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BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION  
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IN THE MATTER OF THE APPLICATION OF  
TUCSON ELECTRIC POWER COMPANY FOR  
THE ESTABLISHMENT OF JUST AND  
REASONABLE RATES AND CHARGES  
DESIGNED TO REALIZE A REASONABLE RATE  
OF RETURN ON THE FAIR VALUE OF ITS  
OPERATIONS THROUGHOUT THE STATE OF  
ARIZONA.

Docket No. E-01933A-12-0291

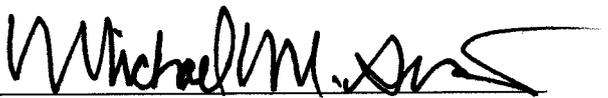
**NOTICE OF FILING DIRECT  
TESTIMONY IN SUPPORT OF  
SETTLEMENT AGREEMENT**

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Pursuant to the requirements of the September 6, 2012 Procedural Order in this matter, attached are the original and 13 copies of the Direct Testimony of Gary Yaquinto on behalf of the Arizona Investment Council in Support of the Settlement Agreement.

RESPECTFULLY SUBMITTED this 14<sup>th</sup> day of February, 2013.

GALLAGHER & KENNEDY, P.A.

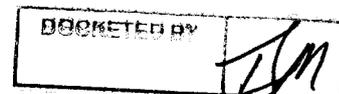
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Original and 13 copies filed this 14<sup>th</sup> day of February, 2013, with:

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Arizona Corporation Commission  
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Phoenix, Arizona 85007

Arizona Corporation Commission  
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1 **Copies** of the foregoing delivered  
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**BEFORE THE ARIZONA CORPORATION COMMISSION**

**COMMISSIONERS**

BOB STUMP, Chairman  
GARY PIERCE  
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IN THE MATTER OF THE APPLICATION OF  
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OPERATIONS THROUGHOUT THE STATE OF  
ARIZONA.

Docket No. E-01933A-12-0291

**Direct Testimony of**

**Gary Yaquinto**

**in Support of Proposed Settlement Agreement**

**on Behalf of**

**Arizona Investment Council**

**February 14, 2013**

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**I. INTRODUCTION**

**Q. Please state your name, position and business address.**

A. Gary M. Yaquinto. I am the President of the Arizona Investment Council (“AIC”). Our offices are located at 2100 North Central Avenue, Phoenix, Arizona 85004.

**Q. Have you previously filed testimony in this proceeding?**

A. Yes, I filed direct testimony on December 21, 2012. As I discussed in that testimony, AIC’s overriding interest in this case is to help ensure that TEP can attract capital on the best possible terms and rates for the investments which are needed to assure the State’s energy future.

**II. AIC SUPPORTS THE PROPOSED SETTLEMENT AGREEMENT**

**Q. What is the purpose of this testimony?**

A. My testimony will explain AIC’s support of the Proposed Settlement Agreement which was filed by the Commission Staff in this docket on February 4, 2012.

**Q. Is AIC a signatory to the Settlement Agreement?**

A. Yes. After intervening and filing testimony, we participated with the other signatories in the discussions and negotiations which led to the execution of the Settlement Agreement by more than a dozen parties to the case. We also participated in meetings arranged by the Company to discuss technical aspects of the Company’s filings.

1 **Q. Why does AIC support the Settlement Agreement?**

2 A. The primary reason AIC supports the Settlement Agreement is because it contains several  
3 provisions that are credit supportive including, but not limited to, the \$76 million non-  
4 fuel base rate increase; the Environmental Compliance Adjustment mechanism (“ECA”);  
5 and the Lost Fixed Cost Recovery procedure (“LFCR”). We also note that, generally,  
6 investors and credit rating agencies look favorably on settlement agreements, because  
7 they resolve issues, which otherwise could lead to regulatory delay, in a more timely and  
8 often a more creative way.

9  
10 Finally, it’s important to stress that TEP’s current rates were approved in late December  
11 2008 based on expenses and income in a 2006 test year. The fact that this many years  
12 later the Settlement Agreement holds the average residential bill impact of the rate  
13 increase to under \$3.00 in these circumstances is remarkable.

14 **Q. Are there particular Settlement Agreement provisions which AIC wants to stress?**

15 A. Yes. First, the ECA enables the Company to seek recovery of some of the costs  
16 necessary to meet government-mandated environmental standards without having to go  
17 through a full rate case. Although this ECA is different than the adjustor mechanism  
18 proposed by TEP and which I supported in my direct testimony, the Settlement  
19 Agreement’s ECA is modeled after a similar adjustor which was approved for APS. It is  
20 an acceptable way to afford more timely recovery on these investments over which TEP  
21 has little-to-no control. It is credit supportive and will be viewed as such by the markets.  
22  
23

1 It's equally important to stress that the ECA is also customer-friendly in two ways. First,  
2 costs to be recovered through the ECA are subject to a cap equal to 0.25 percent of total  
3 TEP retail revenues. Second, by allowing more timely recovery of some of the costs of  
4 these governmentally-mandated controls through small adjustments in between rate  
5 cases, the ECA smooths future consumer rate impacts from general rate increases.

6  
7 The LFCR mechanism in the Settlement Agreement is another important feature from our  
8 standpoint. It helps stabilize earnings which result from unrecovered fixed costs due to  
9 lower sales volumes caused by energy efficiency programs.

10 Additionally, the cost of capital elements contained in the Settlement Agreement, which  
11 include a 10 percent return on equity, are reasonable in this case and are generally credit  
12 supportive.

13  
14 **Q. Are there other reasons for AIC's support of the Settlement Agreement?**

15 **A.** Yes. The Settlement Agreement provides several other provisions we would note.

16  
17 The Settlement Agreement provides an alternative to the LFCR rate mechanism for  
18 residential customers; thus providing a consumer a choice as to different rate approaches  
19 which support energy efficiency programs implemented by the Company. The  
20 Settlement Agreement also assures continuing bill assistance for low-income customers.

21 Finally, the AIC continues to believe that settlement agreements provide opportunities for  
22 creative solutions among parties that would not be available through or produced by  
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litigated proceedings. Settlements like the one reached in this case also help streamline the regulatory process and they lower costs to all parties.

**III. AIC'S RECOMMENDATION REGARDING THE SETTLEMENT AGREEMENT**

**Q. Mr. Yaquinto, what is AIC's recommendation for the Commission in relation to the Settlement Agreement?**

A. The Settlement Agreement represents an appropriate, productive balance among the often widely divergent views of the parties on a broad and challenging set of issues. In reaching that accord, the process was open and transparent and the result reflects give and take on the part of all participants. It builds on progress from the last rate case and should give the Company a realistic opportunity to recover its prudent costs and to earn a reasonable rate of return on investment. We recommend the Commission enter its Order approving the Settlement Agreement.

**Q. Does that conclude your testimony?**

A. Yes.