

1 even smaller percentage of total stranded costs when the post-2004 years are factored into the
2 total.² APS is unaware of any regulatory agency or state legislature that has attempted to so
3 summarily confiscate such a large percentage of utility equity. Although APS does not oppose in
4 principle establishing reasonable pre-set goals for mitigation of stranded costs (in lieu of endless
5 quarreling over this or that specific mitigation measure), what is a “reasonable” target may well
6 vary from utility to utility, and therefore each Affected Utility should be allowed to make some
7 specific proposal in that regard as part of its stranded cost filing.³ The Company finds this a better
8 approach than using some arbitrary percentage of disallowance. Moreover, there is certainly no
9 evidence (and none is cited) that would support the apparent assumption that Affected Utilities
10 could mitigate (through customer growth or otherwise) almost 50% of their stranded costs during
11 the period 1999-2004 and 100% thereafter.⁴

12 The Recommended Order attempts to justify this disallowance as a mere “modification” of
13 the APS proposal to rectify a perceived “major flaw” in such proposal. The so called “major flaw”
14 is the lack of incentive for customers to switch to alternative suppliers unless they can “purchase
15 generation at below market price.” Recommended Order at 2. Yet if a customer can not, in fact,
16 purchase generation for a lower cost than APS can purchase or generate that same power, why
17 should such a customer expect or deserve “to reap any savings”? Far from being a “major flaw,”
18 the Company’s proposal both promotes and reflects principles of economic efficiency.

20 ² The Chief Hearing Officer’s original May 6, 1998, Recommended Opinion and Order proposed a less
21 draconian “reduction schedule” that would have provided greater stranded cost recovery. No explanation for this
22 change is offered.

23 ³ In fairness, it is perhaps such an individual utility filing that is contemplated under Option No. 5 of the
24 Recommended Order. If that is the case, some of the Company’s concerns have been addressed by this March 12th
25 amendment to the earlier recommendation of the Hearing Division.

26 ⁴ As was thoroughly demonstrated at the stranded cost hearing, it is not the disallowance of stranded cost
recovery that incentivizes mitigation but rather the establishment of a fixed mitigation standard. To that end, any
percentage less than 100% would likely be as effective as any other. *See* APS Reply Brief, Section I.C., The
“Incentive to Mitigate” Myth, at 13. However, selecting a goal that is all but unobtainable is simply punitive and may
actually prove counterproductive to mitigation efforts.

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II. THE CURE

To remedy the problems identified above, APS recommends that the Commission consider adopting the Recommended Order with several changes.

First, the Commission should add a finding of fact and conclusion of law, both of which would state that "Affected Utilities are entitled to a reasonable opportunity to fully recover their stranded costs." Such a finding would be fully consistent with the Electric Competition Rules.

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

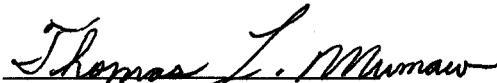
Accordingly, we shall modify Decision No. 61311 to allow each Affected Utility to file a stranded cost recovery plan of its choice that will allow it a reasonable opportunity to recover its stranded costs. Among the options available to each Affected Utility are the following:

This language will make it clear that Affected Utilities are not unreasonably restricted to a specific method of stranded cost recovery, but rather retain the flexibility to propose a plan for Commission consideration, and intervenor review, under Option No. 5, that is tailored to the conditions on their systems and their particular operational and financial circumstances.

Third, the description of Option No. 1 (Net Revenues Loss Methodology) should be modified to eliminate arbitrary stranded cost disallowance percentages and instead encourage a filing Affected Utility to propose its own mitigation plan. Proposed language amending Option 1 is attached hereto as Exhibit A.

RESPECTFULLY SUBMITTED this 7th day of April, 1999.

SNELL & WILMER L.L.P.

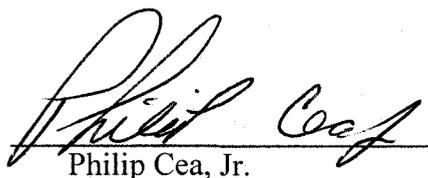


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CERTIFICATE OF SERVICE

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2 The original and ten (10) copies of the foregoing document were filed with
3 the Arizona Corporation Commission on this 7th day of April, 1999, and service was completed
4 by mailing or hand-delivering a copy of the foregoing document this 7th day of April, 1999 to all
5 parties of record herein.
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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.~~