stephanie A. Conaghan  
Duane, Morris & Heckscher LLP  
1667 K Street N.W., Ste. 700  
Washington, D.C. 20006-1608

Steve Wheeler  
Thomas M. Mumaw  
Snell & Wilmer  
400 E. Van Buren Street  
Phoenix, arizona 85004-0001

Raymond S. Heyman  
Darlene M. Wauro  
Roshka Heyman & Dewulf, PLC  
400 North 5<sup>th</sup> Street, Ste. 1000  
Phoenix, Arizona 85004

Peter Glaser  
Doherty Rumble & Butler PA  
1401 New york Ave., NW, Ste. 1100  
Washington, DC 20005

Billie Dean  
AVIDD  
P.O. Box 97  
Marana, Arizona 85652-0987

Bradford A. Borman  
PacifiCorp  
201 S. Main., Suite 2000  
Salt Lake City, Utah 84140

Chris King, Vice President  
CellNet Data Systems, Inc.  
12667 Alcosta Blvd., Ste. 350  
San Ramon, California 94583

Marcia Weeks  
18970 North 116<sup>th</sup> Lane  
Surprise, Arizona 85374

Raymond B. Wuslich  
Winston & Strawn  
1400 L Street, N.W.  
Washington, D. C. 20005

John T. Travers  
William H. Nau  
272 Market Square, Ste. 2724  
Lake Forest, Illinois 60045

Ward Camp  
Phaser Advance Metering Services  
Alvarado Square  
Mail Stop SIM  
Albuquerque, New Mexico 87158

Timothy Michael Toy  
Winthrop, Stimson, Putnam & Roberts  
One Battery Park Plaza  
New York, New York 10004-1490

Thane T. Twiggs  
Idaho Power Company

P.O. Box 70  
Boisse, Idaho 83707