

OPEN MEETING ITEM



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SUSAN BITTER SMITH



JODI JERICH  
Executive Director

ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION  
DOCKET CONTROL

2014 DEC 23 PM 1 43

DATE: DECEMBER 23, 2014

DOCKET NO.: E-04204A-13-0476

ORIGINAL

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Jane L. Rodda. The recommendation has been filed in the form of an Opinion and Order on:

UNS ELECTRIC, INC.  
(FINANCE)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

JANUARY 2, 2015

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

JANUARY 13, 2015 and JANUARY 14, 2015

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

Arizona Corporation Commission

DOCKETED

DEC 23 2014

DOCKETED BY

JODI JERICH  
EXECUTIVE DIRECTOR

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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 BOB STUMP - Chairman  
4 GARY PIERCE  
5 BRENDA BURNS  
6 BOB BURNS  
7 SUSAN BITTER SMITH

8 IN THE MATTER OF THE APPLICATION OF  
9 UNS ELECTRIC, INC. FOR AN ACCOUNTING  
ORDER IN CONNECTION WITH THE  
ACQUISITION OF UP TO A 25% INTEREST IN  
GILA RIVER POWER PLANT UNIT #3.

DOCKET NO. E-04204A-13-0476

DECISION NO. \_\_\_\_\_

OPINION AND ORDER

10 DATE OF HEARING: December 15, 2014

11 PLACE OF HEARING: Tucson, Arizona

12 ADMINISTRATIVE LAW JUDGE: Jane L. Rodda

13 APPEARANCES: Michael Patten, ROSHKA, DEWULF &  
14 PATTEN, PLC, and Bradley Carroll, UNS  
Electric, Inc., on behalf of UNS Electric, Inc.;

15 Daniel Pozefsky, Chief Counsel, Residential  
16 Utility Consumer Office;

17 Charles Hains and Matthew Laudone, Staff  
18 Attorneys, Arizona Corporation Commission  
Legal Division, on behalf of the Utilities  
19 Division.

20 **BY THE COMMISSION:**

21 \* \* \* \* \*

22 Having considered the entire record herein and being fully advised in the premises, the  
23 Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

24 FINDINGS OF FACT

25 Procedural History

26 1. On December 31, 2013, UNS Electric, Inc. ("UNSE" or "Company") filed an  
27 Application with the Commission seeking approval of an accounting order authorizing the deferral for  
28 future recovery of non-fuel costs associated with the Company's prospective purchase of up to a 25

1 percent interest in Unit 3 at the Gila River Power Plant.

2           2.       On March 7, 2014, intervention was granted to Arizona Public Service Company  
3 (“APS”) and the Residential Utility Consumer Office (“RUCO”).

4           3.       On October 28, 2014, the Commission’s Utilities Division (“Staff”) filed the Direct  
5 Testimony of Gerald Becker recommending approval of an accounting order subject to Staff’s  
6 proposed conditions and clarifications.

7           4.       On October 29, 2014, RUCO filed a Request for Procedural Order seeking a procedural  
8 schedule in this matter.

9           5.       By Procedural Orders dated November 3, and November 6, 2014, a telephonic  
10 Procedural Conference was set for November 17, 2014, to discuss establishing procedures for this  
11 matter.

12           6.       UNSE, RUCO and Staff appeared through counsel at the November 17, 2014  
13 Procedural Conference, and agreed on a process for a hearing in this matter.

14           7.       By Procedural Order dated November 18, 2014, the matter was set for hearing on  
15 December 15, 2014, and other procedural deadlines established.

16           8.       On December 2, 2014, UNSE filed affidavits of publication indicating that public  
17 notice of the hearing was published on November 28, 2014, in the *Nogales International*, in Santa  
18 Cruz County, Arizona, and on November 29, 2014, in the *Today’s News-Herald* in Mohave County,  
19 Arizona.

20           9.       On December 5, 2014, RUCO filed the Direct Testimony of Jeffrey Michlik, and  
21 UNSE filed the Direct Testimony of Dallas Dukes.

22           10.      On December 12, 2014, UNSE filed the Plan of Administration (“POA”) for the  
23 proposed accounting order.

24           11.      On December 15, 2014, the hearing convened as scheduled before a duly authorized  
25 Administrative Law Judge at the Commission’s offices in Tucson, Arizona. Mr. Dukes, the Senior  
26 Director of Pricing and Economic Forecasting for Tucson Electric Power Company (“TEP”) testified  
27 for UNSE. Mr. Dukes is responsible for monitoring and determining revenue requirements, customer  
28 pricing and rate structures for all the regulated subsidiaries of UNS Energy Corporation (“UNS

1 Energy”), including UNSE. Mr. Michlik, a Public Utilities Analyst V, testified for RUCO. Gerald  
2 Becker, Executive Consultant III, testified for Staff.

3 12. At the hearing, UNSE introduced a revised POA that included a minor addition from  
4 the version that was docketed on December 12, 2014.<sup>1</sup> A copy of the POA, as agreed to by UNSE,  
5 Staff and RUCO is attached hereto as Exhibit A.

6 **Background**

7 13. UNSE is a wholly owned subsidiary of UNS Energy, and provides electric service to  
8 approximately 93,000 customers in Mohave and Santa Cruz Counties.<sup>2</sup>

9 14. UNSE states that it filed the subject application in December 2013 because it has the  
10 opportunity to acquire up to a 25 percent interest in the Gila River Power Plant Unit 3 (Gila River Unit  
11 3” or “Unit 3”), which is a combined-cycle natural gas fired power plant located on approximately  
12 1,100 acres within the Gila Bend town-site, about 75 miles southwest of Phoenix and 30 miles south  
13 of the Palo Verde Trading hub. According to UNSE, Unit 3 consists of four “power blocks” with each  
14 block representing 550 MW of nominal capacity. UNSE’s sister company, TEP, which provides  
15 electric service in Pima and Cochise Counties, will acquire the other 75 percent of Unit 3.

16 15. The Federal Energy Regulatory Commission (“FERC”) approved UNSE’s acquisition  
17 of the interest in Gila River Unit 3 from Gila River Power, L.L.C., and the Company closed the  
18 transaction in the second week of December 2014. UNSE does not need Commission approval to  
19 acquire an interest in Gila River Unit 3.

20 16. UNSE states that Gila River Unit 3 provides the Company with a unique opportunity  
21 to address its need for base load generation at a reasonable price.<sup>3</sup> Prior to the purchase of Unit 3,  
22 UNSE states that it relied on the wholesale market for approximately 85 percent, or 300-325 MW, of  
23 its annual resource capacity needs, and that acquisition of the share in Unit 3 will reduce its market-  
24 based capacity exposure by 45 percent.<sup>4</sup> UNSE states that although its heavy reliance on wholesale  
25 power has not been problematic in recent years when natural gas prices and capacity values have  
26

27 <sup>1</sup> December 15, 2014 Hearing Transcript (“Tr.”) at 6 and 13.

<sup>2</sup> Application at 2.

28 <sup>3</sup> Ex S-2 Dukes Dir at 1.

<sup>4</sup> *Id.* at 2-3.

1 remained low, for the long-term, market forces could drive energy and capacity costs up and reduce  
 2 the availability of low cost market resources. UNSE claims that the Commission acknowledged  
 3 UNSE's risk in May 2013 when it advised UNSE and other load serving entities about future short-  
 4 term market purchases in their long-term Integrated Resource Plans ("IRPs):

5           The cost and availability of such purchases are subject to a wide array of  
 6 influences that are difficult, if not impossible to predict. For example, if a  
 7 large number of older coal-fired generating plants are retired in the western  
 8 region, the availability of such purchases will decline dramatically, and the  
 cost of such purchases will increase significantly. Reliance on short term  
 market purchases in a long-term plan is difficult, if not impossible to  
 justify.<sup>5</sup>

9 In UNSE's 2012 IRP and confirmed in its 2014 IRP, the Company stated that it will look for  
 10 economically attractive plant acquisition opportunities to firm up its long-term capacity needs.<sup>6</sup>

11           17. UNSE states that an advantage of the Gila River Power Plant is its proximity to  
 12 transmission and natural gas supplies.<sup>7</sup> UNSE asserts that the Gila River Power Plant is one of the  
 13 most efficient combined-cycle plants in the Western Electric Coordinating Council ("WECC") region.  
 14 With a heat rate of approximately 7,000 British thermal units ("BTUs") per kilowatt-hour ("kWh"),  
 15 UNSE believes that it provides a solid base resource by reducing the overall heat-rate when compared  
 16 to market heat rates and existing assets.<sup>8</sup>

17           18. UNSE asserts that acquiring its share of Unit 3 is a significant investment for UNSE, as  
 18 the purchase price of approximately \$55 million represents about 28 percent of the Company's  
 19 original cost rate base established in its last rate case. In addition, the Company states that the non-fuel  
 20 operating costs associated with the purchase are expected to be approximately \$9 million by the end of  
 21 2015, and if not deferred and subject to potential future recovery, would reduce net income by 42%  
 22 (based on 2013 operating results).<sup>9</sup>

23           19. At the time of the hearing, UNSE's debt was rated Baa1 by Moody's Investor Service  
 24 ("Moody's").<sup>10</sup> UNSE argues that without an accounting order that would allow the deferral of certain  
 25

26 <sup>5</sup> Application at 2 *quoting* Decision No. 73884 at 4.

27 <sup>6</sup> Application at 2 *citing* UNSE IRP at 13.

28 <sup>7</sup> Ex A-2 Dukes Dir at 4.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* at 5-6; Tr. at 14.

<sup>10</sup> Ex A-2 Duke's Dir at 6. This is an upgrade from Baa2 since the Company filed its Application.

1 operating expenses associated with Unit 3, the Company would face financial burdens because of the  
 2 size of the investment relative to its capitalization. The Company is particularly concerned about  
 3 maintaining its credit rating as it expects to refinance \$80 of its existing long-term debt due in 2015.<sup>11</sup>

4 **UNSE's Deferral Request**

5 20. Because UNSE's share of the purchase price of Gila River Unit 3 is a substantial  
 6 investment relative to its current rate base, UNSE is seeking an order that would allow the deferral for  
 7 future recovery of the non-fuel costs of maintaining and operating the plant. Following discussions  
 8 with Staff, the Company revised its request from that originally set forth in its application. The  
 9 Company seeks authorization of the following:<sup>12</sup>

10 (a) The deferral of the non-fuel costs associated with owning, operating and  
 11 maintaining UNSE's share of Unit 3 including Operating and Maintenance ("O&M") expenses,  
 12 depreciation and amortization expense, property taxes and carrying costs at a rate of 5.0 percent  
 13 annually;

14 (b) Reductions to UNSE's purchased energy and capacity costs to be retained by the  
 15 Company from the purchase date through the date on which on the plant is placed into rate base upon  
 16 completion of the Company's next rate case;<sup>13</sup>

17 (c) During this period, the purchased energy and capacity savings would serve to off-  
 18 set all, or a portion of, the increase in the Company's non-fuel costs associated with owning and  
 19 operating Unit 3;

20 (d) Upon completion of the Company's next rate case, the ongoing energy and capacity  
 21 cost savings provided by Unit 3 would be passed onto customers, thus mitigating an expected future  
 22 increase in the Company's non-fuel base rates;

23 (e) The purchased energy cost savings shall be calculated monthly based on the  
 24 difference between the actual Unit 3 fuel costs (net of revenues from short-term wholesale sales) and  
 25 the market value of Unit 3 energy production used to service retail load (calculated using published on  
 26 \_\_\_\_\_

27 <sup>11</sup> Tr. at 20.

<sup>12</sup> *Id.* at 6-8.

28 <sup>13</sup> Thus, the benefits of lower fuel or power costs that would otherwise flow to ratepayers through the Purchase Power and Fuel Adjustment Clause ("PPFAC") will also be deferred.

1 and off-peak market prices from the Intercontinental Exchange (“ICE”));

2 (f) The avoided cost of capacity purchases shall be \$1.52 per kW/month, which is  
3 based on third-party quotes for 2015 demand (capacity) options, and which is approximately \$2.5  
4 million on an annual basis;

5 (g) The margin from short-term wholesale sales shall be based on revenues from short-  
6 term wholesale sales less the actual fuel costs for Unit 3 allocated to wholesale sales;

7 (h) The reductions to UNSE’s purchased energy and capacity costs, and the increases  
8 in the margin on short-term wholesale sales, resulting from the ownership of Unit 3, shall be  
9 calculated monthly; and

10 (i) The amount of these cost savings recovered through UNSE’s PPFAC shall not be  
11 included in the Accumulated PPFAC Bank Balance for purposes of calculating accrued interest.

12 21. UNSE asserts that although its revised request is somewhat different from what it  
13 requested initially, the revised approach recognizes several benefits from the deferral of benefits  
14 including: (1) a better matching of customer savings with the costs associated with owning and  
15 operating Unit 3; (2) mitigation of the initial customer rate impact expected to result from UNSE’s  
16 next rate case; and (3) improved cash flow for UNSE during the cost deferral period, which should  
17 further support the Company’s investment grade rating.<sup>14</sup>

18 **Staff’s Position**

19 22. Staff supports approval of an accounting order in this proceeding in conformance with  
20 the Company’s revised request which matches deferred savings and deferred costs, and produces a  
21 less volatile rate impact.<sup>15</sup>

22 23. Staff agrees with the Company’s revised request, and recommended that the deferral of  
23 costs be subject to both a time and dollar limitation. Staff recommends approval of an accounting  
24 order as follows:

25 (a) That cost subject to deferral be limited to:

26 (i) Depreciation and amortization costs;

27 \_\_\_\_\_  
28 <sup>14</sup> Ex A-2 Dukes Dir at 8; Tr. at 22, 25-27.

<sup>15</sup> Ex S-1 Becker Dir. Executive Summary; Tr. at 65-66.

- 1 (ii) Property taxes,  
2 (iii) O&M expenses, and  
3 (iv) Carrying costs, calculated at 5.0 percent annually, associated with owning,  
4 operating, and maintaining the plant;
- 5 (b) That certain benefits of owning the plant shall also be deferred;  
6 (c) That the value of deferred benefits shall be subject to inclusion in the Company's  
7 ongoing PPFAC calculations;
- 8 (d) That the deferred cost and deferred benefits shall be evaluated in a future rate  
9 proceeding;
- 10 (e) That the ratepayers be held harmless for any deferred costs in excess of deferred  
11 benefits;
- 12 (f) That the amount of any deferred benefits in excess of deferred costs shall be used as  
13 a reduction to the running balance in the PPFAC arising from non-Gila River Unit 3 activity;<sup>16</sup>
- 14 (g) That any authorizations to defer costs shall be limited to \$10.5 million;  
15 (h) That any authorizations to defer costs shall expire no later than May 1, 2016. Any  
16 expense incurred after April 30, 2016, would not be eligible for deferral; and
- 17 (i) That no prudence determination be made at this time and that the prudence of the  
18 purchase of Gila River Unit 3 will be determined in a future rate proceeding; that there shall be no  
19 carrying costs on any under-recovered PPFAC balance resulting from the purchase of Gila River Unit  
20 3; and that the Company file a plan of administration within 30 days of the filing of testimony for  
21 consideration and inclusion in the final decision.

22 24. Staff disagrees with UNSE's interpretation of its IRP pursuant to Decision No. 73884.  
23 Staff states that in Decision No. 73884, Staff concluded that UNSE should reduce its reliance on short-  
24 term purchases to meet its long-term needs, and this could be achieved by pursuing long-term  
25 purchased power and not just the purchase of the power plant as Staff believes the Company seems to  
26 suggest. Staff states that Decision No. 73884 did not order UNSE to buy a power plant, nor has UNSE  
27

28 <sup>16</sup> Tr. at 57.

1 sent any proposals to secure long-term power contracts as an alternative to purchasing Gila River Unit  
2 3.<sup>17</sup>

3 **RUCO's Position**

4 25. RUCO supports approval of an accounting order as recommended by Staff and the  
5 Company in this proceeding because:

6 (a) UNSE is only asking that 25 percent share of the Gila River Unit 3 be subject to  
7 deferral, and TEP is not requesting a deferral order for the other 75 percent interest;

8 (b) RUCO agrees with the Company that the acquisition of Gila Unit 3 will have a  
9 significant impact on UNSE's financial statements, and that if an accounting order is not approved,  
10 this could affect UNSE's financial viability in the future;

11 (c) The environmental risks are less for a combined cycle natural gas-fired unit than for  
12 a coal-fired unit, and the lower environmental risks will benefit both UNSE and its ratepayers;

13 (d) UNSE is not requesting deferral of decommissioning costs;

14 (e) It is expected that ratepayers will benefit through UNSE's PPFAC;

15 (f) The transaction will result in an acquisition discount, which benefits both UNSE  
16 and its ratepayers;

17 (g) There is a deferral time period and limitation on the amount that can be deferred;

18 (h) Ratepayers will be held harmless for any deferred costs in excess of deferred  
19 benefits, and there will be no carrying costs on any under-recovered PPFAC balance resulting from  
20 the purchase of Gila River Unit 3; and

21 (i) Although RUCO generally does not approve of carrying costs, RUCO believes that  
22 a carrying cost of 5.0 percent is reasonable in this case and this case only for the reasons cited above.<sup>18</sup>

23 26. RUCO agrees with Staff's recommendations and recommends an additional condition  
24 as follows: in the event a settlement agreement is reached in UNSE's next rate case, any changes to  
25 the deferral order including changes to the carrying costs shall be thoroughly explained in the  
26 settlement agreement.<sup>19</sup>

27 <sup>17</sup> Ex S-1 Staff Dir at 5.

28 <sup>18</sup> Ex RUCO-1 Michlik Dir at 22-23 (emphasis in original); *see also* Tr. at 36-36 and 52-53.

<sup>19</sup> RUCO's proposed recommendation was inspired by events occurring in a proceeding involving Arizona Public Service.

1           27.     RUCO believes the proposed accounting order is in the best interest of ratepayers and  
2 agrees with the final POA as presented at the hearing.<sup>20</sup>

3 **Plan of Administration**

4           28.     The POA, attached as Exhibit A, describes how the proposed Gila River Power Plant  
5 Unit 3 Acquisition Deferred Accounting Order will operate. The POA allows UNSE to defer certain  
6 defined non-fuel costs for the period January 1, 2015 through the earlier of April 30, 2016, or the date  
7 new rates goes into effect.<sup>21</sup> It provides that the cumulative non-fuel costs will not exceed the lower  
8 of \$10.5 million or the cumulative deferred savings as of April 30, 2016. The deferred savings will  
9 continue to accrue until new rates go into effect, but the deferred costs will not extend beyond April  
10 30, 2016. The POA provides that UNSE will file monthly reports with Docket Control, and to RUCO  
11 detailing the calculations related to allowable costs and savings.

12           29.     The POA defines the costs and savings eligible for deferral consistent with the parties'  
13 testimony, except that the POA does not include express recognition that decommissioning costs will  
14 not be included in the eligible O&M costs.<sup>22</sup>

15           30.     The POA should be amended to reflect the agreement of the parties that  
16 decommissioning costs related to Gila River Unit 3 are not included as part of eligible deferred costs.

17 **Analysis and Conclusion**

18           31.     An accounting order is a rate-making mechanism that allows the deferral of costs  
19 and/or savings by a regulated utility for possible future recovery or credit.

20           32.     Under the typical ratemaking process, until the Commission would authorize the  
21 inclusion of the Gila River Unit 3 in rate base, UNSE would not be able to recover the costs of  
22 operating the plant in rates. By approving an accounting order and the POA, the Commission is  
23 authorizing UNSE to create a regulatory asset composed of the cumulative eligible deferred costs  
24 related to operating Gila River Unit 3, and a regulatory liability consisting of the eligible deferred  
25 savings. The Commission will determine how to amortize the regulatory asset and liability in UNSE's

26 \_\_\_\_\_  
<sup>20</sup> Tr. at 32.

27 <sup>21</sup> POA Section 1.

28 <sup>22</sup> RUCOs testimony explicitly mentions that that decommissioning costs will not be included in the deferred costs. Ex RUCO-1 at 16 and Tr. at 35. Mr. Dukes confirmed that the Company will not seek the deferral of decommissioning costs which are usually included as part of depreciation expense. Tr. at 29.

1 next rate case which is expected to be filed in the second quarter of 2016. Absent such accounting  
 2 order, UNSE would be required by Generally Accepted Accounting Principles ("GAAP") to expense  
 3 the operating costs of the plant in the period incurred, and these costs could not retroactively be  
 4 recovered as part of rates.

5 33. We find that under the particular circumstances of this case, approving an accounting  
 6 order, governed by the provisions of the POA as modified herein, is in the public interest. UNSE has  
 7 shown, and Staff and RUCO agree, that the acquisition of the Gila River Unit 3 is likely to benefit the  
 8 Company and ratepayers by providing an efficient and economical source of baseline power, but that  
 9 the financial cost of acquiring and operating UNSE's share in Gila Unit 3 is substantial and may  
 10 detrimentally impact the Company's financial condition. The accounting order is intended as a bridge  
 11 to maintain UNSE's financial condition until its next rate case. As the parties have agreed, ratepayers  
 12 are protected by the limits in amount and in time of the eligible deferred costs, and by the provision  
 13 that deferred costs cannot exceed the deferred benefits.

14 34. By approving the POA, the Commission makes no findings concerning the prudence  
 15 of the purchase of the Gila River Power Plant Unit 3 for ratemaking purposes.

#### CONCLUSIONS OF LAW

17 1. UNSE is a public service corporation within the meaning of Article XV of the Arizona  
 18 Constitution and A.R.S. §§ 40-250, 40-251, 40-221, 40-361 and 40-367.

19 2. The Commission has jurisdiction over UNSE and the subject matter of the application.

20 3. Notice of the application was provided in accordance with the law.

21 4. It is reasonable and in the public interest to authorize UNSE to defer, for possible later  
 22 recovery through rates, the non-fuel costs (as defined in the Plan of Administration) of owning,  
 23 operating, and maintaining its share of the Gila River Power Plant Unit 3.

24 5. The cost deferral authorized herein does not constitute a finding or determination that  
 25 the deferred costs are reasonable, appropriate, or prudent.

26 ...

27 ...

28 ...



1 IT IS FURTHER ORDERED that in the event a settlement agreement is reached in UNS  
2 Electric, Inc.'s next rate case, any changes to the deferral order, including but not limited to the  
3 carrying costs, shall be thoroughly explained in the settlement agreement.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.  
6  
7

8 CHAIRMAN \_\_\_\_\_ COMMISSIONER \_\_\_\_\_

9  
10 COMMISSIONER \_\_\_\_\_ COMMISSIONER \_\_\_\_\_ COMMISSIONER \_\_\_\_\_

11  
12 IN WITNESS WHEREOF, I, JODI JERICH, Executive  
13 Director of the Arizona Corporation Commission, have  
14 hereunto set my hand and caused the official seal of the  
15 Commission to be affixed at the Capitol, in the City of Phoenix,  
16 this \_\_\_\_\_ day of \_\_\_\_\_ 2015.

17 \_\_\_\_\_  
18 JODI JERICH  
19 EXECUTIVE DIRECTOR

20 DISSENT \_\_\_\_\_

21 DISSENT \_\_\_\_\_  
22 JR:tv

1 SERVICE LIST FOR: UNS ELECTRIC, INC.

2 DOCKET NO.: E-04204A-13-0476

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UNS Electric, Inc.  
Gila River Power Plant Unit 3 Acquisition Accounting Order  
Plan of Administration

Table of Contents

1. General Description..... 1  
2. Definitions.....1  
3. Allowable Deferred Costs.....2  
4. Allowable Deferred Savings.....2  
5. Compliance Reports.....3

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EXHIBIT A

## 1. GENERAL DESCRIPTION

This document describes the plan of administration for the Gila River Power Plant Unit 3 Acquisition Deferred Accounting Order ("Order") as approved by the Arizona Corporation Commission ("ACC") in Decision No. XXXXX (date) for UNS Electric, Inc. ("UNSE" or "Company").

The Order authorizes the deferral of certain Non-fuel costs (collectively defined as "Deferred Costs" in Section 3), and short-term fuel and purchased power savings (collectively defined as "Deferred Savings" in Section 4) associated with the Company's purchase of a 25% interest in Unit 3 at the Gila River Power Plant ("Gila 3"). These Deferred Costs and Deferred Savings will be evaluated during the Company's next rate case. During this interim period between January 1, 2015, and the earlier of April 30, 2016, or the date new rates go into effect for UNSE (the "Deferral Period"), the cumulative Deferred Cost will not exceed the lower of \$10.5 million or the cumulative Deferred Savings as of April 30, 2016. For purposes of calculating the Purchased Power and Fuel Adjustment Clause ("PPFAC"), Deferred Savings will continue to accrue until new rates become effective; however, cumulative Deferred Costs will not increase after April 30, 2016, regardless of Deferred Savings applicable to periods after April 30, 2016.

## 2. DEFINITIONS

Accounting Order – A rate-making mechanism used by a regulatory authority that allows the deferral of costs and/or savings by a regulated utility for possible future recovery or credit.

Carrying Costs – Costs accrued at a 5.0000% annual rate on the company's Net Book Investment of Gila 3 including the Company's pro rata share of any directly related associated Material and Supplies.

Fuel and Purchased Power Costs – The costs recorded for the fuel and purchased power used by UNSE to serve both Native Load Energy Sales and Wholesale Sales. Wheeling costs are included in Fuel and Purchased Power costs.

Native Load Energy Sales – Retail Native Load Energy Sales and Wholesale Native Load Energy Sales in the UNSE control area for which UNSE has a generation service obligation.

Net Book Investment – The cost of the Company's investment in its share of the plant, reduced by total depreciation and amortization recorded, plus the Company's pro-rata share of any directly related Materials and Supplies.

Off-Peak Power – Power for delivery Monday through Saturday from hour ending 2300 through hour ending 0600 Pacific Prevailing Time, and hour ending 0100 through hour ending 2400 Pacific Prevailing Time on Sunday and North American Electric Reliability Corporation ("NERC") holidays.

On-Peak Power – Power for delivery Monday through Saturday, excluding NERC Holidays, from hour ending 0700 through hour ending 2200, Pacific Prevailing Time.

Off System Sales - Energy sales other than those to directly meet the Company's native load obligations.

Palo Verde Hub - Palo Verde, also known as "PV" is a major cumulative western market trading hub that includes the Palo Verde substation and the Hassayampa substation.

PPFAC - The Purchased Power and Fuel Adjustment Clause ("PPFAC") initially approved by the Commission in Decision No. 70360, and amended in Decision No. 74235. The PPFAC rate tracks the changes in the cost of obtaining power supplies based upon a historical 12-month rolling average of fuel, purchased power and purchased transmission costs as defined in the PPFAC Plan of Administration and is adjusted monthly.

Short-term Sales - Wholesale sales with a duration of less than one year made to non-Native Load customers for the purpose of optimizing the UNSE system, using UNSE-owned or contracted generation and purchased power.

Wholesale Sales - Sales to non-retail customers.

### **3. ALLOWABLE DEFERRED COSTS**

The Deferred Costs as defined below, associated with owning, operating and maintaining UNSE's 25% interest in Gila 3 will be deferred as a regulatory asset during the Deferral Period, subject to the lower of \$10.5 million or the cumulative Deferred Savings as of April 30, 2016. The costs eligible for deferral are limited to:

1. Depreciation and Amortization costs.
2. Property taxes.
3. O&M expenses.
4. Carrying Costs on Net Book Investment, both as defined above.

### **4. ALLOWABLE DEFERRED SAVINGS**

The Deferred Savings associated with owning and operating UNSE's 25% interest in Gila 3 will be deferred as a regulatory liability, and will accrue during the period beginning January 1, 2015 and ending upon the date new rates go into effect following UNSE's next rate case. The Deferred Savings are limited to:

1. Energy costs based on published PV (the major wholesale power hub for UNSE's service territory) day-ahead-market prices from the Intercontinental Exchange ("ICE") for On-Peak and Off-Peak power, less actual fuel costs, plus
2. Avoided long term capacity procurement costs at \$1.52 per kW/month as approved in Accounting Order Decision No. [XXXXXXX], and offset by
3. Short term wholesale sales revenues associated with Gila 3.

Deferred Savings are considered "allowable costs" for purposes of calculating UNSE's PPFAC but will not be included as part of the PPFAC bank for purposes of calculating accrued interest.

**5. COMPLIANCE REPORTS**

UNSE shall provide monthly reports to the Commission's Docket Control and to the Residential Utility Consumer Office detailing all calculations related to allowable cost included in the PPFAC. Monthly reports will be due within 45 days of the end of a reporting period. The information contained in the Compliance Reports will consist of the following schedules:

- Schedule A: Allowable Deferred Costs
- Schedule B: Allowable Deferred Savings
- Schedule C: Any Wholesale Sales which are 1 year or greater in duration. This schedule shall describe the dates, the number of MW's sold, type of service (firm, non-firm, etc.) and ancillary services (if any), type of sale (on peak, around the clock, etc.),

Gila River Acquisition Deferred Accounting Order  
Schedule A - Deferred Costs

Line No.	Allowable Components	June-15	July-15	Aug-15	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16	Feb-16	Mar-16	Apr-16
1	Purchased Price	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
2	Material and Supplies <sup>1</sup>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
3	Accumulated Depreciation	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
4	Total Rate Base (Line 1 + 2 + 3)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
5	Carrying Costs (Line 4 * 0.03 / 12) <sup>2</sup>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
6	Depreciation and Amortization	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
7	Property Tax	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
8	Operating and Maintenance	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
9	Deferred Costs (Line 5 + 6 + 7 + 8)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
9	Total Deferred Costs <sup>3</sup>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Notes:

- UNSE share of material and supplies attributable to Gila River
- Carrying Costs are calculated at 3% per location, 52X2X2X
- Total Cumulative Deferred Costs will not exceed the lower of \$10.5 million or the cumulative Deferred Savings as of April 30, 2016.

DECISION NO. \_\_\_\_\_

UNS Electric, Inc.  
Gila River Acquisition Deferred Accounting Order  
Schedule B - Deferred Savings

Line No.	Accountable Components	Jan-15	Feb-15	Mar-15	Apr-15	May-15	Jun-15	Jul-15	Aug-15	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16	Feb-16	Mar-16
1	Total Gila River Generation for UNSE, MWh (Line 4 + 11)															
2	Gila River Retail On-Peak, MWh															
3	Gila River Retail Off-Peak, MWh															
4	Total Gila River Retail, GWh (Line 2 + 3)															
5	Palo Verde ICE, On-Peak, \$/MWh (1)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
6	Palo Verde ICE, Off-Peak, \$/MWh (1)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
7	Market Value of Replacement Energy On-Peak (Line 2 * 5)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
8	Market Value of Replacement Energy Off-Peak (Line 3 * 6)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
9	Market Value of Replacement Energy (Line 7 + 8)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
10	Avg. Market Value of Replacement Energy, \$/MWh (Line 9 / 4)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
11	Wholesale Sales from Gila River, MWh (Line 1 - 4)															
12	Wholesale Sales Revenues from Gila River (Line 11 * 13)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
13	Avg. Wholesale Sales from Gila River, \$/MWh	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
14	Gila River Fuel Expense															
15	Gila River Fuel Burn, GWh															
16	Gila River Fuel Expense, \$/MWh (Line 14 / 1)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
17	Gila River Fuel Expense, \$/MWh (Line 14 / 15)	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
18	Market Value of Replacement Energy (Line 9)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
19	Wholesale Sales Revenues from Gila River (Line 12)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
20	Avoided Capacity Savings (2)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
21	Less Gila River Fuel Expenses (Line 14)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
22	Total Deferred Savings (Line 18 + 19 + 20 + 21)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
23	Cumulative Deferred Savings	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Notes:  
1 To be based on market prices from the Intercontinental Exchange (ICE)  
2 Capacity Purchases are \$1.52 per kW/month per Decision XXXXX

UNS Electric, Inc.  
Gila River Acquisition Deferred Accounting Order  
Schedule C - Long-Term Wholesale Sales by UNS Electric, Inc.

UNS Electric *did not* enter into any wholesale sales contracts with a term of at least 12 months

UNS Electric entered into the following wholesale sales contract(s) with a term of at least 12 months. (1)

Line No.	Counterparty	Start Date	End Date	Monthly Sales (MWh)	Firm or Non-Firm	On-Peak, Off-Peak, Around-the Clock	Ancillary Services (if any)
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1

Notes:

1 Confidential contract terms will be made available to Staff and RUCO pursuant to the terms of the protective agreement.