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OPEN MEETING ITEM

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ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
DOCKET CONTROL

DATE: NOVEMBER 23, 2015

DOCKET NO.: E-01773A-12-0305

TO ALL PARTIES:

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

ARIZONA ELECTRIC POWER COOPERATIVE, INC.
(APPROVING ECAR MECHANISM)

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:

DECEMBER 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:

DECEMBER 8, 2015 and DECEMBER 9, 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
NOV 23 2015
DOCKETED BY

JODI JERICH
EXECUTIVE DIRECTOR

This document is available in alternative formats by contacting Shaylin Bernal, ADA Coordinator, voice phone number 602-542-3931, E-mail SABernal@azcc.gov.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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

IN THE MATTER OF THE APPLICATION OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. FOR A HEARING TO DETERMINE THE FAIR VALUE OF ITS PROPERTY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RETURN THEREON AND TO APPROVE RATES DESIGNED TO DEVELOP SUCH RETURN.	DOCKET NO. E-01773A-12-0305 DECISION NO. _____ **OPINION AND ORDER** (Approving ECAR Mechanism)

DATES OF HEARING:	February 20 and August 5, 2015 (Procedural Conferences); August 24, 2015 (Public Comment); October 2, 2015 (Pre-Hearing Conference); October 7, 2015.
PLACE OF HEARING:	Phoenix, Arizona
ADMINISTRATIVE LAW JUDGE:	Teena Jibilian
APPEARANCES:	Ms. Jennifer Cranston, GALLAGHER & KENNEDY, on behalf of Applicant; Mr. William P. Sullivan, CURTIS, GOODWIN, SULLIVAN, UDALL & SCHWAB, on behalf of Mohave Electric Cooperative, Inc. and Navopache Cooperative; Mr. Michael W. Patten, SNELL & WILMER, LLP, on behalf of Trico Electric Cooperative, Inc., and Ms. Bridget Humphrey, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

* * * * * * * * * *

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

FINDINGS OF FACT

Procedural History

1. On July 5, 2012, Arizona Electric Power Cooperative, Inc. ("AEPCO") filed with the Arizona Corporation Commission ("Commission") the above captioned application. AEPCO requested a rate decrease, continuation of its Purchased Power and Fuel Adjustor Clause ("PPFAC") with modifications, and approval of revised depreciation rates.

2. Parties to this docket are AEPCO, Trico Electric Cooperative, Inc. ("Trico"), Sulphur Springs Valley Electric Cooperative, Inc. ("SSVEC"), Mohave Electric Cooperative, Incorporated ("MEC"), and the Commission's Utilities Division ("Staff").

3. On October 25, 2013, the Commission issued Decision No. 74173. Among other things, Decision No. 74173 ordered the record in this case to be held open until April 30, 2014, for the limited purpose of allowing AEPCO to file for Commission approval, if it so chose, after collaboration with Staff, a proposed Environmental Compliance Adjustment Rider and Plan of Administration ("ECAR") fully addressing the technical points raised by Staff in the rate proceeding.

4. On April 30, 2014, AEPCO filed in this docket an Application for Approval of the ECAR Plan of Administration and Tariff ("ECAR Application").

5. Due to the possibility of significant rate increases to AEPCO's Class A member distribution cooperatives through an ECAR surcharge, which could then be passed on to their customers, Decision No. 74173 required AEPCO to provide notice of the proposed ECAR to the Class A member distribution cooperatives' customers, within 30 days of filing an ECAR Application.

6. On May 23, 2014, AEPCO filed a motion to extend the deadline to file proof of notice of its ECAR Application, and on July 30, 2014, the Commission issued Decision No. 74600 in this docket, amending Decision No. 74173 to extend the time for AEPCO to complete the ordered customer notice.

7. On July 24, 2014, AEPCO filed affidavits of publication confirming that it had caused notice of the ECAR Application to be published on June 20, 2014, in the *Mohave Daily News*, on July 21, 2014, in the *Arizona Daily Star,* and in the July 2014 issue of *Currents* magazine. The notice published in June and July of 2014 informed end use customers of the possibility that an

ECAR surcharge mechanism would be implemented at a rate of zero, and subsequently increased to recover specific costs. The notice did not quantify the possible magnitude of the future surcharge.

8. No customer comments on the ECAR Application or intervention requests were filed in response to the June and July 2014 public notice.

9. On September 2, 2014, AEPCO filed a Request for Procedural Order Re ECAR Application. Therein, AEPCO proposed a filing schedule for processing the ECAR Application. The filing indicated that there was a disputed issue between the parties.

10. On September 19, 2014, a Procedural Order was issued setting a filing schedule regarding the ECAR Application.

11. On October 17, 2014, Staff filed a Staff Report on the ECAR Application. Staff recommended approval of the ECAR Application, but recommended against AEPCO's requested approval of recovery of chemical expenses through the ECAR. Staff stated that no other utility has received Commission approval to recover such costs through an environmental surcharge.

12. On November 13, 2014, AEPCO filed its Response to the October 17, 2014 Staff Report on the ECAR Application. AEPCO objected to Staff's recommendation that recovery of chemical expenses not be allowed through the ECAR.

13. On January 14, 2015, a Recommended Order on the ECAR Application was docketed, adopting Staff's recommendations.

14. On January 22, 2015, AEPCO filed a Request for Procedural Conference and Postponement of Commission Consideration Re ECAR. AEPCO requested that the Commission postpone consideration of the ECAR Application until after a hearing could be held on contested issues, and requested that a procedural conference be held for the purpose of scheduling the hearing.

15. On January 23, 2015, AEPCO filed letters from Graham County Electric Cooperative, Inc. ("GCEC"), MEC, SSVEC, and Anza Electric Cooperative, Inc. ("Anza") each of which indicated support for AEPCO's requests.

16. On January 30, 2015, a Procedural Order was issued setting a procedural conference to discuss procedural issues relating to scheduling a hearing on contested issues regarding the ECAR Application.

17. On February 20, 2015, a procedural conference was held as scheduled. AEPCO, MEC, and Staff appeared through counsel. The parties discussed a procedural schedule and other procedural issues. AEPCO was informed of the need for public notice of the potential bill impact to customers of the distribution cooperatives if chemical costs and capital costs were included in the ECAR as proposed, and of the hearing on the ECAR Application. To that end, AEPCO was directed to make a filing in this docket specifying the range of costs that AEPCO would be requesting for inclusion in the proposed ECAR surcharge. AEPCO indicated that some of its Members' newsletters have a 60 day lead time for publication. The parties were informed that upon AEPCO's docketing of the rate impact estimate information, a Procedural Order would be issued setting a hearing date and associated procedural deadlines and requirements, including a prescribed form of notice for provision to the retail customers of AEPCO's Members.

18. On March 6, 2015, AEPCO filed a Status Report.

19. On April 22, 2015, AEPCO filed its Request for Briefing Order in Lieu of Hearing Re ECAR. AEPCO attached to the filing an exhibit consisting of a Stipulated Statement of Facts to which AEPCO and Staff agreed, and which included the cost and bill impact estimates that AEPCO was directed to file during the February 20, 2015 procedural conference. A copy of that Stipulated Statement of Facts is attached hereto and incorporated herein as Exhibit A. AEPCO requested that in lieu of a publicly noticed hearing on the ECAR, that a Recommended Order be prepared following parties' briefing on the contested issue of whether chemical costs should be eligible for recovery through the ECAR.

20. On May 7, 2015, a Procedural Order was issued finding that a hearing on the contested issues in the ECAR Application was necessary. The Procedural Order set a hearing to commence on August 24, 2015, and set associated procedural deadlines, including the publication of notice.

21. On June 19, 2015, AEPCO filed the direct testimonies of Peter Scott and Joe King.

22. On July 21, 2015, AEPCO filed Affidavits of Publication and Mailing certifying provision of the public notice of the ECAR required by the May 7, 2015 Procedural Order.

23. On July 24, 2015, Staff filed a Request for Procedural Conference regarding its request to modify the procedural schedule in this matter.

24. On July 27, 2015, a Procedural Order was issued setting a procedural conference as requested by Staff.

25. On August 5, 2015, a procedural conference was convened as scheduled. AEPCO, MEC and Staff appeared through counsel. The parties discussed the need to continue the hearing and proposed modifications to the procedural schedule.

26. On August 10, 2015, a Procedural Order was issued continuing the hearing to October 7, 2015, and scheduling a public comment hearing to take place on the publicly noticed date for the hearing.

27. On August 18, 2015, AEPCO filed its Consent to Email Service.

28. On August 24, 2015, at the time noticed for the hearing on the ECAR Application, a public comment hearing convened as scheduled. No members of the public appeared to provide public comment.

29. On August 26, 2015, Staff filed the direct testimony of Candrea Allen.

30. On August 28, 2015, a Procedural Order was issued approving AEPCO's request to receive service of all filings in this docket via its designated email address.

31. On October 7, 2015, the hearing on the ECAR Application convened as scheduled. AEPCO, MEC and Staff appeared through counsel. As AEPCO and Staff's prefiled testimony had indicated, they had come to agreement on previously disputed issues related to the ECAR Application, and their witnesses presented evidence for the record demonstrating that agreement. At the close of the presentation of evidence, the parties made brief closing statements, and the matter was taken under advisement.

Description of AEPCO

32. AEPCO was initially granted a Certificate of Convenience & Necessity ("CC&N") by Decision No. 33677 (February 13, 1962). As part of the restructuring of AEPCO in the late 1990s and early 2000s, AEPCO requested that the Commission transfer the transmission portion of AEPCO's CC&N to Southwest Transmission Cooperative, Inc. ("SWTC"). The Commission granted the request in Decision No. 63868 (July 25, 2001). Decision No. 74591 (July 30, 2014) transferred SWTC's CC&N back to AEPCO.

33. AEPCO is a non-profit customer-owned cooperative serving the wholesale power needs of its member distribution cooperatives, who use power supplied by AEPCO to meet the electricity needs of their retail members. AEPCO's three Class A partial-requirements members are Trico, MEC, and SSVEC (collectively, "PRMs"). AEPCO's three all-requirements members are Anza, Duncan Valley Electric Cooperative, Inc., and GCEC (collectively, "CARMS"). With the exception of Anza, which is located in south-central California, AEPCO's member distribution cooperatives are located in rural areas of Arizona. The CARMs receive all of their power and energy needs from AEPCO. Each PRM commits only to purchase a fixed amount of capacity from AEPCO, and may secure additional power and energy from other sources. AEPCO also has a Class D member, Valley Electric Association, Inc., which has a service contract with AEPCO for scheduling and trading services, but takes no power from AEPCO.

Decision No. 74173 and the ECAR Mechanism

34. In the rate case, in response to Staff's expressed concerns regarding potential costs associated with the U. S. Environmental Protection Agency ("EPA") regional haze regulations, AEPCO proposed the concept of a surcharge mechanism to provide recovery of potential costs associated with future environmental compliance obligations in the form of an ECAR. MEC and Trico were supportive of AEPCO's proposal to implement an ECAR in conjunction with a revenue decrease.

35. In the rate case proceeding, Staff did not oppose the concept of an ECAR as a cost recovery mechanism, so long as the ECAR would be used for projects that are the best long-term solution for AEPCO and its members. Staff stated that a number of details remained to be addressed. Staff pointed out that the draft ECAR provided by AEPCO in the rate case lacked minimum or maximum dollar amounts and specificity regarding environmental compliance obligations; did not address whether the surcharge would base revenue requirements upon short- or long-term financing, or simply upon ongoing operating cash requirements; did not include a formalized process and list of regulatory accounts to be used for recording funds received and classification of qualified environmental assets; and did not include a provision requiring that the ECAR remain subject to Commission audit on an annual or bi-annual basis. Staff believed that collaborative work sessions

between AEPCO and Staff might be appropriate to address these technical concerns, prior to AEPCO filing revisions to its proposed ECAR and plan of administration in this docket.

36. AEPCO agreed that this docket should be held open so that the parties could work together to refine the ECAR process and details, and AEPCO and Staff could bring a joint recommendation to the Commission for approval. AEPCO proposed to make a filing requesting Commission approval on or before April 30, 2014, and to continue discussions with Staff regarding ECAR details while AEPCO's Apache Generating Station ("Apache Station") Study was being conducted. AEPCO stated that it would work with its members to prepare an environmental compliance strategy ("ECS") plan to address the EPA regional haze requirements, based on the results of the Apache Station Study, which AEPCO planned to file by June 30, 2014. AEPCO stated that it then planned to file a request to reset the ECAR surcharge from zero to a rate based on the detailed costs identified in the ECS. AEPCO anticipated that its proposed procedure would provide sufficient time for its Best Available Retrofit Technology ("BART") alternative proposal, if approved by the EPA, to be operational by December 2017.

37. Decision No. 74173 found that the concept of an ECAR as a cost recovery mechanism, when properly designed and used for projects that are the best long-term solution for AEPCO and its members, might be acceptable and reasonable. Decision No. 74173 also found that while a properly designed ECAR and plan of administration might provide a means for AEPCO to address future environmental compliance obligations, AEPCO had not presented a fully developed ECAR that could be approved. The record in this rate case was therefore held open until April 30, 2014, for the purpose of allowing AEPCO to file, if it so chose, after collaboration with Staff, a revised ECAR and plan of administration to fully address the technical points Staff raised.

Proposed Updated ECAR

38. On April 30, 2014, as contemplated by Decision No. 74173, AEPCO filed the ECAR Application.

39. On June 19, 2015, AEPCO filed an updated proposed ECAR Tariff and Plan of Administration, attached to the prefiled direct testimony of its witness Joe King. A copy of the updated proposed ECAR Tariff is attached hereto and incorporated herein by reference as Exhibit B,

and a copy of the updated proposed ECAR Plan of Administration is attached hereto and incorporated herein by reference as Exhibit C. The updated ECAR Tariff and Plan of Administration include provisions by which operations costs (including chemical costs) will be recovered through a variable $/kWh energy rate, whereas capital costs will be recovered through a fixed monthly charge.[1]

40. Staff's witness testified that in contrast to Staff's position in the October 17, 2014 Staff Report, Staff now believes that recovery of chemical expense costs through the ECAR is appropriate.[2] Staff's witness testified that its current position is based on information AEPCO provided subsequent to the filing of its October 17, 2014 Staff Report.[3] Staff's witness indicated that according to information provided by AEPCO, the estimates of the costs for chemical expenses represent a significant portion of the total cost estimates for AEPCO to comply with impending EPA regulations.[4] Staff does not dispute the estimates AEPCO has provided for chemical expenses associated with urea and activated carbon that would be used to comply with EPA regulations, and does not dispute the negative impact those expenses could have on AEPCO if they are not recovered.[5] Staff is also in agreement with the updated provision to the ECAR proposal for recovery of operations costs via a variable $/kWh energy rate, because the chemical expenses are ongoing costs that may fluctuate based on the amount of energy produced and consumed.[6] Staff believes that an energy charge would provide transparency and more accurate tracking of the chemical costs.[7] Staff recommends approval of the ECAR Tariff and Plan of Administration set forth in Exhibits B and C.[8]

41. The ECAR proposed by AEPCO is a monthly surcharge intended to provide recovery of potential costs associated with future EPA regional haze environmental compliance requirements for AEPCO's two coal-fired units at AEPCO's Apache Station, and also any other potential

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[1] Rebuttal Testimony of AEPCO witness Peter Scott, Exh. A-10 at 2. The updated ECAR also includes a provision previously advocated by Staff in the Staff Report that would require AEPCO to file a new ECAR Tariff set to zero after refunding any excess collections under an approved ECAR Tariff to its members.
[2] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 5.
[3] *Id.* at 3-4.
[4] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 4.
[5] *Id.*
[6] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 5.
[7] *Id.*
[8] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 6.

obligations mandated by federal, state and/or local environmental regulations. The proposed ECAR Tariff would apply to all of AEPCO's Class A member distribution cooperatives.

42. The ECAR Application requests approval of the ECAR Tariff with the rate set at zero. Once the ECAR Application is approved in this proceeding, AEPCO plans to submit another application, along with an ECS plan, requesting that the ECAR be set at a level to recover Qualified ECS Costs.[9] The ECS plan would include the scope of work, anticipated timelines, and specific cost estimates for Qualified Environmental Compliance Projects ("QECP") that AEPCO plans to implement in order to comply with mandated environmental regulations. The ECAR Plan of Administration provides that Commission-approved costs associated with any QECP, as identified in an ECS plan, are Qualified ECS Costs.

43. The proposed ECAR Tariff and Plan of Administration require AEPCO to submit any proposed change to the ECAR rate, along with an ECS plan, to AEPCO's Board of Directors and AEPCO's Class A member distribution cooperatives for approval of the Board and unanimous consent of the Class A member distribution cooperatives prior to submission for Commission approval.[10] Increases to the ECAR are to be based on Qualified ECS Costs.[11]

44. The proposed ECAR Plan of Administration provides that an approved increase to the ECAR will be apportioned to each member distribution cooperative based on the member's Allocated Capacity Percentage ("ACP"). For capital costs, the monthly dollar amount to be collected from each CARM would be based on its monthly demand ratio share, calculated each month as the percentage of the CARM's 12-month rolling average demand to the total of the CARMs' 12-month rolling average demand, and AEPCO would determine the term of collection for the costs.[12]

45. For operations costs, the operating costs associated with environmental compliance would be assessed to each member on a per kWh basis.[13]

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[9] Qualified ECS Costs are defined in the ECAR Plan of Administration, Exhibit C at 1-2, and do not include environmental fines or penalties, or any costs already recovered through established rate tariffs or any other Commission-approved adjustor mechanism.

[10] Proposed ECAR Tariff, Exhibit B at 2; Proposed ECAR Plan of Administration, Exhibit C at 4.

[11] Proposed ECAR Plan of Administration, Exhibit C at 1-2.

[12] Proposed ECAR Tariff, Exhibit B at 1; Proposed ECAR Plan of Administration, Exhibit C at 2.

[13] *Id.*

46. The proposed ECAR Plan of Administration specifies, by Rural Utilities Service ("RUS") account, the capital addition costs and other costs eligible for recovery through the ECAR, if approved by the Commission.[14]

47. The funds collected through the ECAR would be deposited into an interest bearing investment account ("ECAR Surcharge Account"). The funds would be used only for QECPs in an approved ECS plan, and would be recorded as contributions in aid of construction. The proposed Plan of Administration provides that upon completion or termination of an ECS plan, all remaining funds in the ECAR Surcharge Account, including interest earned, would be refunded to members within 90 days, using the same method for collecting the ECAR surcharge, returning the ECAR rate to zero.[15] AEPCO would then file a revised ECAR Tariff returning the rate to zero, and the rate would remain at zero until AEPCO deemed it necessary to utilize the ECAR Tariff again in response to an environmental regulation, in which case it would prepare and file an initial ECS plan and initial revised tariff for Commission approval.[16]

48. The proposed ECAR Plan of Administration provides that the level of funding and ECAR rate may be adjusted up or down upon the filing of a request and Commission approval. AEPCO would file a request for changing the ECS and the ECAR Tariff, and after a 60 day review period, the new rate would become effective without further Commission action, unless the Commission elects to suspend the revised ECAR Tariff, in which case it would become effective only upon Commission approval.[17]

49. Compliance reporting is required by the proposed ECAR Plan of Administration, on September 1, for the prior January through June period, and on March 1, for the prior July through December period.[18]

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[14] Proposed ECAR Plan of Administration, Exhibit C at 2-3. The ECAR Plan of Administration also provides that the list may be expanded to include other accounts approved by the Commission in the future.
[15] Proposed ECAR Plan of Administration, Exhibit C at 3, 4.
[16] Proposed ECAR Plan of Administration, Exhibit C at 4.
[17] Proposed ECAR Tariff at 1-2, Exhibit B at 2; Proposed ECAR Plan of Administration, Exhibit C at 4.
[18] Proposed ECAR Plan of Administration, Exhibit C at 3-4.

AEPCO's Upcoming Environmental Compliance Obligations

50. There are two federal requirements with upcoming deadlines that may require AEPCO to seek funding through the ECAR: the EPA's regional haze requirements and the EPA's Mercury and Air Toxics Standards ("MATS").[19]

51. In November 2012, the EPA's regional haze federal implementation plan ("FIP") was finalized and required AEPCO to install selective catalytic reduction ("SCR") technology on both Apache Station coal units.[20] AEPCO subsequently proposed its BART alternative emissions reduction plan to the EPA which included the conversion of Apache Station Steam Turbine Unit 2 to natural gas-fired operation, and the installation of selective non-catalytic reduction ("SNCR") technology on Steam Turbine Unit 3.[21] In February 2015, the EPA granted final approval for AEPCO's BART alternative plan.[22] AEPCO's operation of Steam Turbine Unit 3 with SNCR technology will require the use of the chemical urea.[23] AEPCO's deadline for SNCR installation is December of 2017.[24]

52. In order to comply with EPA's MATS requirements, beginning in April 2016, AEPCO must begin using activated carbon in the operation of both its both Apache Station coal units.[25] When Steam Turbine Unit 2 is switched to natural gas operation, activated carbon will be used only in the operation of Steam Turbine Unit 3.[26]

53. AEPCO has not yet prepared an ECS for costs associated with compliance with either the regional haze or MATS regulations. However, AEPCO has estimated total capital costs associated with compliance at $32 million, and from that figure has estimated associated annual capital carrying costs at $0.41 million in 2016, $1.90 million in 2017, and $3.40 million in 2018.[27] AEPCO has estimated annual chemical costs ranging from $2.2 million to $4.5 million in 2016, $3.1

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[19] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 7-8.
[20] Direct Testimony of AEPCO witness Peter Scott, Exh. A-9 at 2.
[21] *Id.* at 3.
[22] *Id.*
[23] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 8.
[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] *Id.;* Exhibit A.

million to $6.2 million in 2017, and $2.2 million to $5 million in 2018.[28] Both sets of estimates are non-cumulative.[29]

54. AEPCO prepared an estimate of the possible rate impacts the ECAR could have on its members' residential customers based on average usage and current rate levels, as shown in Exhibit A. The following estimated information was provided to the residential end users through published notice:[30]

Year	Possible Monthly Impact from Capital Costs	Possible Monthly Impact from Chemical Operating Costs	Possible Total Monthly Impact
2016	$0.11 to $0.19	$0.61 to $2.10	$0.72 to $2.29
2017	$0.53 to $0.90	$0.84 to $2.91	$1.37 to $3.81
2018	$0.94 to $1.61	$0.59 to $2.34	$1.53 to $3.95
Years After 2018	No estimates provided	No estimates provided	No estimates provided

55. AEPCO's witness testified that the use of urea and activated carbon is necessary to comply with the EPA's regional haze ruling and MATS requirements, that the price of urea has historically been volatile, and that industry experts are predicting that environmental regulations will put upward pressure on prices for activated carbon.[31] Because the costs for these chemicals is not recoverable through AEPCO's PPFAC,[32] if they were to be included in AEPCO's base rates as an annual pro-forma expense, their expected fluctuations in price would lead to under- or over-recovery.[33]

56. According to AEPCO's witness Mr. King, it is quite possible that AEPCO would need to file an expedited rate case in early 2016 if chemical costs are excluded from recovery through the ECAR.[34] AEPCO does not believe that filing a rate case under those circumstances would be in the

[28] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 8-9; Exhibit A.
[29] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 9.
[30] *See* AEPCO's July 21, 2015 Compliance Filing Concerning Notice of ECAR Hearing.
[31] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 9-10.
[32] The chemicals that AEPCO will use to comply with EPA's regional haze and MATS requirements are recorded in RUS Account 502 as a steam expense. AEPCO's PPFAC allows recovery of fuel expenses recorded in RUS Account 501, but not steam expenses. Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 11.
[33] *Id.*
[34] Direct Testimony of AEPCO witness Joe King, Exh. A-8 at 12.

best interests of AEPCO and its members.[35] AEPCO requests that the Commission approve its proposed ECAR.

57. As stated above, Staff does not dispute the estimates AEPCO has provided for chemical expenses associated with urea and activated carbon that would be used to comply with EPA regulations, and does not dispute the negative impact those expenses could have on AEPCO if they are not recovered.[36] Staff recommends approval of the ECAR Tariff and Plan of Administration set forth in Exhibits B and C.[37]

Conclusion

58. We agree with AEPCO and Staff that under the special circumstances of this case, it is appropriate to establish an ECAR mechanism to allow recovery of the necessary and prudent capital costs and operating costs AEPCO must incur to achieve compliance with EPA environmental compliance requirements for AEPCO's two coal-fired units at AEPCO's Apache Station, and also with other potential future obligations mandated by federal, state and/or local environmental regulations.

59. While the exact amount of the obligatory capital costs are unknown at this time, the nature of the one-time capital costs expenditures necessary for AEPCO to achieve compliance with environmental regulations, coupled with the fact that AEPCO is a cooperative utility, justify the implementation of the extraordinary rate making mechanism AEPCO requests.

60. AEPCO has demonstrated that the level of chemical costs associated with its environmental compliance obligations are likely to be considerable, ongoing, and volatile, and that failure to recover the costs could negatively impact AEPCO's available working capital. For those reasons, we agree with AEPCO and Staff that cost recovery of chemical expenses necessary for environmental compliance obligations should be included in the ECAR mechanism framework we approve herein.

61. The parties' recommendations for approval of AEPCO's proposed ECAR Tariff and Plan of Administration as they appear in Exhibits B and C are reasonable and should be adopted.

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[35] *Id.*
[36] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 4.
[37] Direct Testimony of Staff witness Candrea Allen, Exh. S-12 at 6.

62. AEPCO should be required to file an ECAR Tariff and Plan of Administration conforming to the Commission approval herein within 15 days of this Decision.

CONCLUSIONS OF LAW

1. AEPCO is a public service corporation within the meaning of Article XV of the Arizona Constitution and A.R.S. §§ 40-250 and 40-251.

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

3. Notice of the application was given in accordance with law.

4. It is just and reasonable and in the public interest to approve AEPCO's proposed ECAR Tariff, set at zero, as it appears in Exhibit B.

5. It is just and reasonable and in the public interest to approve AEPCO's proposed ECAR Plan of Administration as it appears in Exhibit C.

ORDER

IT IS THEREFORE ORDERED that Arizona Electric Power Cooperative, Inc.'s proposed ECAR Tariff as it appears in Exhibit B, set at zero, is hereby approved.

IT IS FURTHER ORDERED that Arizona Electric Power Cooperative, Inc.'s proposed ECAR Plan of Administration as it appears in Exhibit C is hereby approved.

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IT IS FURTHER ORDERED that Arizona Electric Power Cooperative, Inc. shall file, within 15 days of this Decision, as a compliance item in this matter, a proposed Environmental Compliance Adjustment Rider Tariff and Plan of Administration conforming to the approvals herein.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER

COMMISSIONER COMMISSIONER COMMISSIONER

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

_____
JODI JERICH
EXECUTIVE DIRECTOR

DISSENT _____

DISSENT _____
TJ:ru(tv)

SERVICE LIST FOR: ARIZONA ELECTRIC POWER COOPERATIVE, INC.

DOCKET NO.: E-01773A-12-0305

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EXHIBIT A

Docket No. E-01773A-12-0305
Arizona Electric Power Cooperative, Inc.
Environmental Compliance Adjustment Rider
Stipulated Statement of Facts

1. On April 30, 2014, Arizona Electric Power Cooperative, Inc. ("AEPCO" or the "Cooperative") filed its application for approval of an Environmental Compliance Adjustment Rider ("ECAR").
2. The purpose of the ECAR is to establish a monthly surcharge to provide AEPCO with a revenue mechanism to meet future environmental compliance obligations mandated by federal, state and/or local laws or regulations. Examples of such obligations currently faced by AEPCO include:
    a. modifications to AEPCO's generating facilities at its Apache Station and the need to use urea in the Selective Non-Catalytic Reduction ("SNCR") process, which have been approved by the Environmental Protection Agency ("EPA") as a means for AEPCO to meet the EPA's regional haze requirements as of December 2017; and
    b. the Cooperative's need to purchase and use activated carbon in order to comply with the EPA's Mercury and Air Toxics Standards ("MATS") as of April 2016.
3. As proposed, the ECAR rate will initially be set at zero. Thereafter, in response to a particular environmental regulation, AEPCO will analyze its financial status, including its current rate levels and any expenses that qualify for recovery/refund through its Purchased Power and Fuel Adjustment Clause ("PPFAC"), to determine whether the Cooperative requires additional revenue to comply with the given regulation or whether its margins are sufficient. If AEPCO determines that its margins are sufficient, the ECAR rate would remain at zero.
4. If the results of AEPCO's financial analysis indicate that additional revenues are needed for environmental compliance, the Cooperative will prepare and file with Docket Control its initial Environmental Compliance Strategy ("ECS"), which, at a minimum, will include a scope of work, anticipated timelines and cost estimates. Prior to filing an initial ECS, AEPCO must obtain authorization from its Board of Directors as well as unanimous consent from its Class A Distribution Cooperative Members ("AEPCO's Members"). The compliance costs identified for recovery in the initial ECS cannot be recovered through the ECAR without affirmative approval by the Arizona Corporation Commission. If approved, the ECAR rate will be charged to AEPCO's Members, who, in turn, may pass those charges through to their retail members via their respective purchased power clauses.
5. AEPCO's ECAR Plan of Administration ("POA") identifies (by RUS account number) the categories of costs that would be eligible for recovery through the ECAR. AEPCO's proposal includes capital costs necessary to achieve compliance with environmental regulation. AEPCO is also requesting inclusion of certain chemical costs as eligible for recovery through the ECAR. Specifically, the POA identifies as eligible for recovery

RUS Account 502 Steam Expenses "limited to chemical expenses incurred solely due to Environmental Regulation(s) but not including any indirect expenses such as overhead."

6. The Commission's Utilities Division Staff ("Staff") supports approval of the ECAR and use of the mechanism for recovery of necessary capital expenses, as specified by the RUS accounts included in the proposed POA. However, Staff opposes AEPCO's proposal to the extent that it includes chemical costs as eligible for recovery through the ECAR (RUS Account 502-Steam Expenses).
7. The RUS Account 502 chemical costs identified in AEPCO's POA will be necessary for compliance with both the EPA's regional haze and MATS regulations. Specifically, AEPCO's compliance plan for the EPA's regional haze regulation requires the use of urea. Likewise, AEPCO will need to purchase and utilize activated carbon in order to comply with MATS.
8. The price of both urea and activated carbon are subject to market forces, making them variable and potentially volatile. Historically, the price of urea has been highly volatile, as shown on Exhibit 1 to AEPCO's Response to Staff Report re ECAR Plan of Administration and Tariff, dated November 13, 2014 ("AEPCO's Response"). Also, Exhibit 2 to AEPCO's Response indicates that the demand for activated carbon is anticipated to increase significantly in the future, which will result in upward pressure on prices.
9. Another chemical that AEPCO has and will continue to purchase and use in connection with its mercury-related environmental compliance obligations (imposed by the State of Arizona) is calcium bromide. The cost of calcium bromide is included in RUS Account 501 because the chemical is applied before the fuel enters the hopper. Because this chemical is recorded as an RUS Account 501 expense (as opposed to a 502 expense), it qualifies for inclusion in AEPCO's PPFAC.
10. AEPCO's current estimates for the combined RUS Account 502 chemical costs required to comply with the EPA's regional haze and MATS regulations over the next three years range from a low of $2.2 million to a high of $6.2 million annually: $2.2 million to $4.5 million in 2016; $3.1 million to $6.2 million in 2017; and $2.2 million to $5 million in 2018. AEPCO's current estimated revenue requirements associated with the Cooperative's capital investment for compliance with the EPA's regional haze and MATS regulations over the next three years are as follows: $0.41 million in 2016; $1.90 million in 2017; and $3.40 million in 2018.
11. AEPCO asserts that the impact of these costs on the retail customer is difficult to determine because AEPCO's Members have different retail rate levels and structures. Based on its preliminary analysis and communications with and input from the Members, AEPCO estimates the average monthly residential bill impact (based on Member 2013 Form 7 data) related to the chemical compliance costs could range as follows: $0.61 to $2.10 in 2016; $0.84 to $2.91 in 2017; and $0.59 to $2.34 in 2018. Using the same methodology, AEPCO estimates the average monthly residential bill impact related to capital costs could range as follows: $0.11 to $0.19 in 2016; $0.53 to $0.90 in 2017; and $0.94 to $1.61 in 2018. According to AEPCO, these increases are not cumulative and would only be implemented through the ECAR if AEPCO includes the chemical and

capital cost components in its ECS and if that ECS receives approval from AEPCO's Board, its Members and the Commission. AEPCO further asserts that, otherwise, the ECAR associated with any particular ECS may continue at the initially set level of zero. Staff neither agrees nor disagrees with the foregoing assertions or bill impact estimates provided by AEPCO; Staff has no evidence to the contrary and, therefore, is not disputing the Cooperative's assertions or estimates.

EXHIBIT B

ARIZONA ELECTRIC POWER COOPERATIVE, INC.

ENVIRONMENTAL COMPLIANCE ADJUSTMENT RIDER (ECAR)

TARIFF

Effective Date: _____ 1, 2015

PURPOSE

The purpose of the Environmental Compliance Adjustment Rider ("ECAR") is to provide a revenue recovery mechanism that will create a fund to be used for the purpose of meeting environmental compliance obligations mandated by federal, state, or local laws or regulations. The ECAR is the tariff collection mechanism for the overall Environmental Compliance Strategy ("ECS") developed by Arizona Electric Power Cooperative, Inc. ("AEPCO" or "Company") and its Members.

APPLICABILITY

Applicable to all Class A Member Distribution Cooperatives of AEPCO.

TERMS AND CONDITIONS

1. The initial rates of the tariff shall be set at zero. AEPCO will calculate the capital costs (including carrying costs and/or contributions in aid of construction) and operations' costs (including chemical costs) to be collected from each Class A Member Distribution Cooperative through the ECAR as follows:

    a. Capital Costs – AEPCO will allocate the capital costs to each Class A Member Distribution Cooperative as a monthly fixed charge based on the Allocated Capacity Percentage ("ACP") of each Member. The monthly dollar amount to be collected from each individual Collective All-Requirements Member ("CARM") will be based upon each CARM's monthly Demand Ratio Share. The Demand Ratio Share is calculated each month as the percentage of each CARMs' 12-month rolling average demand to the total of the CARMs' 12-month rolling average demand. For contributions in aid of construction, AEPCO will also determine the term of collection for the costs.

    b. Operations' Costs – The operating costs associated with environmental compliance will be assessed to each Member on a per kWh basis.

2. Once the monthly fixed and variable charges and the term of collection, if any, have been established, AEPCO will file the ECS plan and a revised tariff with the Arizona Corporation Commission ("ACC" or "Commission"), for Commission approval.* Once the revised tariff is effective, each Member will be assessed a monthly charge on its bill

for environmental compliance capital costs and a variable charge for environmental compliance operating costs in addition to other rates and charges approved by the Commission. Exhibit A sets forth the monthly Member charges and anticipated term of collection, if any.

3. The level of funding and ECAR rates may be adjusted (up or down) depending on the actual environmental compliance funding needs of the Company as outlined in the ECS plan. Any changes to the ECS and ECAR tariff after the initial ECS plan is approved will be subject to a sixty (60) day ACC Staff review period.* The revised tariff shall become effective at the end of the sixty (60) day period unless the Commission elects to suspend the revised tariff, in which case it shall become effective upon Commission approval.

Details of the operation of the ECAR and ACC compliance requirements are as set forth in the Company's Plan of Administration.

*In order for the ECAR to be revised, AEPCO must obtain Board approval and the unanimous consent of its Class A Member Distribution Cooperatives, prior to being submitted to the Commission.

EXHIBIT A

The Monthly Charges shall be as follows for each of the Company's Class A Member Distribution Cooperatives:

_____ 1, 2015*

Environmental Compliance Capital Costs

Collective All-Requirements Members:

Anza Electric Cooperative, Inc.	$0.00/mo.
Duncan Valley Electric Cooperative, Inc.	$0.00/mo.
Graham County Electric Cooperative, Inc.	$0.00/mo.

Partial Requirements Members:

Mohave Electric Power Cooperative, Inc.	$0.00/mo.
Sulphur Springs Valley Electric Power Cooperative, Inc.	$0.00/mo.
Trico Electric Cooperative, Inc.	$0.00/mo.

Environmental Compliance Operations' Costs

All Members:	$0.00000/kWh

*The stated Monthly Rates apply to service provided on and after this date.

EXHIBIT C

Arizona Electric Power Cooperative, Inc.

Environmental Compliance Adjustment Rider

Plan of Administration

ECAR – Plan of Administration

General Description:

The purpose of the Environmental Compliance Adjustment Rider ("ECAR") Surcharge is to establish a fund to be used for the purpose of meeting, in whole or in part, the cost of environmental compliance obligations imposed on or applicable to the Arizona Electric Power Cooperative, Inc. ("AEPCO") that are mandated by federal, state or local laws or regulations or judicial or regulatory agency interpretations of such laws or regulations ("Environmental Regulations"). The ECAR provides for the recovery of capital addition costs, operations' costs and any other costs specified in the Environmental Compliance Strategy, as approved by the Commission. The ECAR is not intended to recover any costs already recovered in base rates approved in Decision No. 74173 or any subsequent rate case decision or recovered through any other Commission-approved adjustor mechanism.

Key Definitions:

1. ECAR Surcharge – A rate rider approved by the Arizona Corporation Commission ("ACC" or "Commission") in Decision No. XXXXX which authorizes AEPCO to: recover or mitigate Environmental Regulations operations' costs; or fund, in whole or in part, capital additions required by Environmental Regulations.

2. Environmental Compliance Strategy ("ECS") – A formal plan developed by AEPCO to meet Environmental Regulations. The ECS shall include, at a minimum, a scope of work, anticipated timelines and cost estimates.

3. Qualified Environmental Compliance Projects – Projects, as specified in the ECS plan, implemented in order to comply with standards mandated by Environmental Regulations. These standards include, but are not limited to, restrictions of carbon dioxide (CO_2), nitrogen oxide (NO_x), sulfur oxide (SO_x), ozone, particulate matter (PM), volatile organic compounds (VOC), mercury (Hg), and other toxins, coal ash and other requirements.

4. Qualified ECS Costs – The costs associated with Qualified Environmental Compliance Projects as identified in the ECS plan and approved by the Commission as appropriate for recovery through the ECAR Surcharge pursuant to ACC review of the ECS plan. The Qualified ECS Costs must be classified in one or more of the Rural Utilities Service ("RUS") accounts, or any other successor RUS account, listed below under Qualified RUS Accounts. Any costs already recovered in base rates approved in Decision No. 74173 or any subsequent rate case decision or recovered through any

other Commission-approved adjustor mechanism are not Qualified ECS Costs and are not recoverable through the ECAR. Environmental fines or penalties do not qualify for cost recovery through the ECAR Surcharge nor do costs that have been included as part of AEPCO's authorized cost of service for recovery through established rate tariffs.

Calculation of ECAR:

Based on costs detailed in the ECS, AEPCO will calculate the capital costs (including carrying costs and/or contributions in aid of construction) and operations' costs (including chemical costs) to be collected from each Class A Member Distribution Cooperative through the ECAR. AEPCO will allocate the capital costs to each Class A Member Distribution Cooperative as a monthly fixed charge based on the Allocated Capacity Percentage ("ACP") of each Member. The fixed charge to be collected from each individual Collective All-Requirements Member ("CARM") will be based upon each CARM's monthly Demand Ratio Share. The Demand Ratio Share is calculated each month as the percentage of each CARMs' 12-month rolling average demand to the total of the CARMs' 12-month rolling average demand. The operating costs associated with environmental compliance will be assessed to each Member on a per kWh basis. AEPCO will also determine the term of collection for any contributions in aid of construction.

Qualified RUS Accounts:

The costs classified in the following RUS accounts are eligible to be recovered through the ECAR. This list may be expanded to include other accounts approved by the Commission in the future.

Steam Production Plant

- 310 Land and Land Rights
- 311 Structures and Improvements
- 312 Boiler Plant Equipment
- 313 Engines and Engine Driven Generators
- 314 Turbogenerator Units
- 315 Accessory Electric Equipment
- 316 Miscellaneous Power Plant Equipment

Other Production Plant

- 340 Land and Land Rights
- 341 Structures and Improvements
- 342 Fuel Holders, Producers, and Accessories

- 343 Prime Movers
- 344 Generators
- 345 Accessory Electric Equipment
- 346 Miscellaneous Power Plant Equipment

Steam Power Generation Operations

- 502 Steam Expenses (limited to chemical expenses incurred solely due to Environmental Regulation(s) but not including any indirect expenses such as overhead)

Accounting:

Funds collected from the ECAR Surcharge will be separately identified by AEPCO and recorded as a regulatory liability. Accounting for these funds shall be done on a contributing Member Distribution Cooperative basis. Use of these funds to meet Qualified ECS Costs will reduce that regulatory liability on a dollar-for-dollar basis. Funds used for qualified environmental capital additions (as opposed to capital carrying costs) will be recorded as contributions in aid of construction.

Investment Administration:

AEPCO will deposit all funds collected through the ECAR Surcharge in a separate interest bearing investment account ("ECAR Surcharge Account") and may only draw monies from the account to fund Qualified ECS Costs. Interest earned on the investment of these funds shall be retained in the account. Upon completion or termination of the ECS plan, all remaining funds in the ECAR Surcharge Account, including interest earned, will be refunded to Members within ninety (90) days, returning the rates to zero, using the same method established for the collection of the ECAR (see Calculation of ECAR above).

Compliance Reports:

On September 1 for the previous January through June period and March 1 for the prior year July to December period of each year, AEPCO will file semi-annual reports concerning the ECAR Surcharge with the Commission, with a copy to its Members, containing the following information for the reporting period:

1. The beginning balance of the ECAR Surcharge Account.
2. The amount collected from each Class A Member through the ECAR Surcharge, including the total amount collected.
3. The total amount of interest earned by the ECAR Surcharge Account.
4. The total withdrawals for Qualified ECS Costs.
5. The ending balance of the ECAR Surcharge Account.

AEPCO will also file the following supporting information with the semi-annual report:

1. A listing of the dates and amounts of withdrawals.
2. A description of each Qualified ECS Cost paid during the period and the accounting for each cost.

Each report will be certified by AEPCO's Chief Executive Officer or Chief Financial Officer that all information provided in the filing is true and accurate to the best of his or her information and belief. However, no report shall be required for reporting periods during which there is no account activity and both the beginning and ending balances of the ECAR Surcharge Account are zero ($0.00).

ECS and ECAR Surcharge Modifications:

Pursuant to Decision No. XXXXX, the initial ECAR rates shall be set at $0.00. Thereafter, in response to an Environmental Regulation, AEPCO shall file its initial ECS plan and a revised ECAR tariff with Docket Control for Commission approval.

The level of funding and ECAR rates may be adjusted (up or down) depending on the actual environmental compliance funding needs of the Company as outlined in the ECS plan. Any changes to the ECS and ECAR tariff after the initial ECS plan is approved will be subject to a sixty (60) day ACC Staff review period. The revised tariff shall become effective at the end of the sixty (60) day period unless the Commission elects to suspend the revised tariff, in which case it shall become effective upon Commission approval.

Upon completion or termination of the ECS plan, all remaining funds in the ECAR Surcharge Account not needed to meet the Company's objective(s) for the ECS plan, including interest earned, will be refunded to Members within ninety (90) days, returning the rates to zero, using the same method established for the collection of the ECAR. AEPCO will file a revised tariff returning the rates to zero. The rates shall remain at zero until AEPCO deems it necessary to utilize the ECAR tariff again in response to an Environmental Regulation, in which case it will prepare and file an initial ECS plan and initial revised tariff for Commission approval.

AEPCO Board Approval and Member Consent:

Prior to filing an initial ECS plan and revised ECAR tariff or seeking a subsequent modification to either the ECS or ECAR, AEPCO will obtain authorization from its Board. AEPCO shall also notify its Member Distribution Cooperatives sixty (60) days in advance of a proposed filing with the Commission in order to confirm the unanimous consent of its Members. Absent receipt of timely written objections, Member consent shall be deemed obtained and AEPCO may proceed with the filing.