

OPEN MEETING



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MEMORANDUM

Arizona Corporation Commission

TO: THE COMMISSION

DOCKETED

FROM: Utilities Division

FEB 13 2015

DATE: February 13, 2015

DOCKETED BY

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2015 FEB 13 P 3:55

AZ CORP COMMISSION
DOCKET CONTROL

RE: IN THE MATTER OF THE APPLICATION OF ARIZONA PUBLIC SERVICE COMPANY TO SELL TRANSMISSION ASSETS TO SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT (DOCKET NO. E-01345A-14-0272)

ORIGINAL

INTRODUCTION

On July 17, 2014, Arizona Public Service Company ("APS") submitted an application to the Arizona Corporation Commission ("Commission") pursuant to Arizona Revised Statutes ("A.R.S.") §40-285 for authorization to sell a 50% interest in two existing APS transmission lines to Salt River Project Agricultural Improvement and Power District ("SRP") for a total price of \$9.9 million.¹ The assets to be sold include a one-half undivided interest in two transmission lines between the Kyrene and Knox substations, as well as associated facilities and land rights as described in Attachment A to APS's application and repeated below:

The purchased assets comprise of (a) a one-half undivided interest in the Kyrene-Knox Line, including a one-half undivided interest in associated equipment, facilities, fixtures, real and personal property, land rights including without limitation pertinent land grants, easements and licenses, permits, rights and contracts to own, operate and maintain said line; and (b) a one-half undivided interest in that portion of the existing Kyrene-Ocotillo Line that runs between Kyrene Substation and the turning tower on the Kyrene-Knox Line at the Knox Substation and a one-half undivided interest in associated equipment, facilities, fixtures, real and personal property, land rights including without limitation pertinent land grants, easements and licenses, permits, rights and contracts to own, operate and maintain said line.

APPLICATION

As explained in APS's application, APS and SRP are currently parties to a transmission service agreement under which SRP takes point-to-point transmission service on the Kyrene-Knox line under APS's Open Access Transmission Tariff ("OATT"). SRP's transmission service continues from the Knox Substation to the Desert Basin Substation. Under the current agreement, SRP takes 148 megawatts ("MW") of transmission service and pays approximately \$7 million to APS

¹ A.R.S. §40-285 requires public service corporations wishing to sell, lease, assign, mortgage, or otherwise dispose of or encumber plant or other property necessary or useful in the performance of its duties to the public, to first obtain authorization from the Commission. This statute serves to preempt any service impairment due to the disposal of assets that are essential for providing service.

per year for this capacity. SRP has the right to terminate the agreement should SRP acquire its own transmission line between the Kyrene and Knox substations. The agreement is set to expire in May 2016.

APS understands that SRP is pursuing a transmission project that includes SRP owning its own transmission line between Kyrene and Knox substations by June 2016 instead of continuing to take service from APS under the transmission service agreement. To meet the need of owning its own transmission line, SRP has two options: build a new 230 kV line or buy a portion of one or both of APS's existing 230 kV transmission lines between the Knox and Kyrene substations. If SRP pursued the first option and built a new 230 kV transmission line, SRP would encounter expense and other challenges associated with siting and constructing a new line in the middle of a populated area. But, if SRP builds its own line, SRP would terminate its transmission agreement with APS as permitted by the parties' current agreement. Thereafter, APS would continue to own and maintain 100% of the line and incur 100% of the costs of ownership and maintenance, but would no longer receive the transmission revenue from SRP.

The second option, SRP buying a portion of APS's existing lines, addresses both sets of challenges. Under the second option, SRP would buy 50% of the Kyrene-Knox Line and 50% of the Kyrene-Knox Segment. SRP would still cancel its current transmission service agreement with APS, and APS would still lose the resulting transmission revenue from SRP. APS would also avoid, however, the operations and maintenance expense associated with the sold assets as well as capital carrying costs associated with the sold portion of the line. Because APS will lose the transmission revenue under any option, the sale to SRP offers the best outcome for both parties. SRP will avoid the expense and possible disruption to the public associated with constructing a new line and APS will be able to allocate a portion of the operations and maintenance and other cost obligations to SRP.

Under the proposed transaction, APS would sell to SRP (i) 50% of the Kyrene-Knox Line, (ii) 50% of the Kyrene-Knox Segment, and (iii) the facilities, equipment and land rights associated with each 50% share described in Attachment A of the application. Under the proposed sale, SRP would pay APS \$9.9 million for the 50% share in each of the two transmission lines. SRP would continue taking transmission service on the Kyrene-Knox Line until the estimated transaction closing date of May 2016. Upon closing, SRP would assume a 50% ownership in both transmission lines, as well as a 50% responsibility for operations and maintenance costs associated with the Kyrene-Knox Line. When SRP completes the loop of the Kyrene-Knox Segment into the Knox Substation and begins using the Kyrene-Knox Segment, it will begin paying for 50% of the operations and maintenance costs associated with the Segment. As required by Federal Energy Regulatory Commission ("FERC") regulations, proceeds from the sale of the Transmission Assets will be cleared through FERC Account 102 - Electric Plant Purchased or Sold with the gain on the sale of assets being recorded in FERC Account 421.1 - Gain on Disposition of Property.

APS states in its application that selling a 50% portion of the two transmission lines in question would not impair APS's ability to serve the public, as 148 MW of the Kyrene-Knox Line is

already being used to serve SRP as a transmission customer of APS. After the sale, APS would still retain 50% ownership of both transmission lines, which APS states provides an amount of transmission capacity more than sufficient to meet APS's current and projected transmission needs without jeopardizing electric reliability to its customers.

STAFF REVIEW AND RECOMMENDATIONS

Staff's review focused on three areas: a) would the sale of the transmission assets negatively impact the ability of APS to reliably serve its customers, b) is the negotiated sale price reasonable, and c) will the revenues above the current book value from the sale reduce APS's transmission rate base, and therefore its transmission rates, which would ultimately reduce APS's Transmission Cost Adjustor ("TCA").

With respect to the impact on APS's ability to reliably serve its customers, based upon APS's responses to data requests, Staff found that APS uses scheduled capacity of up to 741 MW from the Kyrene Substation. The total rated capacity of the Kyrene-Knox and Kyrene-Ocotillo lines is 1,908 MW, of which APS would retain 50% of that capability or 954 MW, which exceeds APS current scheduling needs. In addition, APS provided 2023 power flow results that showed the project's flow on the two lines would not exceed APS's scheduled capacity of 741 MW. Staff believes this demonstrates that APS will continue to have adequate capacity on the Kyrene-Knox and Kyrene-Ocotillo lines to reliably serve its customers.

APS stated in a response to a Staff data request that the \$9.9 million dollar sale price was negotiated and derives from APS's analysis of the cost to build two recent APS transmission projects and SRP's estimate of what it would cost for SRP to build its own line. Staff understands that SRP's plan for building its own line would be accomplished by rebuilding the existing Jojoba-Kyrene 500 kV line to add a 230 kV double circuit line between the Knox Substation and Kyrene Substation. The line would be approximately 4.5 miles in length. Staff compared the sale price to the cost of a new Greenfield, 4.5 mile, 230 kV double circuit line constructed in an urban area using the transmission cost estimator used by the Western Electricity Coordinating Council ("WECC") in its transmission planning activities. The cost using the estimator is \$9.7 million which would not take into account project specific considerations such as: a) SRP would be building on an existing right-of-way and; b) SRP would be building on the shared structures with the Jojoba-Kyrene 500 kV line. Staff agrees the \$9.9 million sale price is reasonable.

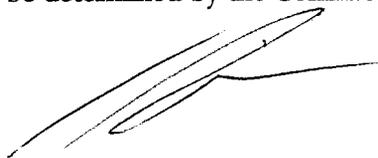
Staff requested that APS provide information regarding the accounting entries it would use to account for the sale of the assets. APS indicated that following this transaction, there would be a reduction in electric plant in-service which would reduce rate base in APS's transmission formula rate, therefore reducing the rate.

In Decision No. 69670, dated June 28, 2007, the Commission granted APS pre-approval of certain property transactions pursuant to A.R.S. §40-285 subject to conditions and limitations specified in that Decision. Among other requirements, Decision No. 69670 required that 50% of the net gain on pre-approved transactions be credited to APS ratepayers. Although this transaction does not meet the explicit criteria for a pre-approved transaction as specified in Decision No. 69670,

Staff believes that the same principal surrounding the sharing of net gain proceeds applied to pre-approved transactions should apply to this transaction.

Based on information provided by APS, 50% of the net gain on the sale of assets from this transaction that would be credited to ratepayers is approximately \$4.68 million. Staff believes that the ratepayers' portion of the net gain on the sale of assets from this transaction should be refunded to ratepayers by placing the total ratepayers' portion of the net gain into an interest bearing deferral account until APS's next rate case.

Staff therefore recommends approval of the proposed transaction, as discussed herein. In addition, Staff recommends that 50% of the net gain on the sale of assets from this transaction should be refunded to ratepayers by placing the total ratepayers' portion of the net gain into an interest-bearing deferral account until APS's next rate case. The method of refund/sharing should be determined by the Commission in the next rate case.



Steven M. Olea
Director
Utilities Division

SMO:CLA:sms\RWG

ORIGINATOR: Candrea Allen and Ray Williamson

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BEFORE THE ARIZONA CORPORATION COMMISSION

- SUSAN BITTER SMITH
Chairman
- BOB STUMP
Commissioner
- BOB BURNS
Commissioner
- DOUG LITTLE
Commissioner
- TOM FORESE
Commissioner

IN THE MATTER OF THE APPLICATION)
 OF ARIZONA PUBLIC SERVICE)
 COMPANY FOR APPROVAL TO SELL)
 TRANSMISSION ASSETS TO SALT RIVER)
 PROJECT AGRICULTURAL)
 IMPROVEMENT AND POWER DISTRICT)

DOCKET NO. E-01345A-14-0272
 DECISION NO. _____
ORDER

Open Meeting
 March 2 and 3, 2015
 Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Arizona Public Service Company ("APS" or "Company") is certificated to provide electric service within portions of Arizona, pursuant to authority granted by the Arizona Corporation Commission ("Commission").

INTRODUCTION

2. On July 17, 2014, APS submitted an application to the Commission pursuant to Arizona Revised Statutes ("A.R.S.") §40-285 for authorization to sell a 50% interest in two existing APS transmission lines to Salt River Project Agricultural Improvement and Power District ("SRP") for a total price of \$9.9 million.¹ The assets to be sold include a one-half undivided interest in two

¹ A.R.S. §40-285 requires public service corporations wishing to sell, lease, assign, mortgage, or otherwise dispose of or encumber plant or other property necessary or useful in the performance of its duties to the public, to first obtain authorization from the Commission. This statute serves to preempt any service impairment due to the disposal of assets that are essential for providing service.

1 transmission lines between the Kyrene and Knox substations, as well as associated facilities and land
2 rights as described in Attachment A to APS's application and repeated below:

3 The purchased assets comprise of (a) a one-half undivided interest in the
4 Kyrene-Knox Line, including a one-half undivided interest in associated
5 equipment, facilities, fixtures, real and personal property, land rights including
6 without limitation pertinent land grants, easements and licenses, permits, rights
7 and contracts to own, operate and maintain said line; and (b) a one-half
8 undivided interest in that portion of the existing Kyrene-Ocotillo Line that
9 runs between Kyrene Substation and the turning tower on the Kyrene-Knox
10 Line at the Knox Substation and a one-half undivided interest in associated
11 equipment, facilities, fixtures, real and personal property, land rights including
12 without limitation pertinent land grants, easements and licenses, permits, rights
13 and contracts to own, operate and maintain said line.

9 APPLICATION

10 3. As explained in APS's application, APS and SRP are currently parties to a transmission
11 service agreement under which SRP takes point-to-point transmission service on the Kyrene-Knox
12 line under APS's Open Access Transmission Tariff ("OATT"). SRP's transmission service continues
13 from the Knox Substation to the Desert Basin Substation. Under the current agreement, SRP takes
14 148 megawatts ("MW") of transmission service and pays approximately \$7 million to APS per year for
15 this capacity. SRP has the right to terminate the agreement should SRP acquire its own transmission
16 line between the Kyrene and Knox substations. The agreement is set to expire in May 2016.

17 4. APS understands that SRP is pursuing a transmission project that includes SRP
18 owning its own transmission line between Kyrene and Knox substations by June 2016 instead of
19 continuing to take service from APS under the transmission service agreement. To meet the need of
20 owning its own transmission line, SRP has two options: build a new 230 kV line or buy a portion of
21 one or both of APS's existing 230 kV transmission lines between the Knox and Kyrene substations. If
22 SRP pursued the first option and built a new 230 kV transmission line, SRP would encounter expense
23 and other challenges associated with siting and constructing a new line in the middle of a populated
24 area. But, if SRP builds its own line, SRP would terminate its transmission agreement with APS as
25 permitted by the parties' current agreement. Thereafter, APS would continue to own and maintain
26 100% of the line and incur 100% of the costs of ownership and maintenance, but would no longer
27 receive the transmission revenue from SRP.

28 ...

1 5. The second option, SRP buying a portion of APS's existing lines, addresses both sets
2 of challenges. Under the second option, SRP would buy 50% of the Kyrene-Knox Line and 50% of
3 the Kyrene-Knox Segment. SRP would still cancel its current transmission service agreement with
4 APS, and APS would still lose the resulting transmission revenue from SRP. APS would also avoid,
5 however, the operations and maintenance expense associated with the sold assets as well as capital
6 carrying costs associated with the sold portion of the line. Because APS will lose the transmission
7 revenue under any option, the sale to SRP offers the best outcome for both parties. SRP will avoid the
8 expense and possible disruption to the public associated with constructing a new line and APS will be
9 able to allocate a portion of the operations and maintenance and other cost obligations to SRP.

10 6. Under the proposed transaction, APS would sell to SRP (i) 50% of the Kyrene-Knox
11 Line, (ii) 50% of the Kyrene-Knox Segment, and (iii) the facilities, equipment and land rights
12 associated with each 50% share described in Attachment A of the application. Under the proposed
13 sale, SRP would pay APS \$9.9 million for the 50% share in each of the two transmission lines. SRP
14 would continue taking transmission service on the Kyrene-Knox Line until the estimated transaction
15 closing date of May 2016. Upon closing, SRP would assume a 50% ownership in both transmission
16 lines, as well as a 50% responsibility for operations and maintenance costs associated with the Kyrene-
17 Knox Line.

18 7. When SRP completes the loop of the Kyrene-Knox Segment into the Knox Substation
19 and begins using the Kyrene-Knox Segment, it will begin paying for 50% of the operations and
20 maintenance costs associated with the Segment. As required by Federal Energy Regulatory
21 Commission ("FERC") regulations, proceeds from the sale of the Transmission Assets will be cleared
22 through FERC Account 102 - Electric Plant Purchased or Sold with the gain on the sale of assets
23 being recorded in FERC Account 421.1 - Gain on Disposition of Property.

24 8. APS states in its application that selling a 50% portion of the two transmission lines in
25 question would not impair APS's ability to serve the public, as 148 MW of the Kyrene-Knox Line is
26 already being used to serve SRP as a transmission customer of APS. After the sale, APS would still
27 retain 50% ownership of both transmission lines, which APS states provides an amount of

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1 transmission capacity more than sufficient to meet APS's current and projected transmission needs
2 without jeopardizing electric reliability to its customers.

3 **STAFF REVIEW AND RECOMMENDATIONS**

4 9. Staff's review focused on three areas: a) would the sale of the transmission assets
5 negatively impact the ability of APS to reliably serve its customers, b) is the negotiated sale price
6 reasonable, and c) will the revenues above the current book value from the sale reduce APS's
7 transmission rate base, and therefore its transmission rates, which would ultimately reduce APS's
8 Transmission Cost Adjustor ("TCA").

9 10. With respect to the impact on APS's ability to reliably serve its customers, based upon
10 APS's responses to data requests, Staff found that APS uses scheduled capacity of up to 741 MW
11 from the Kyrene Substation. The total rated capacity of the Kyrene-Knox and Kyrene-Ocotillo lines
12 is 1,908 MW, of which APS would retain 50% of that capability or 954 MW, which exceeds APS
13 current scheduling needs. In addition, APS provided 2023 power flow results that showed the
14 project's flow on the two lines would not exceed APS's scheduled capacity of 741 MW. Staff believes
15 this demonstrates that APS will continue to have adequate capacity on the Kyrene-Knox and Kyrene-
16 Ocotillo lines to reliably serve its customers.

17 11. APS stated in a response to a Staff data request that the \$9.9 million dollar sale price
18 was negotiated and derives from APS's analysis of the cost to build two recent APS transmission
19 projects and SRP's estimate of what it would cost for SRP to build its own line. Staff understands that
20 SRP's plan for building its own line would be accomplished by rebuilding the existing Jojoba-Kyrene
21 500 kV line to add a 230 kV double circuit line between the Knox Substation and Kyrene Substation.
22 The line would be approximately 4.5 miles in length.

23 12. Staff compared the sale price to the cost of a new Greenfield, 4.5 mile, 230 kV double
24 circuit line constructed in an urban area using the transmission cost estimator used by the Western
25 Electricity Coordinating Council ("WECC") in its transmission planning activities. The cost using the
26 estimator is \$9.7 million which would not take into account project specific considerations such as: a)
27 SRP would be building on an existing right-of-way and; b) would be building on the shared structures
28 with the Jojoba-Kyrene 500 kV line. Staff agrees the \$9.9 million sale price is reasonable.

1 Company's request to sell transmission assets to Salt River Project Agricultural Improvement and
2 Power District as discussed herein.

3 ORDER

4 IT IS THEREFORE ORDERED that the Arizona Public Service Company application to sell
5 transmission assets to Salt River Project Agricultural Improvement and Power District be and hereby
6 is approved as discussed herein.

7 IT IS FURTHER ORDERED that fifty percent of the net gain on the sale of assets from this
8 transaction shall be refunded to ratepayers in a manner to be determined by the Commission in
9 Arizona Public Service Company's next rate case, by placing the total ratepayers' portion of the net
10 gain into an interest-bearing deferral account until Arizona Public Service Company's next rate case.

11 IT IS FURTHER ORDERED that this Order shall become effective immediately.

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

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15 CHAIRMAN

COMMISSIONER

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17 COMMISSIONER

COMMISSIONER

COMMISSIONER

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19 IN WITNESS WHEREOF, I, JODI JERICH, Executive
20 Director of the Arizona Corporation Commission, have
21 hereunto, set my hand and caused the official seal of this
22 Commission to be affixed at the Capitol, in the City of
23 Phoenix, this _____ day of _____, 2015.

24 _____
JODI JERICH
EXECUTIVE DIRECTOR

25
26 DISSENT: _____

27 DISSENT: _____

28 SMO:CLA:sms\RWG

Decision No. _____

1 SERVICE LIST FOR: Arizona Public Service Company
2 DOCKET NO.: E-01345A-14-0272

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