

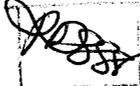
ORIGINAL  
OPEN MEETING



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MEMORANDUM

RECEIVED

Arizona Corporation Commission  
DOCKETED  
2012 MAR 12 P 2:44  
AZ CORP COMMISSION  
DOCKET CONTROL  
MAR 12 2012  
DOCKETED BY 

TO: THE COMMISSION

FROM: Utilities Division

DATE: March 12, 2012

RE: ARIZONA PUBLIC SERVICE COMPANY – APPLICATION FOR A DECLARATORY ORDER THAT A.A.C. R14-2-804 DOES NOT APPLY TO THE TRANSACTION DESCRIBED HEREIN, OR ALTERNATIVELY A WAIVER OF SUCH REGULATION OR APPROVAL THEREUNDER. (DOCKET NO. E-01345A-11-0467)

On December 23, 2011, Arizona Public Service Company (“APS” or the “Company”) filed an application with the Arizona Corporation Commission (“Commission”) seeking a declaratory order that Arizona Administrative Code (“A.A.C.”) R14-2-804 does not apply to the proposed transaction, or alternatively a waiver of such regulation or approval thereunder. APS proposes a transaction by which APS would become part of a strategic alliance between the owners and operators of seven commercial nuclear power plants. Verification of the application was filed with the application.

**Background**

APS is requesting that the Commission confirm that Title 14, Chapter 2, Article 8 of the A.A.C., *Public Utility Holding Companies and Affiliated Interests* (“Affiliated Interest Rules”)<sup>1</sup>, does not apply to APS’s plans to become a member of the STARS Alliance, LLC (“STARS”). STARS is a proposed strategic alliance between the owners and operators of seven commercial nuclear power plants (“Participants”).<sup>2</sup> The Participants propose to form STARS as a Delaware limited liability company.

The Participants all operate between one and three commercial nuclear power generating units at a single site. Additionally, all of the power plants are large (in excess of 1,000 megawatts), pressurized water nuclear reactors that have similar nuclear steam supply systems, and were designed by the same original equipment manufacturer. All of the nuclear sites are located in Nuclear Regulatory Commission (“NRC”) Region IV, spread across the western half of the United States.

<sup>1</sup> A.A.C. R14-2-801, *et seq.*

<sup>2</sup> The following seven entities propose to form and be participants of STARS: Union Electric Company, a Missouri corporation doing business as Ameren Missouri (“Ameren”); Luminant Generation Company LLC, a Texas limited liability company (“Luminant”); Pacific Gas and Electric Company, a California corporation (“PG&E”); Arizona Public Service Company, an Arizona corporation (“APS”); Southern California Edison Company, a California company (“SCE”); STP Nuclear Operating Company, a Texas corporation (“STPNOC”); and Wolf Creek Nuclear Operating Corporation, a Delaware corporation (“WCNOC”).

Through the creation of STARS, the STARS participants seek to form a joint purchasing entity, a resource sharing organization and to have a position in the market for the procurement of goods and services that is comparable to other large fleet operators.<sup>3</sup> The proposed coordinated activities of STARS will assist each Participant in reducing or avoiding operating costs and will not involve the purchase or sale of electricity. STARS is not intended to make any profits and any savings realized through the joint procurement of goods and services will be passed on to the Participants. It is important to note that participation in joint activities of STARS is completely voluntary. APS can elect to participate in only those activities that are beneficial to it and its customers.

### **Affiliated Interest Rules**

One function of the Affiliated Interest Rules is to maintain Commission awareness of the organizational structure and business transactions of regulated public utilities and those utilities' affiliates. The Affiliated Interest Rules require public utilities or affiliates intending to organize a public holding company or to reorganize an existing holding company to notify the Commission of such intent and to provide certain information prescribed in the rules. Additionally, public utilities and their affiliates must agree to make their books and records available to the Commission; get Commission approval prior to certain transactions; and file annual descriptions of diversification plans with the Commission.

An "affiliate" is defined as "any other entity directly or indirectly controlling or controlled by, or under direct or indirect common control with, the public utility." The term "control" means "the power to direct the management policies of such entity, whether through ownership of voting securities, or by contract, or otherwise."

As discussed below, Staff believes that STARS does not meet the definition of an "affiliate" of APS and, as such, the Affiliated Interest Rules are not applicable to STARS.

### **APS's Participation in STARS**

While Staff does not believe Commission review of the transaction is necessary because STARS is not an affiliate of APS, the Commission normally reviews affiliate transactions "to determine if the transactions would impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service." A.C.C. R14-2-804(C).

Staff does not believe that APS's participation in STARS would affect the financial status of the Company or the ability of the Company to provide safe, reasonable, and adequate service.

APS expects that the goods and services APS is likely to acquire through STARS – those which the Company would likely acquire irrespective of the STARS transaction – may be

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<sup>3</sup> Over the past 15 years, there has been considerable consolidation in the ownership of nuclear reactors and operation of nuclear reactors by large nuclear "fleet" operators. The largest operators are Exelon Corporation (17 units), Entergy Corporation (12 units), NextEra Energy Resources, formerly known as Florida Power & Light (8 units), Dominion Resources, Inc. (7 units), Duke Energy (7 units), Southern Company (6 units), Tennessee Valley Authority (6 units), Constellation Energy (5 units), and Progress Energy (5 units). In comparison, the STARS Participants collectively operate 13 units.

acquired for less than they would otherwise by virtue of participation in STARS. Thus, STARS is not anticipated to create any substantial new additional costs for APS which would impair the financial status of the Company. Additionally, the sharing of existing resources and best practices among STARS members will provide opportunities for improved operational efficiency and safety that may improve APS's ability to provide safe, reasonable and reliable services.

### **STARS Structure and Governance**

Given the structure and governance of STARS, Staff does not believe that STARS could assert control over APS, nor does it seem that APS could assert control over STARS. The 20 percent equity interest and the 14 percent voting power that APS would have in STARS is not enough to assert any control over the management decisions of STARS. The role of STARS is similarly limited as far as asserting control over APS. The voluntary nature of APS's participation in contractual relationships eliminates the ability of STARS or other Participants to direct the management policies of APS.

#### *Equity interest*

While STARS will have seven total participants, APS and four other Participants will be equity members of the proposed LLC, each providing \$1,000 as a capital contribution. Two Participants, STP Nuclear Operating Company and Wolf Creek Nuclear Operating Corporation, will be non-equity members of STARS to assure compliance with state law requirements unique to their organizations. As such, APS will have a 20 percent equity interest in STARS.<sup>4</sup>

#### *Series A Board*

STARS will be governed by a board of directors called the Series A Board. The Series A Board will be comprised of one representative from each of the seven Participants. Only the Series A Board will have the authority to make decisions for STARS. No individual Participant will have the ability to make decisions on behalf of STARS.

Each representative on the Series A Board will be entitled to one vote, irrespective of Participant status as an equity or non-equity member and the number of nuclear generating units owned.

Decisions regarding management policy and other significant Series A Board decisions, such as, but not limited to, approving budgets, admitting new Participants, and expanding business activities, will require a unanimous vote of the Series A Board. Other significant

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<sup>4</sup> STP Nuclear Operating Company is owned and operated in part by the City of Austin Texas and the City of San Antonio. Subject to certain exceptions not relevant here, the Texas Constitution prohibits cities from becoming stockholders or subscribers in private companies or from lending their credit or public money to a private company. See Tex. Const. Art. II, §§ 3 and 52. The Wolf Creek Nuclear Operating Corporation was formed by a collaborative of Kansas utility companies, including Kansas Gas and Electric Company, Kansas Power & Light Company and Kansas Electric Power Cooperative. At the time of formation, various representations were made to the respective public utility commissions of Kansas and Missouri that Wolf Creek Nuclear Operating Corporation would not own any property. As such, Wolf Creek Nuclear Operating Corporation believes that, consistent with its representations, it may not own equity in a private entity.

actions, such as incurring expenses exceeding \$25,000 that had not been previously budgeted, will require a super majority vote, defined as a two-thirds vote of the Series A Board.

The STARS LLC Agreement provides that additional series of membership may be created to govern Participants' involvement in specific joint projects that involve less than all seven of the Series A Participants. Each additional Series would be limited to a specific activity that a subset of STARS Participants elects to pursue.

*Costs*

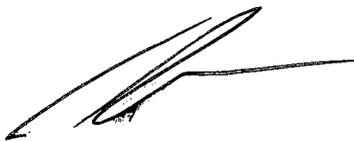
STARS is intended to operate as a not-for-profit entity with STARS activities anticipated to assist each Participant in reducing or avoiding operating costs. STARS will be set-up so that each Participant is obligated only to pay its proportionate share for STARS activities it elects to participate in and, in exchange, it will receive a proportionate share of the economic benefits relating to those activities.

The costs associated with APS's proposed participation in STARS are anticipated to be approximately \$100,000 per year to support the operation of STARS. Costs will vary slightly from year to year, depending on the activities that are undertaken by STARS on behalf of the participants. If the STARS participants undertake new activities, a cost-benefit analysis will be performed so that only new activities with measureable benefits are added.

All Participants, including APS, will pay their fair proportionate share of allocable costs for goods and services that they elect to purchase. To the extent that STARS enters into contractual relationships with third-party suppliers on behalf of the Participants, neither STARS nor any Participant can compel APS to purchase goods and/or services.

**Recommendations**

Given the structure of the Series A Board and the voluntary nature of participation in joint decisions, Staff does not believe that STARS can be characterized as an affiliate of APS. For that reason, Staff recommends that Commission confirm that the Affiliated Interest Rules do not apply to APS's plans to become a member of STARS.



Steven M. Olea  
Director  
Utilities Division

SMO:LAF:sms\MAS

ORIGINATOR: Laura A. Furrey

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

- GARY PIERCE  
Chairman
- BOB STUMP  
Commissioner
- SANDRA D. KENNEDY  
Commissioner
- PAUL NEWMAN  
Commissioner
- BRENDA BURNS  
Commissioner

IN THE MATTER OF ARIZONA PUBLIC SERVICE COMPANY FOR A DECLARATORY ORDER THAT A.A.C. R14-2-804 DOES NOT APPLY TO THE TRANSACTION DESCRIBED HEREIN, OR ALTERNATIVELY A WAIVER OF SUCH REGULATION OR APPROVAL THEREUNDER.

DOCKET NO. E-01345A-11-0467  
 DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
 March 27 and 28, 2012  
 Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Arizona Public Service Company ("APS" or the "Company") is certificated to provide electric service as a public service corporation in the State of Arizona.
2. On December 23, 2011, APS filed an application with the Arizona Corporation Commission ("Commission") seeking a declaratory order that Arizona Administrative Code ("A.A.C.") R14-2-804 does not apply to the proposed transaction, or alternatively a waiver of such regulation or approval thereunder. APS proposes a transaction by which APS would become part of a strategic alliance between the owners and operators of seven commercial nuclear power plants. Verification of the application was filed with the application.

Background

3. APS is requesting that the Commission confirm that Title 14, Chapter 2, Article 8 of the A.A.C., Public Utility Holding Companies and Affiliated Interests ("Affiliated Interest

1 Rules”<sup>1</sup>, does not apply to APS’s plans to become a member of the STARS Alliance, LLC  
2 (“STARS”). STARS is a proposed strategic alliance between the owners and operators of seven  
3 commercial nuclear power plants (“Participants”).<sup>2</sup> The Participants propose to form STARS as a  
4 Delaware limited liability company.

5 4. The Participants all operate between one and three commercial nuclear power  
6 generating units at a single site. Additionally, all of the power plants are large (in excess of 1,000  
7 megawatts), pressurized water nuclear reactors that have similar nuclear steam supply systems, and  
8 were designed by the same original equipment manufacturer. All of the nuclear sites are located in  
9 Nuclear Regulatory Commission (“NRC”) Region IV, spread across the western half of the United  
10 States.

11 5. Through the creation of STARS, the STARS participants seek to form a joint  
12 purchasing entity, a resource sharing organization and to have a position in the market for the  
13 procurement of goods and services that is comparable to other large fleet operators.<sup>3</sup> The proposed  
14 coordinated activities of STARS will assist each Participant in reducing or avoiding operating  
15 costs and will not involve the purchase or sale of electricity. STARS is not intended to make any  
16 profits and any savings realized through the joint procurement of goods and services will be passed  
17 on to the Participants. It is important to note that participation in joint activities of STARS is  
18 completely voluntary. APS can elect to participate in only those activities that are beneficial to it  
19 and its customers.

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23 <sup>1</sup> A.A.C. R14-2-801, *et seq.*

24 <sup>2</sup> The following seven entities propose to form and be participants of STARS: Union Electric Company, a Missouri  
25 corporation doing business as Ameren Missouri (“Ameren”); Luminant Generation Company LLC, a Texas limited  
26 liability company (“Luminant”); Pacific Gas and Electric Company, a California corporation (“PG&E”); Arizona  
Public Service Company, an Arizona corporation (“APS”); Southern California Edison Company, a California  
company (“SCE”); STP Nuclear Operating Company, a Texas corporation (“STPNOC”); and Wolf Creek Nuclear  
Operating Corporation, a Delaware corporation (“WCNOC”).

27 <sup>3</sup> Over the past 15 years, there has been considerable consolidation in the ownership of nuclear reactors and operation  
28 of nuclear reactors by large nuclear “fleet” operators. The largest operators are Exelon Corporation (17 units), Entergy  
Corporation (12 units), NextEra Energy Resources, formerly known as Florida Power & Light (8 units), Dominion  
Resources, Inc. (7 units), Duke Energy (7 units), Southern Company (6 units), Tennessee Valley Authority (6 units),  
Constellation Energy (5 units), and Progress Energy (5 units). In comparison, the STARS Participants collectively  
operate 13 units.

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2 **Affiliated Interest Rules**

3 6. One function of the Affiliated Interest Rules is to maintain Commission awareness  
4 of the organizational structure and business transactions of regulated public utilities and those  
5 utilities' affiliates. The Affiliated Interest Rules require public utilities or affiliates intending to  
6 organize a public holding company or to reorganize an existing holding company to notify the  
7 Commission of such intent and to provide certain information prescribed in the rules. Additionally,  
8 public utilities and their affiliates must agree to make their books and records available to the  
9 Commission; get Commission approval prior to certain transactions; and file annual descriptions of  
10 diversification plans with the Commission.

11 7. An "affiliate" is defined as "any other entity directly or indirectly controlling or  
12 controlled by, or under direct or indirect common control with, the public utility." The term  
13 "control" means "the power to direct the management policies of such entity, whether through  
14 ownership of voting securities, or by contract, or otherwise."

15 8. As discussed below, Staff believes that STARS does not meet the definition of an  
16 "affiliate" of APS and, as such, the Affiliated Interest Rules are not applicable to STARS.

17 **APS's Participation in STARS**

18 9. While Staff does not believe Commission review of the transaction is necessary  
19 because STARS is not an affiliate of APS, the Commission normally reviews affiliate transactions  
20 "to determine if the transactions would impair the financial status of the public utility, otherwise  
21 prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public  
22 utility to provide safe, reasonable and adequate service." A.C.C. R14-2-804(C).

23 10. Staff does not believe that APS's participation in STARS would affect the financial  
24 status of the Company or the ability of the Company to provide safe, reasonable, and adequate  
25 service.

26 11. APS expects that the goods and services APS is likely to acquire through STARS –  
27 those which the Company would likely acquire irrespective of the STARS transaction – may be  
28 acquired for less than they would otherwise by virtue of participation in STARS. Thus, STARS is

1 not anticipated to create any substantial new additional costs for APS which would impair the  
2 financial status of the Company. Additionally, the sharing of existing resources and best practices  
3 among STARS members will provide opportunities for improved operational efficiency and safety  
4 that may improve APS's ability to provide safe, reasonable and reliable services.

5 **STARS Structure and Governance**

6 12. Given the structure and governance of STARS, Staff does not believe that STARS  
7 could assert control over APS, nor does it seem that APS could assert control over STARS. The  
8 20 percent equity interest and the 14 percent voting power that APS would have in STARS is not  
9 enough to assert any control over the management decisions of STARS. The role of STARS is  
10 similarly limited as far as asserting control over APS. The voluntary nature of APS's participation  
11 in contractual relationships eliminates the ability of STARS or other Participants to direct the  
12 management policies of APS.

13 *Equity interest*

14 13. While STARS will have seven total participants, APS and four other Participants  
15 will be equity members of the proposed LLC, each providing \$1,000 as a capital contribution.  
16 Two Participants, STP Nuclear Operating Company and Wolf Creek Nuclear Operating  
17 Corporation, will be non-equity members of STARS to assure compliance with state law  
18 requirements unique to their organizations. As such, APS will have a 20 percent equity interest in  
19 STARS.<sup>4</sup>

20 *Series A Board*

21 14. STARS will be governed by a board of directors called the Series A Board. The  
22 Series A Board will be comprised of one representative from each of the seven Participants. Only  
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25 <sup>4</sup> STP Nuclear Operating Company is owned and operated in part by the City of Austin Texas and the City of San  
26 Antonio. Subject to certain exceptions not relevant here, the Texas Constitution prohibits cities from becoming  
27 stockholders or subscribers in private companies or from lending their credit or public money to a private company.  
28 See Tex. Const. Art. II, §§ 3 and 52. The Wolf Creek Nuclear Operating Corporation was formed by a collaborative of  
Kansas utility companies, including Kansas Gas and Electric Company, Kansas Power & Light Company and Kansas  
Electric Power Cooperative. At the time of formation, various representations were made to the respective public  
utility commissions of Kansas and Missouri that Wolf Creek Nuclear Operating Corporation would not own any  
property. As such, Wolf Creek Nuclear Operating Corporation believes that, consistent with its representations, it may  
not own equity in a private entity.

1 the Series A Board will have the authority to make decisions for STARS. No individual Participant  
2 will have the ability to make decisions on behalf of STARS.

3 15. Each representative on the Series A Board will be entitled to one vote, irrespective  
4 of Participant status as an equity or non-equity member and the number of nuclear generating units  
5 owned.

6 16. Decisions regarding management policy and other significant Series A Board  
7 decisions, such as, but not limited to, approving budgets, admitting new Participants, and  
8 expanding business activities, will require a unanimous vote of the Series A Board. Other  
9 significant actions, such as incurring expenses exceeding \$25,000 that had not been previously  
10 budgeted, will require a super majority vote, defined as a two-thirds vote of the Series A Board.

11 17. The STARS LLC Agreement provides that additional series of membership may be  
12 created to govern Participants involvement in specific joint projects that involve less than all seven  
13 of the Series A Participants. Each additional Series would be limited to a specific activity that a  
14 subset of STARS Participants elects to pursue.

15 *Costs*

16 18. STARS is intended to operate as a not-for-profit entity with STARS activities  
17 anticipated to assist each Participant in reducing or avoiding operating costs. STARS will be set-up  
18 so that each Participant is obligated only to pay its proportionate share for STARS activities it  
19 elects to participate in and, in exchange, it will receive a proportionate share of the economic  
20 benefits relating to those activities.

21 19. The costs associated with APS's proposed participation in STARS are anticipated  
22 to be approximately \$100,000 per year to support the operation of STARS. Costs will vary slightly  
23 from year to year, depending on the activities that are undertaken by STARS on behalf of the  
24 participants. If the STARS participants undertake new activities, a cost-benefit analysis will be  
25 performed so that only new activities with measureable benefits are added.

26 20. All Participants, including APS, will pay their fair proportionate share of allocable  
27 costs for goods and services that they elect to purchase. To the extent that STARS enters into  
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1 contractual relationships with third-party suppliers on behalf of the Participants, neither STARS  
2 nor any Participant can compel APS to purchase goods and/or services.

3 **Recommendations**

4 21. Given the structure of the Series A Board and the voluntary nature of participation  
5 in joint decisions, Staff does not believe that STARS can be characterized as an affiliate of APS.  
6 For that reason, Staff has recommended that Commission confirm that the Affiliated Interest Rules  
7 do not apply to APS's plans to become a member of STARS.

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CONCLUSIONS OF LAW

10 1. Arizona Public Service Company is an Arizona public service corporation within  
11 the meaning of Article XV, Section 2, of the Arizona Constitution.

12 2. The Commission has jurisdiction over APS and over the subject matter of the  
13 Application.

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1 3. The Commission, having reviewed the application and Staff's Memorandum dated  
2 March 12, 2012, concludes that it is in the public interest to approve APS's application for a  
3 declaratory order, as discussed herein.

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ORDER

IT IS THEREFORE ORDERED that the Affiliated Interest Rules do not apply to  
Arizona Public Service Company's plans to become a member of STARS.

**BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I, ERNEST G. JOHNSON,  
Executive Director of the Arizona Corporation Commission,  
have hereunto, set my hand and caused the official seal of  
this Commission to be affixed at the Capitol, in the City of  
Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2012.

\_\_\_\_\_  
ERNEST G. JOHNSON  
EXECUTIVE DIRECTOR

DISSENT: \_\_\_\_\_

DISSENT: \_\_\_\_\_

SMO:LAF:sms/MAS

1 SERVICE LIST FOR: ARIZONA PUBLIC SERVICE COMPANY  
2 DOCKET NO. E-01345A-11-0467

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