

# EXCEPTION



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BEFORE THE ARIZONA CORPORATION COMMISSION

AZ CORP COMMISSION  
DOCKETED

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JIM IRVIN  
Commissioner - Chairman  
RENZ D. JENNINGS  
Commissioner  
CARL J. KUNASEK  
Commissioner

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IN THE MATTER OF THE COMPETITION IN ) DOCKET NO. RE-00000C-94-0165  
THE PROVISION OF ELECTRIC SERVICES )  
THROUGHOUT THE STATE OF ARIZONA. ) TEP'S REQUEST FOR A STAY AND  
) ITS EXCEPTIONS TO THE  
) PROPOSED ORDER ADOPTING  
) RULE AMENDMENTS

On December 4, 1998, the Arizona Corporation Commission ("Commission") issued a Proposed Opinion and Order ("Proposed Order") on Proposed Amendments to the Retail Electric Competition Rules, R14-2-1601, *et seq.* ("Proposed Rules"). Tucson Electric Power Company ("TEP" or "Company") hereby submits a Request for a Stay and its Exceptions to the Proposed Order Adopting Rule Amendments.

**A. The Commission Should Stay all Compliance and Implementation Dates.**

The Proposed Rules contain significant unresolved operational and implementation issues. Consequently, TEP believes that if the Proposed Rules are to be adopted at this time, the Commission should stay all compliance and implementation dates until such time as these issues are resolved. Upon resolution of these issues and after a reasonable notice period, the Commission could lift the stay and retail competition would go into effect in Arizona.

The Proposed Rules require the implementation of retail access on January 1, 1999 for certain customers. They also require the implementation of a residential phase-in program and other compliance obligations by certain dates. If adopted, the Proposed Rules should be stayed because the Commission has not resolved significant issues that are a legal and operational prerequisite for competition to commence.

First and foremost, the Commission has not resolved the issue of stranded costs for the Affected Utilities. TEP did file its Plan for Stranded Cost Recovery pursuant to Commission

1 Decision No. 60977 on August 21, 1998. TEP believes that without a final stranded cost  
2 determination and order, the Commission may not introduce retail competition into TEP's exclusive  
3 service territory. Nor has TEP been afforded its complete Section 40-252 hearing which is required  
4 by law and which is a prerequisite to the issuance of a competitive Certificate of Convenience and  
5 Necessity ("CC&N") to an Energy Service Provider ("ESP"). To do otherwise, would be an  
6 unconstitutional taking of TEP's property without due process and without just compensation.

7 TEP has not taken the position that the Commission does not have the authority to amend its  
8 CC&N. TEP believes that the Commission may do so if it either complies with the standard set  
9 forth in *James P. Paul Water Company v. Arizona Corporation Commission*, 137 Ariz. 426, 671  
10 P.2d 404 (1983), or provides just compensation for the taking of its property. While some of the  
11 parties have argued that the *regulated monopoly* is not a vested property right, the Arizona Supreme  
12 Court has held that the *CC&N* is a constitutionally protected vested property right, the taking of  
13 which requires compensation. In Judge Campbell's November 19, 1997 Minute Entry, he stated the  
14 following:

15 The brief filed by the Mining and Affected Utility Intervenors' (July 25,  
16 1997 at pp. 9 *et. seq.*), addresses whether the change in regulation, even if  
17 it impacts a corporation's value, is a "taking" in the constitutional sense.  
18 The Court need not reach this issue, however, because the Corporation  
19 Commission rules do allow for recovery of stranded costs. Whether a  
20 constitutional challenge can be made is premature and not ripe for decision  
21 until the Commission acts upon TEP's claim for stranded costs under its  
rules, which are not completed. On this record, it is not certain whether  
22 TEP will have any claimed "taking" at all (emphasis added).

23 This passage, along with Judge Campbell's January 13, 1998 Minute Entry which required a  
24 "fair" Section 40-252 hearing *before* a competitive CC&N could be granted, recognizes that the  
25 Commission must act on TEP's stranded cost claim *before* a determination could be made on the  
26 "takings" issue. Although not ripe in November 1997, should the Commission grant a competitive  
27 CC&N and require the Company to open its service territory in January 1, 1999 prior to issuing a  
28 final order with respect to TEP's stranded cost filing, the "takings" issue would certainly be ripe.  
29 This is why TEP's Section 40-252 hearing must be considered in the context of a final stranded cost  
30 proceeding. For the foregoing reasons, TEP believes that the Commission should stay the

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1 compliance and implementation sections of the Proposed Rules until such time as a final stranded  
2 cost order has been issued.

3         Second, the Commission must approve TEP's unbundled distribution tariff. Without final  
4 approval of this tariff, ESP's will be unable to contract with customers for services. Third, the  
5 Commission working groups have not completed their work on operational protocols, which are  
6 essential to the operational implementation of competition. There are also functional separation and  
7 other requirements set forth in the Affiliate Transaction Rules which should not be required until  
8 such time competition is in effect. Fourth, the Arizona Independent Scheduling Administrator is not  
9 yet operational. This is necessary to ensure non-discriminatory transmission access to the Affected  
10 Utilities retail distribution system and to provide scheduling into the various control areas in the  
11 state.

12         Based upon the foregoing, TEP believes that even if the Commission adopts the Proposed  
13 Rules, the order adopting the Proposed Rules should set forth a stay so that the above issues may be  
14 resolved.

15 **B. TEP's Exceptions Specific Exceptions to the Proposed Rules.**

16         1. **R14-2-1603. Certificates of Convenience and Necessity.**

17         TEP is concerned that the Proposed Rule does not address the settlement process  
18 between ESPs and UDCs. The primary settlement issues that we are concerned with involve the  
19 process by which the UDC determines whether the actual power used by the ESPs' customers is  
20 greater than, equal to or less than the power scheduled and delivered by the ESP and the  
21 reconciliation of resulting differences. This includes issues relating to pricing of energy imbalances.  
22 Further, there is no provision requiring contracts between the Scheduling Coordinators and the  
23 control areas.<sup>1</sup>

24         2. **R14-2-1604. Competitive Phases.**

25         A.1. TEP believes that utilizing a single "non-coincident" peak has unintended  
26 consequences. Only customers with 1 MW minimum demand should be eligible for direct access.  
27 Given TEP's customer base, the non-coincident peak criterion could expand the direct access  
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29 <sup>1</sup>TEP is also concerned that it may make more sense to bill the Scheduling Coordinator rather than the ESPs since the  
30 Scheduling Coordinator is the entity with whom the transactions are scheduled.

1 eligibility from the 1 MW customer base to well beyond the 20 percent of TEP's 1995 system retail  
2 peak demand. It would also have the affect of making the 40 kW aggregation meaningless, as well  
3 as impose additional burdens to administer. As the 20 percent cap could be easily reached, there will  
4 be customers that have loads in excess of 1 MW that will not be able to access the competitive  
5 market during the transition period.

6           A.2. In the third sentence, TEP suggests replacing "month" with "six months."  
7 Doing so will better characterize a customer whose load or usage is more consistently at least 40 kW  
8 or 16,500 kWh.

9           3.     R14-2-1606. Services Required to be Made Available.

10           B.     The sentence "Any resulting contract in excess of 12 months shall contain  
11 provisions allowing the Utility Distribution Company to ratchet down its power purchases" should  
12 be eliminated. TEP understands the Commission's intent with respect to this provision; however,  
13 ratchet mechanisms are not typically available in the marketplace and are, therefore, likely to be  
14 expensive. The Commission will oversee the signing of any long-term power purchases by the UDC  
15 and will have significant oversight over such transactions. The provision should also include a  
16 statement that all purchase power costs shall be recovered through a purchased power adjustment  
17 mechanism approved by the Commission.

18           G.1. A sentence should be added to the end that states "Customers who request  
19 such data from a Load-Serving Entity may be charged a reasonable fee for such information."

20           4.     R14-2-1607. Recovery of Stranded Cost of Affected Utilities.

21           A.     Delete "by means such as expanding wholesale or retail markets, or offering a  
22 wider scope of services for profit, among others." As is, this sentence suggests that the Affected  
23 Utility use profits from "expanding [its] wholesale or retail markets" or a "wider scope of services"  
24 to mitigate stranded costs. It is unclear whether the markets and services mentioned are regulated or  
25 unregulated (*i.e.*, competitive). TEP anticipates that most, if not all, new products and services in the  
26 electric industry will develop in the unregulated, competitive marketplace. The very nature of  
27 "unregulated" means that the Commission will not require that profits from such activities be used to  
28 offset costs in the regulated arena. Further, as TEP has proposed to divest itself of generation, the  
29 potential of expanding market opportunities becomes significantly limited.

30     ....

1 F. TEP disagrees with the self-generation exclusion set forth in Paragraph F. If the  
2 Proposed Rule is not modified to ensure that customers who choose to self-generate are responsible  
3 for stranded costs just as any other existing customer, a potentially large and improper economic  
4 incentive for self-generation will be created. This is due to the ability of such customers to avoid  
5 stranded cost charges. The result of the Proposed Rule as written will be to significantly increase  
6 uneconomic self-generation while increasing stranded cost burdens on customers who purchase their  
7 power in the competitive marketplace.

8 5. R14-2-1608. System Benefits Charge.

9 TEP believes that either this section, or the definition of System Benefits Charge,  
10 should incorporate competitive access implementation and evaluation program costs in the System  
11 Benefits Charge. The Proposed Rules do not mention who will be responsible for paying for  
12 competitive access implementation costs. TEP believes that all Affected Utility customers should  
13 pay for the costs of implementing and evaluating the new marketplace, because (a) restructuring was  
14 ordered by the Commission, and (b) all customers and "market-players" potentially stand to benefit  
15 from it.

16 6. R14-2-1609. Solar Portfolio Standard.

17 TEP requests that for purposes of this Proposed Rule, it should be made clear that an  
18 ESP may take credit and be in compliance with this standard if it utilizes the product of an affiliate  
19 that is engaged in the solar industry. For example, Staff specifically recognized this relationship in  
20 subsection K by inserting "affiliate" with respect to the manufacturing credit. It should also be  
21 applicable to other sections of the Proposed Rule where a credit may be taken such as the Early  
22 Installation Credit in subsection D or the renewable goal in subsection H.

23 A. and B. TEP believes that in order to allow for proper advances in technology  
24 and to ensure that money is invested in proven technologies, the percentage should be decreased  
25 from 2/10ths of one percent in 1999 to 1/10th of 1 percent and then increase this percentage by  
26 1/10th of one percent each year until the one percent level is achieved.

27 C. This provision should only apply to competitive retail sales after January 1,  
28 2001. It should not apply to standard offer retail electricity because the UDC is merely procuring  
29 generation through a competitive bid process as required by the Proposed Rules and passing costs  
30 through to standard offer customers. Requiring UDCs to comply with this provision creates a

1 significant cost burden. TEP's estimated cost in 2001, for example, would be approximately \$6.75  
2 million if one half of TEP's current customers choose direct access, and as much as \$13.5 million if  
3 a more significant number of customers choose direct access. This approximates to more than two  
4 times TEP's current expenditures for both DSM and renewables. Further, the cost would increase  
5 thereafter pursuant to the Proposed Rule unless the cost of solar resources is significantly reduced.

6 H. This provision references the Commission's Integrated Resource Planning  
7 ("IRP") Rules, which apply to only four of the Affected Utilities. TEP believes that the IRP  
8 requirements should be repealed or revised given the requirement of the Proposed Rules for an  
9 Affected Utility to divest itself of generation to an affiliate or a non-affiliate. Renewables, for  
10 example, should be the responsibility of the ESPs and not the UDCs who are no longer in the  
11 generation business. To the extent the UDC provides standard offer generation, it will be obtained  
12 through competitive bid from other suppliers.

13 7. R14-2-1610. Transmission and Distribution Access.

14 A. Add at the end of the paragraph "in accordance with FERC Orders 888  
15 and 889."

16 G. TEP believes that the use of Scheduling Coordinators must be a mandatory  
17 requirement for all ESPs (including Aggregators and Self-Aggregators who are not required to use  
18 an ESP) under this Proposed Rule. In order for open access to occur, there needs to be a Scheduling  
19 Coordinator to fill the role as an intermediary between the competitive market and the system control  
20 areas. Without the Scheduling Coordinator, the control areas will be unable to properly schedule  
21 power, which could jeopardize system reliability. TEP also believes that the Rules should specify  
22 minimum requirements for the Scheduling Coordinators such as a 24 hour a day, seven day a week  
23 operation and a license. The Commission working group studying this issue has supported this  
24 concept.

25 H. This section should be modified to allow the Affected Utility to determine the  
26 units which are must-run with consideration of the efforts of the Electric System Reliability and  
27 Safety Working Group findings as the Working Group may not complete all efforts in time for the  
28 competition start date. Further, this section should clearly state that all distribution customers as a  
29 mandatory ancillary service will pay the charges for must-run generation. We believe that this is the  
30 most effective way to ensure that these services are available at reasonable prices.

1           8.     R14-2-1616. Separation of Monopoly and Competitive Services.

2           C.     The following should be added at the end of the paragraph: "Generation  
3 Cooperatives will be subject to the same limitations that its member Distribution Cooperatives are  
4 subject to." This is necessary to prevent AEPCO (or its affiliate) and other generation cooperatives  
5 from competing in the retail electric market while utilizing the services of its Distribution  
6 Cooperatives.

7           9.     R14-2-1617. Electric Affiliate Transaction Rules.

8           TEP believes that this section should not be adopted at this time. There needs to be further  
9 input by the Affected Utilities with respect to the implications of these Proposed Rules from both a  
10 financial and operational perspective, as well as an assessment as to whether the Proposed Rules give  
11 a competitive advantage to non-Affected Utilities. Notwithstanding TEP's position and without  
12 waiver thereof, TEP has the following comments:

13           A and B.     TEP strongly requests that a provision be added that requires the  
14 Affected Utilities' generation affiliates to offer power to all parties on the same terms such output is  
15 offered to its affiliate UDC pursuant to a bulletin board requirement similar to that required by the  
16 FERC for affiliated marketers. The Company believes that this requirement is necessary to ensure  
17 that utilities that transfer generation to an affiliate do not utilize their generation subsidiaries to  
18 obtain advantages for their competitive retail efforts.

19           A.1.     TEP believes that this section can be eliminated because the provisions of A.2  
20 contain all of the necessary safeguards. It is also unclear as to its purpose in light of A.2.

21           A.6.     TEP believes that there is no purpose to be served by this provision except to  
22 disadvantage smaller corporate entities such as TEP. It makes a presumption that separation is  
23 appropriate in all instances when the Commission has always had the ability to review affiliate  
24 relationships under the Affiliate Rules. What this does is to deny day-to-day expertise necessary to  
25 efficiently carry out responsibilities to different entities. So long as proper allocation and conflict  
26 policies are in effect, this provision is unnecessary. At the very least, the Proposed Rule should  
27 provide for a waiver by the Commission upon a demonstration by the Affected Utility that  
28 appropriate procedures have been implemented that ensure that the utilization of common board  
29 members and corporate officers does not allow for the sharing of confidential information with  
30 affiliates or otherwise circumvent the purpose of this Proposed Rule.



1 Original and ten copies of the foregoing  
2 filed this 9th day of December, 1998, with:

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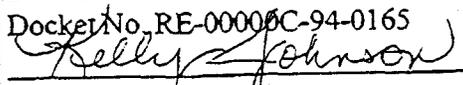
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