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BEFORE THE ARIZONA CORPORATION

COMMISSIONERS

BOB STUMP - Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

Arizona Corporation Commission

DOCKETED

DEC 18 2014

DOCKETED BY

IN THE MATTER OF THE JOINT APPLICATION
OF UNS ELECTRIC, INC. AND UNS GAS, INC.
FOR A FINANCING ORDER AUTHORIZING
VARIOUS FINANCING TRANSACTIONS.

DOCKET NO. E-04204A-13-0447
DOCKET NO. G-04204A-13-0447

DECISION NO. 74865

ORDER

Open Meeting
December 11 and 12, 2014
Phoenix, Arizona

BY THE COMMISSION:

* * * * *

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

FINDINGS OF FACT

Procedural History

1. On December 18, 2013, UNS Electric, Inc. ("UNS Electric") and UNS Gas, Inc. ("UNS Gas") (collectively, the "Companies") filed with the Commission pursuant to Arizona Revised Statutes ("A.R.S.") §§ 40-301 and 40-302, a Joint Application for Financing ("Application"). The Application requests that the Commission authorize the Companies to: (1) refinance their joint revolving credit facility that expires November 2016; (2) increase the amount of credit available under one or more revolving credit facilities to each company, individually, from \$70 million to \$100 million; (3) refinance long-term indebtedness maturing in August 2015; (4) increase the amount of long-term indebtedness outstanding at UNS Electric by up to \$80 million and at UNS Gas by up to \$50 million; (5) authorize UNS Electric to issue additional debt up to \$35 million and accept new equity contributions up to \$35 million in order to finance the purchase of a 25 percent interest in Gila

1 River Unit 3 (“Gila River”);¹ (6) authorize the Companies to provide security for any such financing
2 transactions; and (7) authorize the Companies to enter into these financings up to December 31, 2019.

3 2. The requested authority is intended to replace the financing authority granted in
4 Decision No. 71917 (October 12, 2010), which expires on December 31, 2014.

5 3. On March 28, 2014, the Companies filed “Notice of Filing Affidavits of Publication”
6 indicating that the public notice of the Application was published in *The Arizona Daily Star*
7 published in Flagstaff, Coconino County, on March 25, 2014; in *The Kingman Daily Miner* published
8 in Mohave County on March 24, 2014; in *The Nogales International*, published in Cochise County,
9 on March 25, 2014; in the *Courier*, published in Prescott, Yavapai County, on March 24, 2014; and
10 in *Today’s News-Herald*, published in Lake Havasu, Mohave County, on March 24, 2014.

11 4. On September 17, 2014, the Commission’s Utilities Division (“Staff”) filed its Staff
12 Report recommending that the Application be approved subject to conditions.

13 5. On September 30, 2014, the Companies filed a letter indicating that although they
14 agreed with the vast majority of Staff’s recommendations, they were working with Staff to address
15 two main concerns, and were attempting to agree upon clarifications and modifications to Staff’s
16 recommendations.

17 6. On October 9, 2014, the Companies filed Comments on Staff Report (“Comments”).
18 In their Comments, the Companies explained that specific language included in two of Staff’s
19 recommendations created significant concerns for the Companies, and also that the Companies
20 believed that they needed additional ordering language (beyond Staff’s recommendations) in order to
21 be able to fully utilize the authority Staff was recommending. The Companies attached proposed
22 language that incorporated and modified Staff’s recommendations. The filing indicated that Staff
23 was in agreement with the modifications as presented in the Comments.

24 7. By Procedural Order dated October 14, 2014, the parties were requested to clarify
25 certain points raised by their proposed modified recommendations.

26 8. On October 31, 2014, the Companies and Staff filed a Joint Response to the
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28 ¹ Gila River is a combined cycle gas fired power plant. A 25 percent interest equates to 137.5 MW. See Staff Report, Attachment A at 7.

1 Procedural Order (“Joint Response”), which offered a further modification to the proposed conditions
2 in an attempt to avoid ambiguity.

3 9. By Procedural Order dated November 4, 2014, the parties were requested to
4 supplement the record with information concerning UNS Gas’ capital budget and planned use for the
5 requested additional long-term debt.

6 10. On November 26, 2014, Staff filed a Supplemental Staff Report including the
7 Engineering Report for UNS Gas.

8 11. On November 26, 2014, the Companies filed a Response to the November 4, 2014
9 Procedural Order and Related Supplemental Staff Report, indicating that they support the
10 Supplemental Staff Report, and also waive the ten-day exception period to the extent necessary to
11 facilitate having this matter considered by the end of the year.

12 **Background**

13 12. The Companies are wholly owned subsidiaries of UniSource Energy Services, Inc.
14 (“UES”), which in turn is owned by UNS Energy Corporation (“UNS”).² The Companies are for-
15 profit “Class “A” Arizona public service corporations with their principal offices located in Tucson,
16 Arizona.

17 13. UNS Electric is a vertically integrated electric utility serving approximately 92,500
18 retail customers in Mohave and Santa Cruz counties. In 2013, UNS Electric had a peak demand of
19 427 MW. UNS Electric owns 153 MW of conventional gas fired generation capacity and makes
20 market capacity purchases (conventional and renewable) to meet the remainder of its demand net of
21 distributed generation and energy efficiency efforts. UNS Electric delivers energy over 334 miles of
22 transmission and sub-transmission lines and 3,650 miles of overhead and underground distribution
23 lines. UNS Electric’s total capital budget for the five year period 2014-2018 is estimated at \$252
24 million, which includes \$54.8 million for the proposed acquisition of a 25 percent interest in Gila
25 River in 2014.³

26 14. UNS Gas is a gas distribution company serving more than 147,000 retail customers in

27 ² On August 15, 2014, Fortis, Inc., a publically traded utility holding company, acquired UNS, and consequently is the
28 ultimate parent of UNS Electric, UNS Gas and their affiliate, Tucson Electric Power Company (“TEP”).

³ Staff Report Attachment A at 1-2.

1 Mohave, Yavapai, Coconino, Navajo, and Santa Cruz counties.⁴

2 15. The Companies currently have financing authority granted in Decision No. 71917
3 (October 12, 2010), which authority expires on December 31, 2014. Decision No. 71917 conditions
4 the Companies' authority to issue additional long-term debt (excluding debt issued under revolving
5 credit facilities and long-term debt being issued to refinance debt) upon the borrowing entity having
6 equity equal to at least 33 percent of its total capital and a Cash Coverage Ratio ("CCR") of at least
7 1.75 when equity is between 33 and 40 percent of total capital, or a CCR of at least 1.25 if equity is
8 40 percent or higher of total capital.⁵

9 **The Companies' Credit Agreement Request**

10 16. In Decision No. 71917, the Commission authorized UNS Electric and UNS Gas to
11 refinance or amend their joint revolving credit facility. The Companies state that the current credit
12 agreement dated November 9, 2010, as amended ("Credit Agreement"), consists of a \$100 million
13 joint revolving credit facility and expires in November 2016. UNS Electric and UNS Gas are each
14 authorized to borrow under the facility up to a maximum of \$70 million, however, the combined
15 amount borrowed cannot exceed \$100 million. The obligations of each borrower are several and not
16 joint, so neither company guarantees the obligations of the other. The credit facility is unsecured and
17 the obligations of each borrower are guaranteed by UES.⁶

18 17. The Companies use their revolving credit facilities as: (1) a source of liquidity for
19 working capital purposes; (2) to issue Letters of Credit ("LOCs") to provide credit enhancement to
20 counterparties for their energy procurement and hedging activities; and (3) for other lawful corporate
21 purposes.⁷

22 18. Borrowings under the credit facility bear interest at a variable interest rate consisting
23 of a spread over the London Interbank Offered Rate ("LIBOR") or an Alternate Base Rate (similar to
24 a prime rate). As of December 1, 2013, the applicable borrowing rate was LIBOR plus 1.25 percent
25 or Alternate Base Rate plus 0.25 percent. The Companies also pay a commitment fee of 0.20 percent

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27 ⁴ Application at 2.

⁵ Decision No. 71917 at 18.

⁶ Application at 3.

⁷ Application at 8.

1 on the unused portion of the revolving credit facility. As of December 1, 2013, UNS Electric had \$25
2 million in outstanding loans under the revolving credit facility and UNS Gas had no outstanding
3 loans under the revolving credit facility.⁸

4 19. The current credit facility has a sublimit for the issuance of LOCs. Up to \$50 million
5 of the total \$100 million credit facility may be used to issue LOCs to provide credit support for the
6 Companies' energy procurement and hedging activities. Fees are payable on the notional amount of
7 the outstanding LOCs. As of November 30, 2013, the applicable LOC fee was 1.25 percent. In
8 addition, the Companies pay an "LOC Fronting Fee" of 0.25 percent to the issuing banks. As of
9 December 1, 2013, UNS Electric had \$0.2 million of LOCs issued under the credit facility and UNS
10 Gas had no LOCs issued under the credit facility. The Credit Agreement is scheduled to expire on
11 November 9, 2016.

12 20. In order to meet their short-term liquidity needs, the Companies are seeking authority
13 to enter into one or more credit agreements, or refinance their existing credit agreements, such that
14 after giving effect of the entry of such a facility, the amount of credit available to each company,
15 individually, does not exceed \$100 million.⁹ They state the expanded capacity under such
16 agreement(s) will provide each with greater liquidity as they grow, including liquidity to support their
17 commodity procurement or hedging activities. They assert that the requested refinancing and
18 modifications to their credit agreements are necessary in order for them to continue to provide cost
19 effective, reliable and safe electric and gas distribution service.¹⁰ The Companies state that the term
20 and interest rate of any new Credit Agreement will depend on market conditions at the time the new
21 agreement or extension is executed, but that the term would not exceed five years.¹¹

22
23 ⁸ Application at 4.

24 ⁹ Thus, increasing the current limit of \$70 million applicable for each company. The Companies note in their Comments
25 on the Recommended Order (docketed December 8, 2014) that amounts borrowed under revolving credit agreements are
26 typically not required to be repaid until the date that the facility expires. For credit agreements with a term of more than
27 one year, this results in such borrowings being a form of long-term debt. For GAAP purposes, however, the Companies
28 state that borrowings for short-term liquidity needs are treated as short-term debt rather than long-term debt since the
borrower typically prepays such debt within twelve months rather than upon the expiration of the facility. For purposes of
Staff's financial analysis of the Companies' request, amounts borrowed under revolving credit agreements have been
considered as short-term debt, notwithstanding the fact that such amounts may usually be due more than twelve months
after they are borrowed.

¹⁰ Application at 4.

¹¹ Application at 5.

1 **The Companies' Long-term Debt Requests**

2 21. In Decision No. 70360 (May 27, 2008), the Commission authorized UNS Electric to
3 issue long-term debt to finance the purchase of the Black Mountain Generating Station; and in
4 Decision No. 71917, authorized UNS Electric to issue up to \$30 million in long-term debt for its
5 2010-2014 capital budget. UNS Electric has \$80 million of long-term debt which matures in 2015
6 and another \$50 million of long-term debt maturing in 2023. This Application is intended, *inter alia*,
7 to provide UNS Electric with the necessary authority to refinance the \$80 million of long-term debt
8 which matures in 2015.¹²

9 22. In Decision No. 71917, the Commission authorized UNS Gas to issue up to \$30
10 million in long-term debt. At the time of this Application, UNS Gas had \$50 million in senior notes
11 that mature in August 2015. UNS Gas states that this Application is intended to provide it with the
12 necessary authority to refinance these notes. UNS Gas also has \$50 million of long-term notes that
13 mature in August 2026.¹³

14 23. In addition to the refinancing of existing notes, and in light of their ongoing capital
15 expenditure needs, UNS Electric requests authority to issue up to \$80 million in additional long-term
16 debt, and UNS Gas requests authority to issue up to \$50 million of additional long-term debt.

17 24. The Companies state that the specific terms of any long-term debt to be issued under
18 the requested authority would depend on market conditions at the time of issuance, the credit ratings
19 of each company, and other factors such as the maturity dates of other outstanding indebtedness and
20 the mix of fixed and floating rate debt at each company. The Companies state that the new long-term
21 debt would be issued on either a fixed or floating rate basis, and the specific interest rates will depend
22 on market conditions at the time of issuance. Other variables to be determined at the time of issuance,
23 depending on market conditions, include the maturity date and whether the debt will be secured or
24 unsecured.¹⁴

25 25. UNS Electric and UNS Gas intend to use the proceeds from the issuance of new long
26 term debt to: (1) refinance existing long-term debt; (2) finance a portion of their respective capital

27 ¹² Application at 5.

28 ¹³ *Id.*

¹⁴ Application at 6.

1 expenditure program for the next five years; (3) pay down any outstanding borrowings under their
2 joint revolving credit facility; and (4) in the case of UNS Electric, finance a portion of the acquisition
3 of an interest in Gila River.

4 26. The Companies state that as of September 30, 2013, Moody's Investor Service has
5 rated the \$100 million of UNS Electric guaranteed senior notes, the \$100 million of UNS Gas
6 guaranteed senior notes, and the UNS Electric/UNS Gas revolving credit facility at Baa2.¹⁵

7 27. The Companies believe that the conditions contained in Decision No. 71917 affecting
8 the CCR and equity as a percentage of total capital were reasonable at that time, and that is it
9 reasonable and prudent to condition the issuance of additional long-term indebtedness (excluding
10 debt issued under the revolving credit facilities and long-term debt being issued to refinance debt)
11 upon such equity and cash coverage ratios.¹⁶

12 28. UNS Electric and UNS Gas believe that the amount of financing authority required in
13 this proceeding is in the public interest as reasonable, prudent and consistent with sound financial
14 practices and their duties as public service corporations, and will not diminish their financial
15 integrities.¹⁷

16 **Gila River Purchase Financing**

17 29. UNS Electric anticipates that it will have the opportunity to purchase a 25 percent
18 interest in Gila River Unit 3 as part of a purchase and sale agreement being negotiated between TEP,
19 UNS Electric and Gila River. UNS Electric expects the purchase transaction to close by the end of
20 2014. To finance the purchase and maintain a balanced capital structure, UNS Electric states that it
21 will need to use a mixture of debt and equity. UNS Electric seeks authority to issue up to \$35 million
22 of new debt (in addition to the \$80 million of new long-term debt discussed above), and to receive up
23 to \$35 million of additional equity contributions from its parent. UNS Electric states that the final
24 decision on which capital source to use will depend on the cost of debt at that time, as well as UNS
25 Electric's ability to maintain a reasonably balanced capital structure after the purchase is
26 consummated. UNS Electric emphasizes that it will not raise more than needed to complete the

27 ¹⁵ Application at 8.

28 ¹⁶ Application at 9-10.

¹⁷ Application at 10.

1 purchase.¹⁸

2 30. UNS Electric states that depending on market conditions, the debt could be either
3 long-term, short-term, or intermediate-term, and that in the latter cases, UNS Electric seeks authority
4 that would allow it to refinance any short- or intermediate-term debt with new long-term debt at a
5 later date prior to January 2020.¹⁹ UNS Electric requests flexibility to issue either long-, short- or
6 intermediate-term debt in order to take advantage of market conditions and to potentially realize
7 economies of scale by timing the issuance of new long-term debt to coincide with the refinancing of
8 the long-term debt maturing in 2015.²⁰

9 31. The terms of the new debt, whether long-, short-, or intermediate-term will depend on
10 market conditions at the time and on lenders' assessment of UNS Electric's creditworthiness. If it
11 were to issue long-term debt, UNS Electric expects that it would have a maturity between five and
12 thirty years, with the principal likely due in a single payment at maturity. UNS Electric states that the
13 debt may be issued in the public markets or in a private placement and may be issued in connection
14 with a refinancing of any short- or intermediate-term debt. In addition, the debt may be unsecured, or
15 secured by the assets being purchased, or secured on the same basis as other secured borrowings at
16 UNS Electric.²¹ If UNS Electric were to issue short- or intermediate-term debt it would have a
17 maturity between one month and five years, and interest would likely be at a variable rate, and
18 principal likely due in a single payment at maturity. As with the long-term debt, any short or
19 intermediate-term debt may be unsecured, secured with the assets being purchased, or secured on the
20 same basis as other secured borrowings at UNS Electric.

21 32. UNS Electric currently acquires several hundred megawatts of market purchases to
22 service its load. In its 2012 Integrated Resource Plan ("IRP"), UNS Electric stated that it would
23 monitor the market for economically-attractive plant acquisition opportunities. UNS Electric believes
24 that Gila River's capacity of 550 MW offers both TEP and UNS Electric an opportunity to meet the
25 short-term resource needs with the acquisition of a large scale generation asset. According to UNS

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27 ¹⁸ Application at 6-7.

¹⁹ Application at 7.

²⁰ Application at 7-8.

28 ²¹ Application at 7.

1 Electric, the 25 percent interest in Gila River gives it a needed base load and intermediate resource
 2 that fits its smaller load requirements at a clear and significant discount that will provide significant
 3 value to its customers.²²

4 33. Arizona Administrative Code (“A.A.C.”) R14-2-705(B)(5) requires load serving
 5 entities to use an RFP process to acquire wholesale energy and capacity unless the transaction is a
 6 “genuine unanticipated opportunity to acquire a power supply resource at a clear and significant
 7 discount, compared to the cost of acquiring new generating facilities, and will provide unique value
 8 to the load-serving entity’s customers.”

9 34. UNS Electric asserts that the Gila River purchase price of \$395/kW is a “clear and
 10 significant” discount to the cost of acquiring new generating facilities.²³ UNS Electric estimates the
 11 cost of a new combined cycle generating unit to be \$1,320/kW. UNS Electric’s analysis of the Gila
 12 River acquisition, compared to new construction, shows a savings of \$1,358 million in net present
 13 value revenue requirement over the 2015-2029 time frame, compared to operating a new combined
 14 cycle unit at an average capacity factor of 41.7 percent. In addition, UNS Electric states that the plant
 15 provides a unique value due to its ability to serve both UNS Electric’s Mohave and Santa Cruz
 16 operations due to synergies with TEP.

17 **Staff’s Engineering Review**
 18 **UNS Electric**

19 35. UNS Electric anticipates cumulative capital expenditures of \$190 million (exclusive of
 20 Gila River) for the periods 2013 to 2017.²⁴

21 36. Staff reviewed UNS Electric’s 2014-2018 capital budget to determine if it provides for
 22 reliable operation and maintenance of the electric system, and adequately addresses the needs of UNS
 23 Electric’s projected customer and load growth; and whether the capital expenditures on generation,
 24 transmission and distribution infrastructure are appropriate and reasonable.²⁵

25 37. UNS Electric experienced an annual average peak demand growth rate of
 26 approximately 1.2 percent per year over the period 2004-2013 and an annual average customer

27 ²² Staff Report Attachment A at 7-8, *citing* UNS Electric’s response to Staff Data Request 3.3.

²³ Staff Report Attachment A at 8.

²⁴ Application at 8.

28 ²⁵ Staff Report Engineering Report at 2.

1 growth rate of 1.8 percent for the same period. Staff states that UNS Electric's peak demand has
 2 been relatively flat from 2005 to 2013.²⁶ UNS Electric currently forecasts a moderate growth rate of
 3 0.5 percent per year over the 2013 actual peak of 427 MW for the period 2014-2018.

4 38. System reliability is measured by numerical indexes including: System Average
 5 Interruption Frequency Index ("SAIFI"), System Average Interruption Duration Index ("SAIDI"),
 6 Customer Average Interruption Duration Index ("CAIDI") and Momentary Average Interruption
 7 Frequency Index ("MAIFI"). The reliability indexes for UNS Electric from 2010 through 2013 are as
 8 follows:

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Average</u>
SAIFI	0.88	1.5	1.5	1.8	1.4
SAIDI (Minutes)	53.92	107.3	100.5	109.4	92.8
CAIDI (Minutes)	61.17	71.0	68.8	61.3	65.6

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13 39. Staff states that the indices show that over the last four years, the average customer
 14 experienced between one and two service outages per year (SAIFI) with an outage duration of about
 15 one hour to about one hour and 11 minutes (CAIDI). Staff notes that in UNS Electric's last rate case
 16 (Decision No. 74235) while Staff found that UNS Electric's three-year average values for 2010-2012
 17 showed above average reliability compared to similar utilities, concern was expressed about the
 18 upward trend in SAIDI and SAIFI. As a result, UNS Electric agreed to implement a procedure to
 19 target annual maintenance toward its worst performing circuits identified by service area and
 20 reliability indices, which Staff believes should help reverse the upward trend.

21 40. Staff's review of the installed cost of a new combined cycle power plant the size of
 22 Gila River resulted in estimates from \$950/kW to \$1,475/kW in 2014 dollars. Staff acknowledges
 23 that the \$398/kW price for Gila River is about 60 percent below the lowest estimate for a new plant
 24 identified by Staff.²⁷

25 ...

26 ...

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²⁶ *Id.*

28 ²⁷ Staff Report Attachment A at 8.

1 41. Based on its review of UNS Electric's capital budget, Staff concludes that:²⁸

2 (1) As indicated by its reliability indexes, UNS Electric is currently operating and
3 maintaining its electric system in a reliable manner.

4 (2) UNS Electric's capital budget appears to adequately address the needs of UNS
5 Electric's projected customer and load growth.

6 (3) UNS Electric's capital expenditures on its existing generation, and its
7 transmission and distribution infrastructure upgrades and new additions appear
8 appropriate and reasonable. Staff states that the cost of acquiring Gila River is
9 substantially below the cost of constructing a comparable new generating plant and
10 meets the needs for base load/intermediate capacity identified in UNS Electric's 2012
11 IRP.

12 (4) Based on Staff's review of UNS Electric's economic analysis and the need to
13 reduce its reliance on short-term market purchases, Staff concludes that the acquisition
14 of Gila River "appears reasonable." Staff expressed concern that UNS Electric did not
15 solicit long-term purchase power agreements, but Staff did not include a prudency
16 review as part of its review of this financing request. Staff states that this concern is
17 more appropriately addressed if and when UNS Electric seeks to recover the costs
18 associated with Gila River in rates. Staff states that UNS Electric should be aware that
19 Staff's review of any such future filing may include an evaluation of whether or not a
20 long-term power purchase agreement would have been a better alternative.

21 (5) Based on a review by the Commission's Utilities Compliance Section, UNS
22 Electric currently has no delinquent compliance items.

23 UNS Gas

24 42. UNS Gas serves over 150,000 natural gas customers in Santa Cruz, Mohave, Yavapai,
25 Coconino and Navajo Counties, which is an increase of over 3,800 over the last four years.²⁹

26 43. UNS Gas anticipates cumulative capital expenditures of \$72 million between 2013 and
27 2017.

28 44. Staff states that it has analyzed UNS Gas' capital budget, which provides monies for
infrastructure development, including new distribution mains and services, upgrades to the existing
systems and installation of new equipment such as measurement and pressure regulating stations.

45. Based on its review, Staff believes that UNS Gas' proposed capital expenditures are
appropriate to meet the projected needs of UNS Gas' existing and projected new customers and
ensure system reliability. Staff further concludes that the expenditure levels associated with the

²⁸ Staff Report at 4-5. Staff's conclusions do not imply any specific treatment of rate base for rate making purposes in any future rate filings.

²⁹ Supplemental Staff Report at 1.

1 projects proposed by the Company appear to be reasonable, but states that this does not imply a
2 specific treatment of rate base for rate making purposes in the Company's future rate filings.³⁰

3 **Staff's Financial Review**

4 **UNS Electric**

5 46. As of December 31, 2013, UNS Electric's capital structure consisted of short-term
6 debt totaling \$22.15 million, or 7.4 percent of total capital, long-term debt of \$130 million, or 43.7
7 percent of total capital, and equity of \$145.601 million, 48.9 percent of total capital.

8 47. According to Staff's financial analysis, if all amounts requested by UNS Electric were
9 to be fully executed, UNS Electric's short-term debt would increase to \$122.15 million, or 22.3
10 percent of total capital, its long-term debt would increase from \$130 million to \$245 million, or 44.7
11 percent of total capital, and its equity would increase from \$145.6 million to \$180.6 million, but
12 decrease to 33.0 percent of total capital.

13 48. In its Staff Report, Staff stated that it usually considers equity at 40 percent of total
14 capital as the minimum financially prudent capital structure for an investor-owned utility with access
15 to the capital markets. In its Staff Report, Staff expressed the belief that any general authorization for
16 UNS Electric to incur sort-term (revolver) debt or long-term debt within the thresholds as proposed
17 should be subject to the condition that, subsequent to any debt issuance, common equity represents no
18 less than 40 percent of total capital; and that UNS Electric should ascertain compliance with its ratio
19 requirements in its debt covenants and refrain from any transaction that would create a failure to
20 comply with those covenants.³¹

21 **UNS Gas**

22 49. As of December 31, 2013, UNS Gas' capital structure contained no short-term debt
23 and consisted of long-term debt totaling \$100 million, or 51.8 percent of total capital, and equity of
24 \$93.082 million, or 48.2 percent of total capital.

25 50. According to Staff, if the amounts requested to be authorized were to be fully drawn,
26 UNS Gas' capital structure would contain \$100 million of short term debt, or 29.1 percent of total

27 _____
28 ³⁰ Supplemental Staff Report.

³¹ Staff Report at 6.

1 capital, long-term debt would increase to \$150.0 million, or 43.7 percent of total capital, and its
2 equity would not change, but as a percentage of total capital would decrease to 27.1 percent.³²

3 51. In the Staff Report, Staff recommended that any general authorization for UNS Gas to
4 incur short-term (revolver) debt or long-term debt as proposed in this proceeding should be subject to
5 the condition that, subsequent to any debt issuance, common equity represents no less than 40 percent
6 of total capital. Staff also recommended that UNS Gas should ascertain compliance with its ratio
7 requirements and refrain from any transaction that would create a failure to comply with those
8 covenants.³³

9 **Staff's Recommendations (both Companies)**

10 52. The Companies' existing debt covenants include an Interest Earned Ratio ("ICR") that
11 is calculated differently than the Times Interest Earned Ratio ("TIER") that is commonly used by
12 Staff when evaluating requests for authority to incur debt. The debt instruments require a minimum
13 ICR of 2.50 and maximum debt as a percentage of total capital of 65 percent. The Companies expect
14 the new debt instruments will contain the same debt covenants as the existing instruments.

15 53. Staff calculates the pro forma ICR for UNS Electric to be 2.48 and the pro forma ICR
16 for UNS Gas to be 2.53 assuming that the Companies were to draw the full amount of the proposed
17 debt.³⁴

18 54. Staff recommended that any authority granted in this proceeding be conditioned upon
19 the Companies compliance with their debt covenants, including the ICR amounts. Staff further
20 recommends that any authority granted in this proceeding be conditioned upon the Companies'
21 compliance with the maximum debt percentage allowed therein, and that in the event that the
22 Companies' equity percentages fall below 40 percent, the Companies should file an equity
23 improvement plan with the Commission within 60 days.³⁵

24 55. In addition to the ratios required by their loan covenants, the Companies proposed to
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27 ³² Staff Report at 7 and Schedule GWB-2.

³³ Staff Report at 7.

³⁴ *Id.*

28 ³⁵ Staff Report at 8.

1 condition their authority to borrow on meeting a CCR of 1.75.³⁶ Staff believes that because it is not
 2 relevant to the loan covenants, a CCR requirement is unnecessary in this proceeding. However, Staff
 3 calculated a CCR assuming that the Companies draw the full amount of the proposed debt,
 4 determining that UNS Electric would have a CCR of 2.03, and UNS Gas would have a CCR of
 5 1.85.³⁷

6 56. In the Staff Report, Staff concluded that the issuance of the requested short-term and
 7 long-term debt (including credit facilities), is within the Companies' corporate powers, is compatible
 8 with the public interest, would not impair their ability to provide services and would be consistent
 9 with sound financial practices, subject to the following conclusions and conditions.³⁸

10
 11 (1) Authorize the Companies to refinance their joint revolving credit facility that
 expires in November 2016;

12 (2) Authorize the Companies to increase the amount of credit available under the
 13 revolving credit facilities to each company, individually, from \$70 million to \$100
 million.

14 (3) Authorize the Companies to refinance their long-term indebtedness maturing in
 15 August 2015.

16 (4) Authorize UNS Electric to increase the amount of long-term indebtedness
 17 outstanding by up to \$80 million, and authorizing UNS Gas to increase its long-term
 indebtedness by up to \$50 million.

18 (5) Authorize UNS Electric to finance the purchase of an interest in Gila River
 19 Unit 3 by issuing additional debt up to \$35 million and accepting new equity
 contributions from its parent in an amount up to \$35 million.

20 (6) Authorize the Companies to provide security for any such financing
 transactions.

21 (7) Authorize the Companies to enter into these financings through December 31,
 22 2019.

23 (8) Cancel all previously authorized but unused borrowing authority.

24 (9) Establish as a compliance item in this matter a requirement for the Companies
 25 to file with Docket Control, within 60 days of the execution of any financing
 transaction authorized herein, a notice confirming that such execution has occurred
 26 and a certification by an authorized officer that the terms of the financing fully comply
 with the granted authorizations.

27 ³⁶ CCR is the number of times internally generated cash covers required interest payments on short-term and long-term
 debt. A CCR greater than 1.0 means that operating cash flow is greater than interest expense.

28 ³⁷ Staff Report at 8.

³⁸ Staff Report at 8.

1 (10) Require the Companies to make available to Staff, upon request, a copy of any
2 loan documents executed pursuant to the authorization granted herein.

3 (11) Condition any authority granted herein upon the Companies having at least 40
4 percent equity and being in full compliance with their loan covenants including but not
5 limited to the required "Interest Earned Ratio" of 2.50.

6 (12) Require that in the event that either of the Companies' equity falls below 40
7 percent of total capital, the Company file an equity improvement plan with the
8 Commission within 60 days.

9 **The Companies' Position**

10 57. The Companies agreed with Staff's Recommendations 1, 2, 3, 6, 7, 9, 10 and 12;³⁹
11 proposed minor clarifications to Staff's Recommendations 4 and 5; and had significant concerns with
12 Staff Recommendations 8 and 11.

13 58. The Companies agreed with Staff Recommendation 4, but UNS Electric would like to
14 include language that clarifies that the \$80 million is in addition to the \$35 million of debt that could
15 be issued for the acquisition of Gila River.

16 59. The Companies agree with Staff Recommendation 5, however, UNS Electric would
17 like clarifying language to make clear that it could refinance the debt initially issued for the Gila
18 River purchase. The Companies assert that this addition is important because the initial Gila River
19 debt financing may be short- or intermediate-term which would likely be refinanced, and also, to
20 allow it to timely refinance long-term debt in order to reduce debt costs.⁴⁰

21 60. The Companies state that as proposed, Staff Recommendation 8 could have the
22 unintended effect of canceling the Companies' unused revolving credit capacity under the existing
23 revolving credit facility at the time the new financing order is issued.⁴¹ The Companies state that if
24 they cannot use their existing revolving credit facility, they would have to immediately arrange for
25 new credit facilities, but establishing a new credit facility would take several weeks and leave them
26 with insufficient liquidity in the interim. They state that arranging for a new credit facility is
27 unnecessary as their current facility, which was authorized in Decision No. 71917, does not expire
28 until November 2016.⁴²

³⁹ Comments at 2.

⁴⁰ Comments at 3.

⁴¹ *Id.*

⁴² The replacement for Staff Recommendation 8 is Condition 20 set forth in the Comments.

1 61. The Companies assert that as written, complying with the financial ratio tests in Staff
2 Recommendation 11 would restrict the Companies' ability to access their revolving credit facility
3 when needed. They believe that if these new ratio tests are adopted, there needs to be additional
4 ordering language (similar to that in the Companies' most recent previous financing order (Decision
5 No. 71917)) to specify how the ratios would be calculated.⁴³ The Companies state that this approach
6 has been adopted in the past and is still reasonable and prudent. They note further that the ordering
7 language in Decision No. 71917) specifically limited the financial ratio test to the issuance of new
8 long-term debt, and assert that financial ratio tests have not been previously required for revolving
9 credit loans, refinancing transaction, or contributions of parent company equity. Therefore, they seek
10 to clarify that only issuances of new long-term debt are subject to the equity ratio and interest
11 coverage tests. Furthermore, they state that as recognized in the Staff Report, the revolving credit
12 loans are already limited by financial covenants contained in their revolving credit agreements which
13 require that each Company limits its total debt to less than 65 percent of total capital, and thus, the
14 Companies cannot request revolving credit loans that would result in equity being lower than 35
15 percent.⁴⁴

16 62. The Comments contain 20 proposed ordering paragraphs that incorporate Staff's
17 recommendations as modified by the Companies' concerns. Staff agreed with the proposed
18 modifications. The Companies requested an Order from the Commission that includes the
19 following:⁴⁵

20 (1) Finding and concluding that approval of the Application is in the public
 interest;

21 (2) Authorizing UNS Electric and UNS Gas to enter into one or more credit
22 agreements with terms of up to five years, and to enter into agreements to refinance
23 any such credit or reimbursement agreements with new terms of up to five years,
24 which may consist of one or more revolving credit facilities so long as, after giving
effect to the entry of such a facility, the amount of credit available under such facilities
to each company, individually, does not exceed \$100 million;

25 (3) Authorizing UNS Electric and UNS Gas to issue long-term debt to refinance
long-term debt maturing in August 2015;

26 (4) Authorizing UNS Gas to issue up to \$50 million of additional long-term debt;

27 ⁴³ Comments at 3-4.

28 ⁴⁴ Comments at 3-4.

⁴⁵ Comments at Exhibit A.

1 (5) Authorizing UNS Electric to issue up to \$80 million of additional long-term
2 debt for purposes other than purchasing a share of Gila River;

3 (6) Authorizing UNS Electric to issue new debt up to \$35 million and accept new
4 equity contributions from its parent up to \$35 million, for the specific purpose of
5 purchasing a share of Gila River;

6 (7) Authorizing UNS Electric to issue long-term debt to refinance debt issued
7 under the authority set forth in (6) above;

8 (8) Authorizing UNS Electric and UNS Gas to provide security for any such
9 financing transactions;

10 (9) Conditioning the issuance of long-term indebtedness under the authority set
11 forth in (4), (5) and (6) above, upon: (i) the borrowing entity having equity equal to at
12 least 40 percent to total capital and (ii) the borrowing entity being in full compliance
13 with its debt covenants, including an ICR of at least 2.50 times;⁴⁶

14 (10) Condition any borrowing under a credit agreement authorized in (2) above
15 upon the borrowing entity being in full compliance with the covenants contained in
16 such agreement, which based upon the terms of the credit agreement in effect as of the
17 date of the Order, would be expected to contain a limitation on indebtedness that is
18 approximately equivalent to requiring equity equal to or greater than 35 percent of
19 total capital;

20 (11) Specifying that for purposes of the Order, the equity ratio and ICR shall be
21 determined on a pro forma basis after giving effect to the issuance of the long-term
22 debt to be issued pursuant to the authority and the discharge of any debt being
23 refunded or refinanced thereby (with the ICR calculation, in the case of indebtedness
24 bearing a floating interest rate, at the rate initially in effect on the date of issuance
25 thereof);

26 (12) Specifying that for purposes of the Order, the equity ratio shall be the ratio of
27 (a) common stock equity to (b) total capitalization, using the most recently audited
28 financial statements as adjusted for capital contributions, distributions, and issuances,
29 repayment or purchases of debt or equity occurring after the most recently audited
30 financial statements;

31 (13) Specifying that for purposes of the Order, the total capitalization shall be
32 defined as the sum of common stock equity, preferred stock, long-term debt (including
33 current maturities), short-term debt and capital lease obligations (including current
34 obligations under capital leases);

35 (14) Specifying that for purposes of the Order, the ICR for a Company shall be the
36 ratio of (a) Consolidated Net Income Available for Interest Charges for a period of
37 four consecutive fiscal quarters ending prior to that date of issuance to (b) Interest
38 Charges for the same four consecutive fiscal quarters, each as defined in such
39 Company's most recent long-term debt agreement as in effect on the date the Order is
40 issued;

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46 Staff agreed with the Companies' argument that the purpose of short-term borrowing requires greater flexibility, and that the requirement to maintain equity at or above 40 percent of total capitalization should appropriately apply to the issuance of new long-term debt. Joint Response at 1.

1 (15) Ordering that in the event that either Company's equity percentage falls below
2 40 percent, the Companies shall file an equity improvement plan with the Commission
3 within 60 days;

4 (16) Specifying that for purposes of this Order, any future changes in GAAP
5 [Generally Accepted Accounting Principles] that have the effect of lowering a
6 Company's equity will be exempted from the equity and interest coverage tests until
7 the Commission makes a determination. The Company shall make a filing with the
8 Commission requesting such a determination within 60 days following the end of the
9 fiscal quarter in which the GAAP change occurs;

10 (17) Establishing as a compliance item in this matter, a requirement for the
11 Companies to file with Docket Control, within 60 days of the execution of any
12 financing transaction authorized herein, a notice confirming that such execution has
13 occurred and a certification by an authorized officer that the terms of the financing
14 fully comply with the authorizations granted;

15 (18) Ordering the Companies to make available to Staff, upon request, a copy of
16 any loan documents executed pursuant to the authorization granted herein;

17 (19) Authorizing the execution, delivery and performance by UNS Electric and
18 UNS Gas of all contracts, agreements, and other instruments which are incidental to
19 any or all of the foregoing or otherwise deemed by UNS Electric and UNS Gas to be
20 necessary, desirable or appropriate in connection therewith;

21 (20) Ordering that the authorization to issue long-term debt, and to enter into one or
22 more credit agreements for revolving credit facilities in the Order shall replace the
23 existing authorization of Decision No. 71917, and that such authorization in Decision
24 No. 71917 terminate upon the effective date of the Order except that UNS Electric and
25 UNS Gas may continue to utilize their existing authorized agreements for revolving
26 credit facilities until the earlier of the execution of the new credit facilities authorized
27 herein of the expiration of the existing credit facility;⁴⁷

28 (21) Ordering that the Order be deemed effective upon issuance and that UNS
Electric and UNS Gas may enter into the transactions authorized under the Order
though December 31, 2019; and

(22) Granting any other relief that the Commission determines to be appropriate and
in the public interest at this time.

63. In response to the October 14, 2014 Procedural Order which sought clarification of the
parties' positions, the Companies and Staff proposed a modification of the proposed paragraph 2 as
follows:

Authorizing UNS Electric and UNS Gas to enter into one or more credit agreements
with terms of up to five years, and to enter into agreements to refinance any such
credit or reimbursement agreements with new terms of up to five years, which may
consist of one or more revolving credit facilities provided that : (1) after giving effect

⁴⁷ Modified pursuant to Joint Response and October 14, 2014 Procedural Order.

1 to the entry of such a facility, the amount of credit available under such facilities to
2 each company, individually, does not exceed \$100 million; (2) any borrowing under
3 the credit agreement(s) authorized herein shall be conditioned upon the borrowing
4 entity being in full compliance with the covenants contained in such agreement(s); and
5 (3) such facilities contain a debt to capitalization limit that is substantially the same as
6 the 65 percent limit contained in the existing credit facilities between UNS Electric or
7 UNS Gas and their lenders.

8 64. The parties state that the revised paragraph 2 now effectively incorporates the current
9 equity ratio in the future credit facilities and its adoption would make paragraph 10 no longer
10 necessary. The parties explain that the revolving facilities are needed to provide immediate liquidity,
11 and as modified, paragraph 2 does not have the impact of adding undue additional constraints on
12 individual borrowings under the facilities that may have the unfortunate consequence of prohibiting
13 access to liquidity when such access is most critical to the Company. The parties assert that if
14 additional tests beyond the terms of the credit facilities are added for each draw under the facility, the
15 validity of each loan request may be subject to question by the bank. They assert that the reporting
16 requirement of paragraph 15 provides comfort that the Companies will not over-extend themselves by
17 use of other revolving credit facilities.

18 Conclusion

19 65. The Application, with the addition of the conditions as set forth in the Comments and
20 Joint Response, is reasonable and in the public interest, as it appropriately balances the Companies'
21 need to access the debt market to finance needed capital improvements (and acquisition of a low cost
22 generation source) and obtain a revolving line of credit to assist in daily operations with the
23 Commission's duty under A.R.S. §§40-301 and 40-302 to protect ratepayers from imprudent
24 financial transactions.

25 CONCLUSIONS OF LAW

26 1. The Companies are public service corporations within the meaning of Article XV of
27 the Arizona Constitution and A.R.S. §§ 40-285, 40-301, 40-302, and 40-303.

28 2. The Commission has jurisdiction over UNS Electric and UNS Gas and of the subject

1 matter of the Application.

2 3. Notice of the Application was given in accordance with the law.

3 4. The authorizations granted herein are for lawful purposes which are within the
4 corporate powers of the Companies, are compatible with the public interest, with sound financial
5 practices, and with the proper performance by the Companies of service as public service
6 corporations, and will not impair the Companies' ability to perform that service.

7 5. The financing approved herein is for the purposes stated in the Application, is
8 reasonably necessary for those purposes, and except for certain uses of the revolving credit facilities,
9 such purposes are not reasonably chargeable to operating expenses or to income.

10 **ORDER**

11 IT IS THEREFORE ORDERED that UNS Electric, Inc. and UNS Gas, Inc. are hereby
12 authorized to enter into one or more credit agreements with terms up to five years, and to enter into
13 agreements to refinance any such credit or reimbursement agreement with new terms of up to five
14 years, which may consist of one or more revolving credit facilities provided that: (1) after giving
15 effect to the entry of such a facility, the amount of credit available under such facilities to each
16 company, individually, does not exceed \$100 million; (2) any borrowing under the credit
17 agreement(s) authorized herein shall be conditioned upon the borrowing entity being in full
18 compliance with the covenants contained in such agreement(s); and (3) such facilities contain a debt
19 to capitalization limit that is substantially the same as the 65 percent limit contained in the existing
20 credit facilities between UNS Electric, Inc. or UNS Gas, Inc. and their lenders.

21 IT IS FURTHER ORDERED that UNS Electric, Inc. and UNS Gas, Inc. are hereby
22 authorized to issue long-term debt to refinance long-term debt maturing in August 2015.

23 IT IS FURTHER ORDERED that UNS Gas, Inc. is hereby authorized to issue up to \$50
24 million of additional long-term debt.

25 IT IS FURTHER ORDERED that UNS Electric, Inc. is hereby authorized to issue up to \$80
26 million of additional long-term debt for purposes other than purchasing a share of Gila River Unit 3.

27 IT IS FURTHER ORDERED that UNS Electric, Inc. is hereby authorized to issue new debt
28 up to \$35 million and accept new equity contributions from its parent up to \$35 million, for the

1 specific purpose of purchasing a share of Gila River Unit 3, and is further authorized to issue long-
2 term debt to refinance the debt initially issued for the purchase of its share of Gila River Unit 3.

3 IT IS FURTHER ORDERED that UNS Electric, Inc. and UNS Gas, Inc. are authorized to
4 provide security for any such financing authority granted herein.

5 IT IS FURTHER ORDERED that UNS Gas, Inc.'s authority to issue new long-term debt in
6 the amount of \$50 million, UNS Electric, Inc.'s authority to issue new long-term debt up to \$80
7 million and UNS Electric, Inc.'s new long term debt of up to \$35 million for the purchase of Gila
8 River Unit 3 granted herein above are conditioned on: (1) the borrowing entity having equity equal to
9 at least 40 percent of total capital; and (2) the borrowing entity being in full compliance with its debt
10 covenants, including an Interest Coverage Ratio of at least 2.50 times.

11 IT IS FURTHER ORDERED that for purposes of this Order, the equity ratio and Interest
12 Coverage Ratio shall be determined on a pro forma basis after giving effect to the issuance of the
13 long-term debt to be issued pursuant to the authority and the discharge of any debt being refunded or
14 refinanced thereby, with the Interest Coverage Ratio calculated, in the case of indebtedness bearing a
15 floating rate of interest, at the rate initially in effect on the date of issuance thereof.

16 IT IS FURTHER ORDERED that for purposes of this Order, the equity ratio shall be the ratio
17 of (a) common stock equity to (b) total capitalization, using the most recent audited financial
18 statements as adjusted for capital contributions, distributions, and issuances, repayment or purchases
19 of debt or equity occurring after the most recently audited financial statements; and that for purposes
20 of this Order, total capitalization shall be defined as the sum of common stock equity, preferred stock,
21 long-term debt (including current maturities), short-term debt and capital lease obligations (including
22 current obligations under capital leases).

23 IT IS FURTHER ORDERED that for purposes of this Order, the Interest Coverage Ratio for a
24 borrowing entity shall be the ratio of (a) Consolidated Net Income Available for Interest Charges for
25 a period of four consecutive fiscal quarters ending prior to that date of issuance to (b) Interest
26 Charges for the same four consecutive fiscal quarters, each as defined in such Company's most recent
27 long-term debt agreement as in effect on the effective date of this Order.

28 ...

1 IT IS FURTHER ORDERED that in the event either UNS Electric, Inc.'s or UNS Gas, Inc.'s
2 equity ratio falls below 40 percent of total capitalization, the affected entity shall file an equity
3 improvement plan with the Commission within 60 days.

4 IT IS FURTHER ORDERED that for purposes of this Order, any future changes in GAAP
5 that have the effect of lowering either UNS Electric, Inc.'s or UNS Gas, Inc.'s equity will be exempt
6 from the equity and interest coverage tests until the Commission makes a determination, and the
7 affected company shall make a filing with the Commission requesting such a determination within 60
8 days following the end of the fiscal quarter in which the GAAP change occurs.

9 IT IS FURTHER ORDERED that UNS Electric, Inc. and UNS Gas, Inc. shall file with
10 Docket Control, as a compliance item in this docket, a notice confirming that the execution of any
11 financing transaction authorized herein, within 60 days of the execution, which notice shall contain
12 certification by an authorized officer that the terms of the financing fully comply with the
13 authorizations granted herein.

14 IT IS FURTHER ORDERED that UNS Electric, Inc. and UNS Gas, Inc. shall make available
15 to Staff, upon request, a copy of any loan documents executed pursuant to the authorizations granted
16 herein.

17 IT IS FURTHER ORDERED that UNS Electric, Inc. and UNS Gas, Inc. may engage in any
18 transaction and/or to execute and deliver any documents necessary to effectuate the authorizations
19 granted herein.

20 IT IS FURTHER ORDERED that the authorization granted herein to issue long-term debt,
21 and to enter into one or more credit agreements for revolving credit facilities replaces the existing
22 authorization granted in Decision No. 71917, and the authorization granted in Decision No. 71917
23 shall terminate upon the effective date of this Order, except that UNS Electric, Inc. and UNS Gas,
24 Inc. may continue to utilize their existing authorized agreements for revolving credit facilities until
25 the earlier of the execution of the new credit facilities authorized herein or the expiration of the
26 existing credit facility

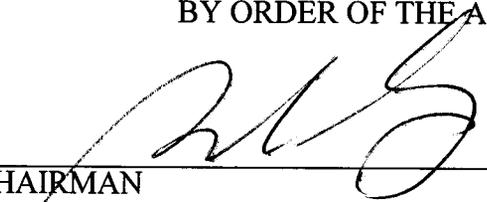
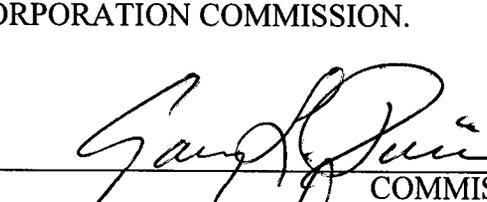
27 IT IS FURTHER ORDERED that the authority granted herein shall terminate December 31,
28 2019.

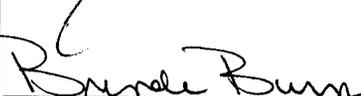
1 IT IS FURTHER ORDERED that the finance authority granted herein is expressly contingent
2 upon UNS Electric, Inc.'s and UNS Gas, Inc.'s use of the proceeds for the purposes stated in the
3 Application and approved herein.

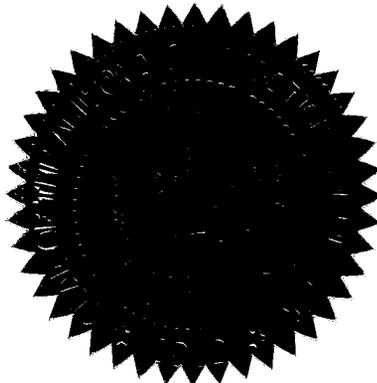
4 IT IS FURTHER ORDERED that approval of the financing set forth herein does not
5 constitute or imply approval or disapproval by the Commission of any particular expenditure of the
6 proceeds derived thereby, including the purchase of the interest in Gila River Unit 3, for purposes of
7 establishing just and reasonable rates.

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

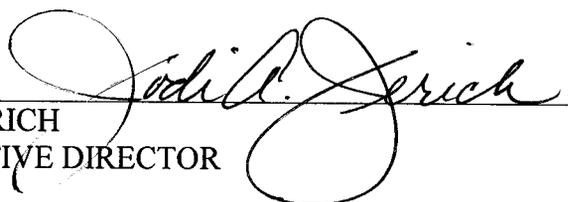
9 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

10
11  
12 CHAIRMAN COMMISSIONER

13   
14 COMMISSIONER COMMISSIONER COMMISSIONER



15 IN WITNESS WHEREOF, I, JODI JERICH, Executive
16 Director of the Arizona Corporation Commission, have
17 hereunto set my hand and caused the official seal of the
18 Commission to be affixed at the Capitol, in the City of Phoenix,
19 this 18th day of December 2014.

20 
21 JODI JERICH
22 EXECUTIVE DIRECTOR

23 DISSENT _____

24 DISSENT _____
25 JR:ru

1 SERVICE LIST FOR: UNS ELECTRIC, INC. and UNS GAS, INC.

2 DOCKET NOS.: E-04204A-13-0447 and G-04204A-13-0447

3 Bradley S. Carroll
4 UNS Energy Services
5 Legal Department – MS HQE 910
6 PO Box 711
7 Tucson, AZ 85702

8 Mr. Michael Patten
9 Roshka De Wulf & Patten, PLC
10 One Arizona Center
11 400 East Van Buren Street, Suite 800
12 Phoenix, AZ 85004
13 Attorneys for UNS Electric, Inc. and UNS Gas, Inc.

14 Janice Alward, Chief Counsel
15 Legal Division
16 ARIZONA CORPORATION COMMISSION
17 1200 West Washington Street
18 Phoenix, AZ 85007

19 Steven M. Olea, Director
20 Utilities Division
21 ARIZONA CORPORATION COMMISSION
22 1200 West Washington Street
23 Phoenix, AZ 85007

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25
26
27
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