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BEFORE THE ARIZONA CORPORATION COMMISSION

COMISSIONERS:
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BOB STUMP
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ANDY TOBIN

IN THE MATTER OF THE APPLICATION OF UNS ELECTRIC, INC. FOR THE ESTABLISHMENT OF JUST AND REASONABLE RATES AND CHARGES DESIGNED TO REALIZE A REASONABLE RATE OF RETURN ON THE FAIR VALUE OF THE PROPERTIES OF UNS ELECRIC, INC., DEVOTED TO ITS OPERATIONS THROUGHT THE STATE OF ARIZONA AND FOR RELATED APPROVALS	DOCKET NO. E-04204A-15-0142

Arizona Corporation Commission
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INITIAL POST-HEARING BRIEF OF

FRESH PRODUCE ASSOCIATION OF THE AMERICAS

April 25, 2016

I. INTRODUCTION

The Fresh Produce Association of the Americas ("FPAA") intervened in this matter on behalf of its members who have experienced significant financial hardships as a result of UNS Electric, Inc.'s ("UNSE" or "the Company") recent shift in rate design for customers in the Large General Service class. FPAA members make up the bulk of the produce import industry in Nogales, Arizona—a vital economic driver for an already economically depressed Santa Cruz County. Since UNSE's last rate case, many FPAA members' energy costs have risen so dramatically that they are now facing the serious dilemma of whether to move their operations out of UNSE's service territory. FPAA opposes UNSE's current application for an additional rate increase on the newly proposed Medium General Service Class, and asks that the Arizona Corporation Commission consider FPAA members' unique load profile as FPAA seeks relief from an inequitable rate design.

II. BACKGROUND

In Decision 74235[1] the Arizona Corporation Commission, in addition to approving a 9% increase over adjusted test year revenue, approved a new large general service tariff for UNSE, which included a ratcheted demand provision ("demand ratchet") that would adjust the monthly billing demand to the maximum of either the monthly metered demand or 75% of the greatest demand in the preceding 11 months. That demand ratchet came about as the result of settlement negotiations in which neither FPAA nor any other representatives of the Nogales produce industry participated. Prior to that decision, UNSE had never before used a demand ratchet to recover fixed costs from its large commercial customers.

[1] Decision 74235, Docket No. E-04204A-12-0504, December 31, 2013.

Being unfamiliar with demand ratchets and wholly unsuspecting of the impact it would have on FPAA member operations, FPAA chose not intervene in UNSE's previous rate case.

When asked at hearing about UNSE's philosophy of designing demand charges that are "fair and equitable" for different customer classes, UNSE witness Dallas Dukes stated:

> [W]e know the costs are incurred by the system, and those are allocated to that customer class. And the most fair and equitable way to present that to the customers is in a manner that gives them the price signals based on how those costs are incurred, and then to step back and look at the bill impacts and how they are being charged now and make sure that we are not giving them – we are not making such significant changes that they cannot understand their bill and they cannot control their bill.
>
> . . .
>
> It starts to give them that information and gives them the opportunity to control their bill and – but not in a manner that's so punitive in its initial change that it is not fair to them.[2]

Since the rates approved by Decision 74235 went into effect on January 1, 2014, many FPAA customers have experienced a rate impact of 20 to 30 percent as a direct result of the demand ratchet. This rate impact is greater than was intended by the rate design approved by the Commission in Decision 74235. In the present case pending before the Commission, UNSE proposes additional increases in customer charges and demand charges, as well as a new cost-allocation methodology, which will only serve to further exacerbate the problems being faced by FPAA members. Although fuel prices are currently historically low, FPAA believes that the proposed increases in UNSE's non-fuel rate components (*i.e.*, the basic service charge, the demand charge, and the energy delivery charges) will result in an *additional* rate increase of at least 2-5% for the typical FPAA member.

[2] Hearing Transcript, p.1905, line 22—p. 1906, line 17.

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At hearing, UNSE's CEO David Hutchens was asked by several parties about potential "unintended consequences" of the Company's rate designs. At one point, Mr. Hutchens was asked directly if customers experiencing 20 to 30 percent rate increases qualified as an unintended consequence. He responded that, "From an unplanned perspective, if there was a very drastic increase, yes, that would be an unintended consequence. If it affected a particular class, that's indeed what we're looking for."[3]

During these proceedings UNSE has repeatedly touted the need to attract new businesses to its service territory, and avoid the loss of additional large customers. Yet, as expressed in FPAA's Direct and Surrebuttal Testimony, many FPAA members have been forced to consider relocating their operations due to unmanageable energy costs resulting from UNSE's recent rate changes, namely the demand ratchet. When asked by Judge Rodda at the hearing about this shift to Texas, FPAA witness Lance Jungmeyer stated:

> [T]hey talk about it more and more every year. We are not necessarily seeing them close up shop in Nogales. What we are seeing is that they are diverting a significant amount of growth.
>
> As was pointed out by UNS's attorney, the [Arizona] industry is growing and has grown about 15 percent, I would say, during the period that was mentioned in that exhibit. What we have seen is, during that same time, Texas has grown by leaps and bounds. They re promoting a very conducive environment, and they have worked hard to create that within their state. And we in a sense are always trying to match that or exceed that in order to keep our business competitive in Arizona and maintain.[4]

At the public hearing conducted in Nogales on March 22, 2016, several representatives of very large FPAA businesses spoke on record to Chairman Little, Commissioner Burns, and Commissioner Tobin about the pressure they feel to move to Texas—a state whose regulatory body, the Texas Public Utilities

[3] Hearing Transcript, p. 339, lines 8-14.
[4] *Id,* p. 3019, lines 2 - 15.

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Commission—has gone to great lengths to protect counter-seasonal produce import businesses from the unfair and punitive nature of demand ratchets. These sophisticated and experienced business owners, whose companies directly or indirectly contribute to over 4,000 jobs in Santa Cruz County, expressed frustration with the ratchet-inflated summertime bills they now are forced to pay to UNSE. They very bluntly stated that it no longer makes economic sense for them to invest new money in Nogales. Their dollars are better spent in the much more regulatory friendly environment of Texas.

When questioned about this topic, Mr. Hutchens stated the following:

> Q. [I]s there an overall impact or rate impact or percentage increase on large commercial users that you would feel is excessive or counter to your stated goals of attracting new businesses, or even maintaining the ones you already have?
>
> A. There is. There isn't a hard and fast percentage, but you know it when you see it.
>
> Q. Generally if you were aware of specific rate design measures that were directly contributing to a large customer base of commercial users leaving the service territory, would you deem that an unintended consequence of that rate design?
>
> A. Yes.
>
> Q. And if that were happening, would the company look for options to mitigate the loss of those businesses if it could be done in a reasonable manner?
>
> A. Yes.

III. ARGUMENT

A. <u>Demand charges should reflect a customer's contribution to the overall system peak.</u>

Throughout its written testimony and at the hearing, FPAA has repeated asserted that its members generally do not contribute to UNSE's overall system peak demand the same way the rest of the businesses in the Large General Service (and newly proposed Medium General Service) class do. As FPAA witness Lance Jungmeyer pointed out:

> FPAA members provide refrigeration services primarily in the periods from October through June. And the facilities go almost entirely dormant from July through September. We are considered a counter-seasonal industry."[5]
>
> . . .
>
> And when you look at the overall demand of the industry with high peaks in the wintertime and low valleys in the summer, it would seem that we provide an involuntary demand-side management benefit to UNSE in the system by reducing their demand here in the hottest months of the year when they face, when most of Arizona's customers face difficulty and expense.[6]

Nucor's expert witness, Dr. Jay Zarnikau , very aptly explained how demand ratchets, and demand charges in general, should be reflective of cost causation principles as they relate to a utility's peak demand:

I

> A. Based on the theory of cost causality adopted by the utility, to which I pretty much agree, the utility incurs generation capacity costs and transmission capacity costs based on peak demands, what the peak demand is and peak demand needs. Yet, when they designed the demand charge applicable to your clients and my clients, it is a formula. It is based on a minimum demand. . . . It is based on . . . one half the demand during off-peak periods, and it is based on a demand within a very large on-peak period.
>
> If truly the company believes that capacity costs of generation or transmission are really caused by peak needs, the system peak, then that formula just doesn't seem very relative, seems out of line with their theory.
>
> Q. So in your opinion, the demand charges or, in this case, the demand ratchet both of us, or my clients and your company, are subjected to, you believe it should reflect the true contribution to the system peak?
>
> A. Yes. Yeah. We have, I guess, a different solution to the problem similar problem. As I understand your members don't really cause or contribute that much to an August or July system peak. You are on during June, that's --
>
> Q. Correct.
>
> A. By the company's definition that's one of the peak months, but I am

[5] Hearing Transcript, p. 3005, line 24—p. 3006, line 3.
[6] Hearing Transcript, p. 3006, line 20—p. 3007, line 1.

> somewhat sympathetic to the situation your members are in. You also do not really contribute that much to the annual system peak, as it should be defined, as a narrow window of hours. Yes.[7]

When FPAA members get charged according to the same demand ratchet formula as all the rest of the customers in their class, even though FPAA members don't contribute anywhere near as much to the system's overall peak summer demand as other in that class, FPAA members will inevitably be subsidizing the rest of the class during the summer. When asked by Judge Rodda about the unfair intra-class subsidies Nucor alleges it is paying in the Large Power Service class, Dr. Zarnikau replied, "And as I mentioned, it is kind of a similar situation to the Fresh Produce group. They are not operating during the summer peaks, yet they are paying demand charges as if they were."[8]

B. <u>FPAA members' load characteristics are unique to UNSE's system and therefore warrant unique rate treatment.</u>

UNSE has acknowledged that despite its best efforts when designing the demand ratchet during the last rate case, some FPAA customers were inordinately harmed. Speaking of the previous rate case, UNSE witness Craig Jones stated:

> I believe when we changed the rates in the last case, we identified almost 80 percent of the customers in that class actually were either neutral or took a benefit of the rate design. There were 20 percent or so that were not benefiting from the rate design. And obviously, the customers you're referencing fell in that 20 percent.[9]

Considering their importance to UNSE's customer base and the greater Nogales economy, FPAA is asking that UNSE, or the Commission, take affirmative steps to correct the inordinate impacts FPAA members have experienced. As pointed out throughout these proceedings, there are models for fairly treating large

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[7] Hearing Transcript, p. 2420, line 4—p. 2421, line 11.
[8] *Id,* p. 2436, line 13-16.
[9] Hearing Transcript, p. 2054, lines 17-13.

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counter-seasonal customers such as those FPAA represents. Texas has created a minimum load-factor threshold for industries such as the seasonal produce industry, below which demand ratchets cannot be applied. FPAA sees no reason why a similar approach could not work in Arizona.

On cross examination by Judge Rodda, UNSE witness Craig Jones was asked about FPAA's concerns and whether the Company had considered different rate relief options for them:

> Q. If we take as true their statements about how important they are to Santa Cruz County, and I do know Santa Cruz County is tough. It's a tough place right now. And I think the company is cognizant of that and wants to help with your economic development rider.
>
> A. You're absolutely right.
>
> Q. So can they be a separate class and treated somehow differently than other large users?
>
> A. Absolutely. And to your comments, yes, we are very sympathetic to that class. We would like to do what we can. . . . That is absolutely an option, as you mention. We had chosen not to do that because there are a lot of subgroubs that would like to have their own special rate.
>
> I think we have all the – I believe – I think I can say this. We have the intent of trying to do something to help alleviate their concerns. It does – it may or may not ultimately result in a cost being shifted to another class if we can get creative enough to accommodate some of the concerns they have and not result in a cost shift. Obviously, that would be the preferred method.
>
> But yes, we would be very much interested in dealing with – not dealing with, trying to work out an option for them.[10]

[10] *Id*, p. 2661, line 5—p. 2662, line 24.

C. Demand ratchets disincentivize investment in energy conservation technologies.

Faced with the reality of rapidly increasing energy costs, many FPAA members have looked to large solar distributed generation ("DG") installations for relief. However, because of the demand ratchet, the expected savings from solar have been greatly diminished. Normal residential solar customers have the benefit of accumulating net-meting credits during the off-peak winter months, which are then used to help offset higher on-peak summertime power bills. However, counter-seasonal users like FPAA members lose out on that benefit because the credits they accumulate during their non-operating summer months are swept or reset, per Commission rule, right when their operations are beginning to ramp up again in the fall. Thus, FPAA members have to hope that their solar installations will provide a net savings to them during the winter, either by reducing their real-time energy costs or by reducing their demand. In many instances, solar does neither.

On cross-examination, UNSE witness Craig Jones was asked about the interplay between energy charges and demand charges as it relates the practicality of commercial scale DG installations for customers like FPAA members:

> Q. Now I'm certainly not a solar expert, and there's plenty of people in this room who could correct me if I'm wrong. But what I'm told is that, at least for commercial scale solar, due to the low fuel prices today, the monthly lease charges that those commercial users are being charged is roughly equivalent to what the energy costs would have been charged by the utility. Do you have any reason to dispute that?
>
> A. I honestly could not dispute or support it
>
> Q. And that's fine. If that is true, someone investing in solar would have to hope for some benefit, not on the energy side of the equation, but more on the demand side of the equation, correct?
>
> A. To what end?

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Q. If you're not going to save on the energy costs on the bill because essentially you're paying the same amount of money towards your lease that you would have been paying towards the company, you would have to hope that the solar panels reduce somehow your demand and save you on that side of the equation, correct?

A. I guess it depends on what your end goal is in installing solar.

Q. Would you agree that the end goal for most would be to save money, right? If that was your end goal, I should say. Some may have other goals. If your end goal was to save money for your commercial facility?

A. There are a couple of assumptions in there you would have to make. I mean if in fact it did offset – if the cost of the lease, assuming that was a reasonable price to begin with, is actually such that the energy savings negated and nothing more, and your end goal would have been to actually create savings, then doing something to mitigate any demand charges would be your next option.

Q. Okay. So under that framework, if your demand for the company, for the user ultimately fell outside of the window or your peak demand fell outside of the window when solar was peaking or most productive, say at 6:00 p.m., the sun has practically gone down, and you're subjected to a demand ratchet, essentially that solar wouldn't provide you much benefit on the demand side either, would it?

A. It depends on what other actions you took in combination with the solar. Solar itself may not.[11]

For a residential DG customer, the negative impact of an untimely peak in demand will only be felt for one month, at which point their demand calculation is reset. For FPAA members, however, the demand ratchet continues to inflict the pain of an untimely spike in demand for an entire year! And since demand charges make up such a large portion of FPAA member bills, the pain can be substantial. Even if FPAA members invest in demand side management equipment to help mitigate costly spikes in demand, they won't be able to realize any benefit from that investment for another 12 months—assuming no unusual

[11] Hearing Transcript, p. 2682, line 22—p. 2684, line 15.

operational conditions or system events force them to bypass that equipment thus pushing the timeline out further.

At hearing, UNSE expert witness Dr. Edwin Overcast gave a perfect example of how a large commercial customer may fail to realize the benefit of investing in energy conservation measures. He spoke of a tennis facility whose owner was very disappointed when he installed skylights on the facility but failed to see the anticipated savings on his bill. Dr. Overcast told the owner that he had failed to "recognize there was a demand charge in there, and [he] made the wrong decision."[12]

E. UNSE's Economic Development Rider should be flexible enough to include FPAA members.

UNSE has proposed an Economic Development Rider ("EDR") that would provide discounts to new and existing customers that produce large numbers of jobs, with the goal of strengthening the overall health of the UNSE service territory. A 2013 study published by the University of Arizona found that for every 100 direct produce import jobs in Nogales, 52 secondary jobs a generated in the local economy. [13] Yet because FPAA members typically only reach a load factor of 45 percent, even during their peak operating periods, they would not qualify for the EDR as proposed, which requires a load-factor of 75 percent. UNSE has expressed some willingness to modify its EDR proposal to try to accommodate FPAA members. We encourage the Company to continue to explore that option.

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[12] Hearing Transcript, p. 1416, lines 5—p. 1417, line 2.

[13] *See* https://ag.arizona.edu/arec/publication/fresh-product-and-production-sharing-foundations-and-opportunities-nogales-and-santa

IV. CONCLUSION

FPAA recognizes and appreciates the concerns that have been expressed by UNSE for the impacts our members have experienced since the last rate case. We welcome any and all efforts to mitigate those impacts going forward. FPAA has provided UNSE with a list of all identifiable produce coolers in the Nogales area, in order to help UNSE better evaluate those mitigation options. Whether UNSE elects to treat FPAA members as a distinct rate class, offer FPAA economic incentives, eliminate the ratchet based on load-factor measurements, or otherwise modify the demand ratchet in some manner to more equitably reflect FPAA member contributions to the overall system peak, FPAA will continue to work with UNSE to consider all reasonable options. The health of UNSE's southern service territory and the greater Santa Cruz County depend on it.

DATED this 25th day of April, 2016.

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