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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

- DOUG LITTLE – Chairman
- BOB STUMP
- BOB BURNS
- TOM FORESE
- ANDY TOBIN

AZ CORP COMMISSION  
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION  
OF TUCSON ELECTRIC POWER  
COMPANY FOR APPROVAL OF ITS 2016  
RENEWABLE ENERGY STANDARD AND  
TARIFF IMPLEMENTATION PLAN

DOCKET NO. E-01933A-15-0239

IN THE MATTER OF THE APPLICATION  
OF TUCSON ELECTRIC POWER  
COMPANY 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 TUCSON ELECTRIC POWER  
COMPANY DEVOTED TO ITS  
OPERATIONS THROUGHOUT THE  
STATE OF ARIZONA AND FOR  
RELATED APPROVALS.

DOCKET NO. E-01933A-15-0322

**NOTICE OF FILING REPLY  
BRIEF ON BEHALF OF  
FREEPORT MINERALS  
CORPORATION AND  
ARIZONANS FOR ELECTRIC  
CHOICE AND COMPETITION**

Arizona Corporation Commission  
**DOCKETED**

JUN 24 2016

DOCKETED BY *YK*

**REPLY BRIEF**  
  
OF FREEPORT MINERALS COMPANY AND  
  
ARIZONANS FOR ELECTRIC CHOICE AND COMPETITION  
  
REGARDING TEP 2016 REST IMPLEMENTATION PLAN

JUNE 24, 2016

1 Freeport Minerals Corporation and Arizonans for Electric Choice and Competition  
2 (collectively “AECC”) hereby submit their Reply Brief in the above captioned Docket  
3 relating to the 2016 Renewable Energy Standard and Tariff (“REST”) Implementation  
4 Plan.

### 5 INTRODUCTION

6 In its Initial Post-Hearing Brief, Tucson Electric Power Company (“TEP” or  
7 “Company”) characterizes the very narrow issue before the Arizona Corporation  
8 Commission (“Commission”), coincident with approval of the Company’s 2016  
9 Renewable Energy Standard Tariff (“REST”) Implementation Plan, as one of **customer**  
10 **choice**.<sup>1</sup> In supporting its request to expand the Company’s existing TEP-Owned Rooftop  
11 Solar (“TORS”) program, as well as to introduce a new Residential Community Solar  
12 (“RCS”) program, TEP states that “Customers should have the choice to select the offering  
13 that best suits them.”<sup>2</sup>

14 In its Opening Brief, Staff offers comments concerning the interplay between  
15 A.R.S. §40-202(B), the Commission and the Retail Electric Competition Rules (“Rules”).<sup>3</sup>  
16 Staff suggests that these Rules are “an incomplete and out of date scheme that was intended  
17 as a transition, and was never implemented” despite the Arizona Court of Appeals ruling in  
18 *Phelps Dodge v. Arizona Elec. Power Coop.*, 207 Ariz. 95, 83 P3d 573 (App.  
19 2004)(“*Phelps Dodge*”) that the Rules “are workable and can therefore continue to exist  
20 intact.”<sup>4</sup> In fact, the Arizona Court of Appeals remanded to the Commission previous  
21 decisions and orders promulgating A.A.C. R14-2-1603, 1605, 1609(A) –(B), 1612, 1614,  
22 1615(B) and 1617 with “instructions to submit these rules to the attorney general for  
23 review under A.R.S. §41-1044(B).” AECC contends that if the Rules are “incomplete” or

24 \_\_\_\_\_  
25 <sup>1</sup> TEP Initial Post-Hearing Brief (“TEP Brief”) at 2.

26 <sup>2</sup> *Id.*

<sup>3</sup> A.A.C. R14-2-1601 *et seq.*

<sup>4</sup> *Phelps Dodge* at 95, 11, 587, 589.

1 “out of date,” – which they are not – it is because of the Commission’s own failure to  
2 follow the Arizona Court of Appeals mandate on remand.

3 AECC’s concerns are twofold:

4 (i) a Commission determination of whether adoption of TEP’s expanded TORS or  
5 newly crafted RCS programs (which TEP argues provide customers with more choice and  
6 greater cost savings) are in the public interest *should not be made* without considering other  
7 customer choice offerings in TEP’s rate application, such as full customer choice or, in the  
8 alternative, a proposed buy-through option for large customers similar to the AG-1 tariff  
9 approved for Arizona Public Service Company (“APS”); and

10 (ii) the Commission should refrain from making any substantive determination as to  
11 the current state of the Rules and role of competitive markets in the sale and purchase of  
12 electricity within the state of Arizona, based on the scope of this proceeding and its impact  
13 on TEP’s 2016 REST Implementation Plan and rate application.

14 In light of these concerns, AECC believes that it is appropriate to submit this Reply  
15 Brief to respond to the issues raised by TEP and Staff in their Initial Post-Hearing and  
16 Opening Briefs respectively.

## 17 DISCUSSION

### 18 I. Procedural Issue

19 AECC is delighted that TEP supports programs that encourage customer choice and  
20 the opportunity for ratepayers to receive like services – at a lower cost.<sup>5</sup> AECC notes,  
21 however, that TEP is willing to allow cost shifts to other ratepayers in order to benefit the  
22 limited few taking advantage of the TORS and RCS subsidies, and it would be wholly  
23 appropriate for the Company to take the same view towards opportunities that might  
24 benefit its commercial and industrial customers, which are already subsidizing rates.

25  
26 

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<sup>5</sup> TEP Brief at 2.

1 Although these programs are being considered within the context of TEP's 2016 REST  
2 Implementation Plan, the larger policy issues concerning customer choice and competition  
3 are nonetheless the same as they are in the rate case proceeding.

4 AECC does not agree that the Commission can make a fully informed choice  
5 whether adopting these programs will serve the public interest without weighing their costs  
6 and overall impact within the broader scope of the rate case. TORS and RCS do not  
7 represent the only programs designed to offer customers choice in generation in a  
8 competitive market; AECC supports full retail competition<sup>6</sup>, and in the alternative, the  
9 adoption of a buy-through tariff (similar to APS' AG-1 tariff) that would provide larger  
10 customers with choice and an opportunity to reduce power costs.

11 In determining whether such a buy-through program serves the public interest, the  
12 Commission will weigh evidence concerning, among other things, the cost of the buy-  
13 through program and potential impact to the Company and other ratepayers. The  
14 Commission will then weigh this evidence against other competing interests in adopting a  
15 rate design and revenue requirement that produces just and reasonable rates for all classes  
16 of customers. An expanded TORS and new RCS program should go through no less of a  
17 review. Whether these programs are in the public interest should be considered within the  
18 overall context of TEP's rate application, especially since TEP intends to include these  
19 competitive solar generation assets in rate base.<sup>7</sup>

20 AECC strongly urges the Commission not to decide these issues until a full record  
21 can be made about the potential rate impacts that an expanded TORS program, and new  
22 RCS program, will have on TEP and its customers before determining whether adoption of  
23 either program is in the public interest.

---

25 <sup>6</sup> Full retail competition would allow customers to not only purchase or lease solar DG products, but a wide variety of  
26 offerings that cater to that specific customer's preferences (i.e. renewable energy) and needs.

<sup>7</sup> TEP Brief at 7-8.

1     **II.     Choice and Competition**

2             Staff addresses the issue of choice and competition in electric generation, which the  
3     Arizona Legislature has declared is the public policy of the state of Arizona.<sup>8</sup> While AECC  
4     does not believe that this proceeding is the correct forum to address these issues, AECC  
5     nonetheless is concerned by the positions taken by Staff and must respond in order to  
6     preserve its rights. Accordingly, AECC incorporates the July 15, 2013 and August 16,  
7     2013 briefs filed in Docket No. E-00000W-13-0135<sup>9</sup>, attached hereto as Exhibit A.

8             In her May 23, 2013 letter to interested stakeholders, attached hereto as Exhibit B,  
9     Executive Director Jodi Jerich set forth eighteen (18) questions about retail electric  
10    competition, noting that “It is clear that the Commission must undertake a rigorous  
11    examination of the complex issues surrounding electric retail competition in order to reach  
12    an informed choice.” Ms. Jerich also indicated that “The Commission plans to take the  
13    material filed in the above referenced generic docket and consider it at an upcoming **Open**  
14    **Meeting.**” [Emphasis added].

15            Several stakeholders, including AECC, spent considerable time, resources and  
16    expense to address the questions and issues raised in Ms. Jerich’s letter. Unfortunately, the  
17    Open Meeting and full vetting of issues promised to interested stakeholders never came to  
18    pass. During a September 11, 2013 Staff meeting, the Commission’s legal division opined  
19    that there were threshold constitutional impediments to moving towards a competitive  
20    market in generation based on *Phelps Dodge*. As a result, Ms Jerich was directed to  
21    administratively close the generic docket. AECC contended then, as it does now, that the  
22    Commission legal division’s conclusion that the *Phelps Dodge* decision prohibits the use of  
23    market-based rates is in error.

24  
25            

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<sup>8</sup> A.R.S. §40-202(B).

26            <sup>9</sup> Generic Docket No. E-00000W-13-0135, *In the Matter of the Commission’s Inquiry into Retail Electric Competition*

1 Had the Commission continued its inquiry into retail electric competition, then  
2 questions surrounding the state of the Rules and applicability of A.R.S. §40-202(B) would  
3 be answered, thus avoiding the speculation and uncertainty that continues to plague the  
4 Commission and interested stakeholders when addressing issues such as the ones presented  
5 in this proceeding. As such, AECC urges the Commission to re-open generic docket E-  
6 00000W-13-0135 so that a determination can be made as to the state of the Rules and  
7 whether choice and competition can move forward.

8 RESPECTFULLY SUBMITTED this 24<sup>th</sup> day of June, 2016.

9 FENNEMORE CRAIG, P.C.

10  
11 By: 

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18 **ORIGINAL** and 13 copies filed  
19 this 24<sup>th</sup> day of June, 2016 with:

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24 **COPY** of the foregoing hand-delivered/mailed  
25 This 24<sup>th</sup> day of June, 2016 to:

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21 this 24<sup>th</sup> day of June, 2016 to  
22 Parties of Record:

23 By:   
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**EXHIBIT A**

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11 and Arizonans for Electric Choice and Competition

DOCKETED BY nr

BEFORE THE ARIZONA CORPORATION COMMISSION

12 IN THE MATTER OF THE  
13 COMMISSION'S INQUIRY INTO RETAIL  
14 ELECTRIC COMPETITION

DOCKET NO. E-00000W-13-0135

**FREEPORT-MCMORAN COPPER &  
GOLD INC. AND ARIZONANS FOR  
ELECTRIC CHOICE AND  
COMPETITION INITIAL COMMENTS  
AND RESPONSE TO STAFF'S MAY 23,  
2013 LETTER CONCERNING  
ELECTRIC RETAIL COMPETITION**

15  
16 Freeport-McMoRan Copper & Gold, Inc. and Arizonans for Electric Choice and  
17 Competition (collectively, "AECC") hereby submit these Initial Comments and Response  
18 to Staff's May 23, 2013 letter concerning retail electric competition.

INTRODUCTION

19  
20 The adoption of the rules which implemented retail electric competition in the State  
21 of Arizona involved a long, deliberate and well-considered process. The Arizona  
22 Corporation Commission ("Commission") first opened an investigation into retail electric  
23 competition in 1994. The first version of the Retail Electric Competition Rules ("Rules")  
24 was adopted by the Commission in 1996, and thereafter modified a number of times until  
25 the current version finalized by the Commission in 1999.

26 Concurrently with the adoption of the Rules by the Commission, the Arizona

1 Legislature passed legislation which provided that: "It is the public policy of this State  
2 that a competitive market shall exist in the sale of electric generation service." The  
3 Legislature confirmed the Commission's authority to "transition to competition for  
4 electric generation service" and set forth certain conditions relating to the transition  
5 (A.R.S. § 40-202(B)). The Arizona Legislature also passed legislation in 1998 which  
6 enabled public power entities, such as the Salt River Project ("SRP"), to transition to  
7 competition in electric generation service (A.R.S. §§ 30-801 and 30-813 "Electric Power  
8 Competition").

9 Adoption of the Rules by the Commission resulted in immediate rate decreases for  
10 investors-owned utility ("IOU") customers. The IOU rate decreases were negotiated in  
11 tandem with the adoption of direct access. SRP customers also received a decrease in  
12 rates during the period in which the Rules were adopted. During the years 1999 and 2000,  
13 approximately fifteen entities known as electric service providers, or ESP's, received  
14 Certificates of Convenience and Necessity ("CC&N") to provide competitive electric  
15 service, meter services and/or meter reading services.

16 On September 10, 2002, the Commission issued an Order commonly referred to as  
17 the "Track A Order" (Decision No. 65154). This Order reversed the requirement of the  
18 Rules that the affected utilities ("Arizona Public Service Company, Tucson Electric Power  
19 Company, UNS Electric Company, Arizona Electric Power Cooperative and various other  
20 Electric Cooperatives") ("Affected Utilities") divest their generation assets, and  
21 suspended the requirement that provided for the affected utilities to purchase all of their  
22 power in the competitive market.

23 In 2004, the Arizona Court of Appeals issued a decision commonly referred to as  
24 the "Phelps Dodge" Decision. (*Phelps Dodge v. Ariz. Elec. Power Coop.*, 207 Ariz 95, 83  
25 P.3d 573 (App.2004)). Although the Court in *Phelps Dodge* held that a provision in the  
26 Rules relating to the setting of rates (A.A.C. §14-2-1611(A)) was unconstitutional, the

1 Court stated that “The remaining Rules, however, can be applied in a manner consistent  
2 with the Constitution.” *Id.* at 109, 587. In addition, the Court determined that the Rules  
3 were independent of the unconstitutional provision and were “enforceable standing  
4 alone”. *Id.* at 110, 588. The Court severed the provision and left the remaining Rules  
5 intact, stating that “the remaining Rules are workable and can therefore continue to exist  
6 intact”. *Id.* at 111. 589. The Court expressed concern with some other provisions of the  
7 Rules, which concerns are discussed more fully in AECC’s answers to the Commission  
8 Staff’s questions. Subsequent to the adoption of the Rules by the Commission in 1999,  
9 hearings were held for the recovery of stranded costs by the Affected Utilities. Affected  
10 Utilities were permitted to, and have recovered, stranded costs resulting from the  
11 implementation of retail electric competition in Arizona.

12 Currently, retail electric competition is available in seventeen (17) States and the  
13 District of Columbia. These jurisdictions account for over forty percent of all electricity  
14 consumption in the United States. Experience of those jurisdictions with competitive  
15 markets demonstrates the following reasons customers support retail electric competition:  
16 (i) the rising cost of electricity; (ii) a greater selection of providers; (iii) more  
17 choices in energy service offerings and a more diverse fuel supply including  
18 renewable energy options; (iv) the means to better manage their electricity costs, and for  
19 ways to decrease the amount of power and thereby reduce the cost of electricity; (v) real-  
20 time control of electricity consumption through smart meters; (vi) more pricing plans;  
21 and (vii) newer and better products and services as demonstrated by the deregulation of  
22 telecommunications terminal equipment.

23 In addressing the questions posed by Commission Staff on May 23, 2013, AECC’s  
24 response will demonstrate how and why retail electric competition will provide benefits  
25 for all classes of electricity consumers.

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**RESPONSES TO QUESTIONS POSED BY STAFF**

1. **Will retail electric competition reduce rates for all classes of customers – residential, small businesses, large business and industrial classes?**

**Response:** In general, retail competition will place downward pressure on electricity prices as customers gain access to lower-cost power supplies. This is evident from the success of APS’s AG-1 program for commercial and industrial customers, in which customers have made cost-saving power arrangements with competitive suppliers. The extent to which individual customer classes will experience lower rates with the introduction of retail competition will depend, in part, on the extent of cross-subsidization in regulated rates. That is, subsidy-paying classes that pay rates above cost of service will likely experience a greater potential for savings, whereas subsidy-receiving classes will have less potential for savings.

2. **In addition to the possibility of reduced rates, identify any and all specific benefits of retail electric competition for each customer class.**

**Response:** In addition to the possibility of lower prices, retail competition will expand the pricing *options* available to customers; that is, customers will be able to choose from a spectrum of fixed-price and variable-price options, in which the latter moves as market prices change. This allows a customer to select a pricing option that best fits their risk profile. Sophisticated customers (i.e., commercial and industrial) will further be able to manage their pricing risk through hedging products. Competitive suppliers will also be able to offer customers innovative products, such as energy planning solutions, invoicing auditing and management, access to real-time meter-data, access to real-time wholesale electricity market purchasing platforms, and program management for demand response program participation. Retail competition will also allow for the provision of custom-tailored green products, in which customers can blend in a proportion of renewable energy that best meets their preferences.

1       **3. How can the benefits of competition apply to all customer classes equally**  
2       **or equitably?**

3       **Response:** Direct access service can coexist with retention of cost-based utility rates.  
4       The selection of direct access service by customers will vary by class, so participation  
5       will never be “equal.” However, the benefits can be equitable by permitting customers  
6       from every customer class to participate. Further, residential participation can be  
7       enhanced by allowing for municipal aggregation, in which local governments act as  
8       load aggregators on behalf of their residents. Forms of municipal aggregation are  
9       permitted in Ohio, California, Illinois, Massachusetts, and New Jersey.

10       **4. Please identify the risk of retail electric competition to residential**  
11       **ratepayers and to the other customer classes. What entity, if any, would be**  
12       **the provider of last resort?**

13       **Response:** The degree of risk of introducing retail competition would depend in part  
14       on the model selected. While AECC is open to the investigation of a wide range of  
15       models, AECC has consistently advocated a model in which there would be little  
16       downside risk to reinstating direct access service in Arizona. For example, AECC is  
17       not proposing that the Commission abandon current cost-of-service regulation. No  
18       customer would be forced from cost-of-service rates over which the Commission  
19       would still assert jurisdiction. Under AECC’s recommended approach, customers  
20       would simply have an alternative option for obtaining generation supply through direct  
21       access service. Because utility service would remain intact under this approach, the  
22       incumbent utilities would remain providers of last resort. This is a very low-risk  
23       proposition.

24       **5. How can the Commission guarantee that there would be no market**  
25       **structure abuses and/or market manipulation in the transition to and**  
26       **implementation of retail electric competition?**

1 **Response:** Under AECC's recommended approach, cost-of-service pricing options  
2 would remain in place under the full jurisdiction of the Commission. Additionally,  
3 because ESPs will need to be approved through the issuance of competitive CC&Ns,  
4 their conduct – and prices offered – will still require Commission oversight. Finally,  
5 Affected Utilities choosing to participate in the competitive market through an affiliate  
6 will need to adhere to a strict Code of Conduct filed with the Commission and the  
7 Federal Energy Regulatory Commission ("FERC").

8 6. **What, if any, features, entities or mechanism must be in place in order for**  
9 **there to be an effective and efficient market structure for retail electric**  
10 **competition? How long will it take to implement these features, entities or**  
11 **mechanisms?**

12 **Response:** For direct access to be successful, there must be non-discriminatory access  
13 to the transmission system. Moreover, there must be a means for equitably  
14 apportioning the rights to use transmission paths that access liquid trading hubs (e.g.,  
15 Palo Verde). In most direct access states, FERC-regulated Regional Transmission  
16 Organizations ("RTOs") fulfill this role. However, FERC also requires that  
17 transmission providers outside of RTOs offer non-discriminatory access to the  
18 transmission system, a principle that applies to competitive retail providers in direct  
19 access states.

20 In the absence of an RTO, Arizona stakeholders formed – with the encouragement  
21 of the Commission – the Arizona Independent Scheduling Administrator Association  
22 ("AZISA"), which is a FERC-jurisdictional entity charged with supporting the  
23 provision of comparable, non-discriminatory retail access to the Arizona transmission  
24 system, and to facilitate a robust and efficient competitive electric market in Arizona.  
25 AZISA's FERC-approved Phase 1 protocols govern the allocation of the first 300 MW  
26 of direct access service.

1 If and when direct access service exceeds 300 MW, the AZISA would need to file  
2 Phase 2 protocols with FERC, along with a business plan covering all AZISA  
3 activities, including monthly Allocated Retail Network Transmission ("ARNT")  
4 auction mechanism, Must Run Generation Procedures and an energy imbalance  
5 trading mechanism. In recent Board meetings, AZISA members have generally agreed  
6 that the AZISA can incorporate present Western Electricity Coordinating Council  
7 ("WECC") practices and requirements regarding scheduling and delivery of retail  
8 competitors' power, and that the AZISA must focus on transmission allocation issues.  
9 FERC approval is required for any changes to the AZISA's Phase 1 Protocols and, as  
10 noted, any Phase 2 Protocols necessary to facilitate competitive load beyond 300 MW.  
11 Thus, while certain federal approvals are still necessary to fully implement retail  
12 competition in the state, the structure is already in place for the Commission to  
13 facilitate an expedient and smooth transition towards choice and competition.

14 7. Will retail electric competition require the divestiture of generated assets  
15 by regulated electric utilities? How would FERC regulation of these  
16 facilities be affected.

17 Response: No, the reinstatement of direct access service does not require divestiture  
18 of generation assets by regulated electric utilities. Although retail electric competition  
19 can be accompanied by required divestiture of generation assets, divestiture is not a  
20 necessary component of allowing direct access to proceed. Michigan and Oregon  
21 each permit direct access without requiring divestiture of utility assets. In both of  
22 these states direct access service coexists with state-regulated cost-based utility  
23 service.

24 8. What are the costs of the transition to retail electric competition, how  
25 should those costs be quantified, and who should bear them?  
26

1       **Response:** The costs of the transition to retail electric competition are typically placed  
2 into two general categories: “stranded” cost and compliance/implementation costs.  
3 Stranded cost generally refers to that portion of the embedded cost of utility-owned  
4 fixed generating assets that is rendered uneconomic as a result of retail competition,  
5 i.e., it is the difference between “cost” and “market.” Stranded cost has received  
6 considerable attention from the Commission in the past.

7               Stranded cost is defined in R-2-1601(40) as:

8               a. The verifiable net difference between:

9                       i. The net original cost of all the prudent jurisdictional assets and  
10                       obligations necessary to furnish electricity (such as generating plants,  
11                       purchased power contracts, fuel contracts, and regulatory assets),  
12                       acquired or entered into prior to December 26, 1996, under traditional  
13                       regulation of Affected Utilities; and

14                       ii. The market value of those assets and obligations directly  
15                       attributable to the introduction of competition under this Article;

16               b. Reasonable costs necessarily incurred by an Affected Utility to effectuate  
17               divestiture of its generation assets;

18               c. Reasonable employee severance and retraining costs necessitated by  
19               electric competition, where not otherwise provided; and

20               d. Other transition and restructuring costs as approved by the Commission  
21               as part of the Affected Utility’s Stranded Cost determination under R14-2-  
22               1607.

23       The recovery of stranded cost is addressed in R-2-1607. The factors to be considered  
24       by the Commission are spelled out in R-2-1607.E, which provides that:

25       “The Commission shall, after hearing and consideration of analyses and  
26       recommendations presented by the Affected Utilities, staff, and intervenors, determine  
      for each Affected Utility the magnitude of Stranded Cost, and appropriate Stranded  
      Cost recovery mechanisms and charges. In making its determination of mechanisms

1 and charges, the Commission shall consider at least the following factors:

- 2
- 3 1. The impact of Stranded Cost recovery on the effectiveness of competition;
- 4 2. The impact of Stranded Cost recovery on customers of the Affected Utility who
- 5 do not participate in the competitive market;
- 6 3. The impact, if any, on the Affected Utility's ability to meet debt obligations;
- 7 4. The impact of Stranded Cost recovery on prices paid by consumers who
- 8 participate in the competitive market;
- 9 5. The degree to which the Affected Utility has mitigated or offset Stranded Cost;
- 10 6. The degree to which some assets have values in excess of their book values;
- 11 7. Appropriate treatment of negative Stranded Cost;
- 12 8. The time period over which such Stranded Cost charges may be recovered. The
- 13 Commission shall limit the application of such charges to a specified time period;
- 14 9. The applicability of Stranded Cost to interruptible customers.

15  
16 Of note, R-2-1607.E (8) provides that Commission shall limit the application of  
17 such charges to a specified time period. In 1999, Arizona Public Service Company  
18 ("APS") entered a settlement agreement in Docket No. E-01345A-98-0473 at al,  
19 approved with modifications by the Commission that provided for full recovery of  
20 stranded cost by December 31, 2004. In a subsequent settlement agreement approved  
21 by the Commission in Docket No. E-01345A-03-0437, APS further agreed to  
22 permanently forego any stranded cost claims associated with the West Phoenix CC-4,  
23 West Phoenix CC-5, Saguaro CT-3, Redhawk CC-1, and Redhawk CC-2 units, which  
24 came into rate base in that case. Similarly, in 1999, TEP entered a settlement  
25 agreement in Docket No. E-01933A-98-0471 et al, approved with modifications by the  
26 Commission that provided for full recovery of stranded cost by December 31, 2008.

With the passage of time and new generation investments made by utilities, it is

1 conceivable that utilities may make new stranded cost claims if direct access is  
2 reinstated. However, these potential claims would have to be resolved taking into  
3 account the prior agreements and Commission orders addressing stranded cost  
4 recovery.

5 Compliance or implementation costs refer to going-forward administrative costs  
6 associated with accommodating a direct access regime. Both APS and TEP were  
7 previously permitted to recover in rates certain specific costs to implement direct  
8 access. In a settlement agreement approved by the Commission in Docket No. E-  
9 01345A-03-0437, APS was permitted to recover \$47.7 million through a Competitive  
10 Rules Compliance Charge ("CRCC"). The CRCC was recovered over a five-year  
11 period. Similarly, in a settlement agreement approved by the Commission in Docket  
12 No. E-01933A-07-042, TEP was permitted to recover \$14.2 million through the  
13 establishment of an Implementation Cost Recovery Asset ("ICRA") to reflect TEP's  
14 costs of transitioning to retail competition. The ICRA was recovered over a period of  
15 four years.

16 Affected Utilities should be required to identify any incremental  
17 implementation costs they would seek to recover from customers if direct access is  
18 reinstated. Any allowed incremental cost recovery should take into account the costs  
19 that have already been recovered from customers for this express purpose.

20 **9. Will retail electric competition impact reliability? Why or why not?**

21 **Response:** No. There is no reason to believe that retail electric competition will  
22 impact reliability. Direct access is not new or novel, and reliable electric service has  
23 been unimpaired in other direct access jurisdictions. If customers are allowed to take  
24 direct access service, the electric grid would still continue to be operated as it is today,  
25 pursuant to reliability standards developed and enforced by the North American  
26 Electric Reliability Corporation ("NERC") and WECC. It is financial transactions

1 relating to generation service that will be different. The distribution and transmission  
2 systems will continue to be owned and operated by the incumbent utilities with no  
3 implications for changes in reliability.

4 Long-term planning can still take place pursuant to the integrated resource  
5 planning ("IRP") process. Through the IRP process, utilities can manage their  
6 exposure to direct access service by planning their long-term and short-term resource  
7 acquisitions and constructing resource portfolios in anticipation that certain levels of  
8 loads will either depart or re-enter utility service. The IRP process already takes into  
9 account uncertainties such as natural gas prices, economic conditions, environmental  
10 requirements, renewable energy targets, energy efficiency, transmission system  
11 changes, and federal policy changes. Incremental shopping load is just one more  
12 variable to be evaluated and addressed. Utility IRPs should incorporate reasonable  
13 assumptions about the level of incremental direct access load to be expected across the  
14 relevant planning horizon. The resources selected in the IRP should include products  
15 that can accommodate departing loads or to hedge against inaccuracies in load  
16 forecasts.

17 **10. What are the issues relating to balancing area authorities, transmission**  
18 **planning, and control areas which must be addressed as part of a**  
**transition to retail electric competition?**

19 **Response:** There are no major implications for balancing area authorities,  
20 transmission planning, and control areas a result of direct access, except that there  
21 would be more parties scheduling on the transmission system and a larger number of  
22 transactions requiring after-the-fact accounting. *As explained in the responses filed*  
23 *by the AZISA, the scheduling and delivery of power in a competitive retail market*  
24 *should be performed the same as any other energy transaction. Scheduling*  
25 *coordinators will schedule to the customer's balancing authority at interconnection*  
26 *schedule points. The balancing authority will deliver power and energy to the end use*

1 customer and charge FERC-approved transmission rates and ACC distribution rates,  
2 plus appropriate ancillary services. If direct access service resumes, where the power  
3 comes from may change, and scheduled paths for delivery of power may change, but  
4 in general, service to retail customers will continue in much the same manner as it is  
5 today in that the multiple control area operators that exist in Arizona will balance the  
6 system and the issue will become more focused on the cost and the accounting for the  
7 energy imbalances. If transmission paths are congested, there are mechanisms for  
8 settlement to ensure that the utilities' existing customers are not harmed by cost  
9 shifting, as required under their FERC OATT, and those of the AZISA.

10 **11. Among the states that have transitioned to retail electric competition,**  
11 **which model best promotes the public interest for Arizonans? Which**  
12 **model should be avoided?**

13 **Response:** AECC is not wedded to a specific model adopted in another state, but  
14 believes that aspects of certain models adopted elsewhere can be instructive in  
15 developing an "Arizona model." One model that may be particularly useful for  
16 Arizona, at least for an initial transition period, is the Multi-Year Opt Out program  
17 developed in Oregon for the Portland General Electric ("PGE") service territory.

18 By way of background, Oregon is a direct access state. Non-residential customers  
19 with billing demands of 30 kW or greater are eligible to shop. Oregon's incumbent  
20 utilities have *not* been required to divest their generation and each offers state-  
21 regulated cost-based bundled service to all customers. Under the direct access rules,  
22 Oregon utilities offer an annual shopping program pursuant to which customers can  
23 select direct access service for a one-year period. Shopping customers participating in  
24 this program are subject to a transition adjustment (i.e., stranded cost charge or credit)  
25 equal to the difference between cost-based generation and market prices. Because it  
26 is designed to repeatedly produce a breakeven value proposition for customers, the

1 *annual* shopping program in Oregon is not very popular and AECC does *not*  
2 recommend that it be used as a model for Arizona.

3 In contrast, the PGE Multi-Year Opt Out program was designed to offer a genuine  
4 transition to market pricing. Pursuant to this program, participants are subject to  
5 transition adjustments for five years, after which they migrate to full market pricing;  
6 that is, they are no longer subject to transition adjustments starting in Year 6 of their  
7 continuous direct access service. (Any application of transition adjustments in  
8 Arizona would need to take into account the prior resolution of stranded cost discussed  
9 above.) Participating customers must also provide advance notice (currently two years)  
10 of any intention to return to cost-based rates. To date, no participants in this program  
11 have requested to return to incumbent utility service.

12 The drawbacks of this program are that participation is limited to customers with  
13 individual site demands of at least 250 kW that can aggregate at least 1 MW of load.  
14 There is also an overall participation cap of 300 MW. These specific restrictions are  
15 negotiated components of the PGE program and need not be applied to Arizona.

16 The appeal of this program is that it provides significant notice that allows the  
17 incumbent utility to plan for the departure (and potential return) of direct access  
18 customers. At the same time, it provides a pathway to genuine market pricing for  
19 participants by establishing a terminal date for transition charges. At the same time,  
20 customers that elect to remain on Commission-regulated cost-based rates may do so.  
21 In this sense, it is a conservative approach that offers genuine customer choice, while  
22 retaining many aspects of the status quo.

23 AECC does not offer a comprehensive list of programs to be avoided, but notes that  
24 California's initial restructuring requirement that all power be purchased in a short-  
25 term market (the ill-fated California Power Exchange) was a well-documented disaster  
26 not to be repeated. AECC also discourages the Commission from adopting approaches  
that provide for open-ended stranded cost recovery, such effectively occurs in Ohio,

1 which has an active retail shopping market, but which also requires substantial non-  
2 bypassable charges paid to incumbents in the interest of "rate stability."

3  
4 **12. How have retail rates been affected in states that have implemented retail**  
5 **electric competition.**

6 **Response:** Retail electricity rates in states that have implemented direct access service  
7 have been affected not only by the transition to competition but also by factors such as  
8 changing fuel prices, transitional price caps and more. Nevertheless, many studies  
9 have evaluated the rate impacts associated with retail electric choice. As is often the  
10 case with studies that seek to isolate the effect of one of multiple variables, there are a  
11 range of conclusions. Study conclusions vary based on methodology, the geographic  
12 area studied, the study's measurement technique, and other factors. Despite the  
13 variance in conclusions, most studies have shown that implementation of retail electric  
14 choice has led to lower retail electric rates for consumers.

15 Vince Persico and Phillip Novak<sup>1</sup> recently wrote an editorial for *The Daily Herald*<sup>2</sup>  
16 in which they assess consumer savings resulting from retail electric choice in Illinois.  
17 The analysis compares Illinois's retail electric rates to the national average, both in the  
18 decade before the implementation of electric choice and in the decade following  
19 implementation of retail electric choice. The authors find that, in the decade before  
20 retail competition, Illinois consumers paid 12% more than the national average for  
21 electricity, but in the decade following restructuring Illinois retail electric prices have  
22 been 7% below the national average. The authors conclude that this price swing has  
23 saved electric consumers in Illinois \$31 billion. This analysis highlights the significant  
24 benefits attributable to retail electric choice.

25 <sup>1</sup> Vince Persico and Philip Novak were members of the Illinois House of Representatives who co-sponsored the  
26 electricity choice law in 1997.

<sup>2</sup> Vince Persico and Phillip Novak, *\$31 Billion in Benefits and Counting*, *The Daily Herald*, Dec. 27, 2012, available  
at: <http://www.dailyherald.com/article/20121227/discuss/712279988/>

1 A 2005 study by Paul Joskow<sup>3</sup> uses an econometric time-series model to estimate  
2 restructuring's effect on price. Joskow analyzed state-level retail electric price data  
3 from 1970-2003 and concludes that retail choice reduced retail electric rates by about  
4 5-10%, although his study has been criticized for not separating the price effects of  
5 competition from the effect of state-mandated price reductions, or price caps.<sup>4</sup>

6 Swadley and Yücel (2011)<sup>5</sup> addressed this criticism by performing a sophisticated  
7 econometric analysis of the effect of retail choice on retail electric rates, with a focus  
8 on the residential sector. They noted that previous studies attempting to isolate the  
9 effect of the transition to retail choice were complicated by the existence of temporary  
10 pricing schemes (such as transitional price caps). While the pricing schemes were in  
11 use their effect on rates was inseparable from the rate impact of retail choice.  
12 However, several years of data are now available following the expiration of many of  
13 these pricing schemes, allowing the authors to revisit the analysis in an attempt to  
14 isolate the rate effects of the transition to competition. They concluded that  
15 competition can reduce residential electric rates, but that increasing participating in the  
16 competitive market is a crucial element to achieving rate reductions.

17 A 2011 article published in the UCLA Undergraduate Journal of Economics<sup>6</sup> uses  
18 an econometric model to assess the effects of retail competition. It concludes that the  
19 effect of retail competition is significant and finds that, all else equal, those states with  
20 competitive retail electricity markets see electricity prices 0.6 cents/kWh below those  
21 that do not have competitive retail markets.

22 <sup>3</sup> Joskow, P. (2005). Market for Power in the United States: an Interim Assessment. *AEI-Brookings Center for  
Regulatory Studies*.

23 <sup>4</sup> See: Kwoka, J. (2008). Restructuring of the U.S. Electric Power Sector: A Review of Recent Studies. *Review of  
Industrial Organization*, 32, 165-196.

24 <sup>5</sup> Swadley, A. and Yücel, M (2011). Did residential electricity rates fall after retail competition? A dynamic panel  
analysis. *Energy Policy*. 39(12). 7701-7711.

25 <sup>6</sup> Andrews, R. (2010). Giving Customers a Choice: Examining the Effect of Retail Competition on the Electric Power  
Industry. *University of California, Los Angeles Undergraduate Journal of Economics*. 1 (2). Available at:  
26 <http://www.uclaeconjournal.com/issues/w10/2.pdf>

1           These and other studies showing significant benefits to retail competition are  
2 encouraging. Yet irrespective of the study results from other states, an Arizona  
3 approach that provides customers with an opportunity to shop, while retaining cost-  
4 based utility service under Commission jurisdiction, will place downward pressure on  
5 rates, as utilities experience an added incentive to operate efficiently. Customers  
6 should have the ability to save money from shopping if they so choose, while  
7 customers preferring to remain on utility service should also be free to do so.

8           **13. Is retail electric competition viable in light of the Court of Appeals decision**  
9 **in *Phelps Dodge Corp. v. Ariz. Elec. Power Coop.*, 207 Ariz. 95, 83 P.3d 573**  
10 **(App. 2004)? Are there other legal impediments to the transition to and/or**  
11 **implementation of retail electric competition.**

12           **Response:** The Court of Appeal's holding in the *Phelps Dodge* case has been widely  
13 misconstrued as one finding the Rules unconstitutional. This is not the case. The  
14 court determined that only one specific rule [R14-2-1611(A)] was unconstitutional on  
15 its face because it allowed the competitive market *alone* to determine just and  
16 reasonable rates.

17           **A. Market Rates**

18           R14-2-1611(A) states that "Market determined rates for Competitive Services, as  
19 defined in R14-2-1601 shall be deemed to be just and reasonable." In *Phelps Dodge*,  
20 the court found R14-2-1611(A) unconstitutional because the Commission was  
21 essentially allowing the market to exclusively set rates, thus abdicating its  
22 responsibility under Article 15, Section 3 and Section 14 of the Arizona Constitution.  
23 That responsibility includes the requirement to ascertain the fair value of an electric  
24 providers' property within the state, as well as considering the interests of consumers  
25 and providers in setting just and reasonable rates. Adhering to the precedent  
26 established by the Arizona Supreme Court in *US West Communications, Inc. v. Arizona Corp. Comm'n*, 201 Ariz. 242, 34 P.3d 351 (2001), the Court held that while

1 the Commission was required to ascertain and consider a competitive provider's fair  
2 value of property located within the state when setting rates, it retains "broad  
3 discretion in determining the weight to be given that factor in any particular case."

4 To the extent necessary, R14-2-1611(A) could be modified to provide for a range  
5 of rates. However, because the requirement to ascertain fair value is a constitutional  
6 mandate, the Commission can fulfill its duty absent a specific rule in the process of  
7 granting competitive CC&Ns to ESPs, and consider fair value as one of many factors  
8 when establishing a range of rates that a provider can charge for retail electric service.  
9 *Phelps Dodge* left intact the Commission's ability to establish a range of permissible  
10 rates.<sup>7</sup> The Court held that "Nothing in the plain language of Article 15, Section 3  
11 requires the Commission to prescribe a single rate rather than a range of rates." *Id.* at  
12 109, 587.<sup>8</sup> Indeed, the Commission has the discretion to adopt various approaches to  
13 fulfill its functions "as long as the method complies with the constitutional mandate  
14 and is not arbitrary and unreasonable." *Arizona Corp. Comm'n v. Arizona Pub. Serv.*  
15 *Co.*, 113 Ariz. 368, 371, 555 P.2d 326, 329 (1976).

15 **B. A.A.C. R14-2-1609(C)-(J); R14-2-1615(A), (C)**

16 A.A.C. R14-2-1609(C)-(J) established the requirement for Commission-regulated  
17 transmission and distribution owners in Arizona to provide non-discriminatory access  
18 to competitive electric service providers, so that they could effectively market  
19 generation services to retail consumers. The Court held that the Commission was  
20 without constitutional or legislative authority to promulgate R14-2-1609(C)-(J), and  
21 declined to infer any grant of authority for the Commission to interfere with the  
22 management decisions of Affected Utilities. However, invalidating this portion of the  
23 Rules does not render the remainder of them inoperable; open access to transmission

24  
25 <sup>7</sup> Rates for competitive telecommunication services include a range with a maximum and minimum rate. *See* A.A.C. R14-2-1109.

26 <sup>8</sup> *See* also A.R.S. §40-368, which allows the Commission to establish a sliding scale of charges and rates.

1 and distribution is a matter of federal concern regulated by the FERC.

2 FERC Orders 888 and 889 require all public utilities that own, control or operate  
3 facilities used for transmitting electric energy to file “open access non-discriminatory  
4 transmission tariffs,” as well as establishing an open access internet-based system  
5 (“OASIS”) for obtaining transmission service. Simply put, the federal scheme  
6 established by FERC to facilitate the movement of electricity among markets  
7 supplants the requirements established in R14-2-1609(C)-(J), and the need for non-  
8 discriminatory access. Furthermore, the protocols established by the AZISA on file  
9 with FERC can facilitate direct access in the absence of R14-2-1609.

10 Likewise, R14-2-1615(A) and (C) – which required Affected Utilities to divest  
11 themselves of generation assets – are not needed in order for retail electric competition  
12 to work in Arizona. In many states with competitive markets, incumbent utilities  
13 continue to own and operate generation assets as part of standard offer service.  
14 Investor-owned utilities might wish to divest themselves of generation assets in a  
15 competitive market, but doing so voluntarily is not the same as being required to by  
16 rule, which the Commission is without authority to do.<sup>9</sup> Furthermore, since *Phelps*  
17 *Dodge* upheld the validity of A.A.C. R14-2-1616 [Code of Conduct], the Rules already  
18 contain a mechanism to address market power and cross-subsidization issues in the  
19 event any investor-owned utility chooses to participate in the competitive market  
20 through a competitive affiliate.

21 C. A.A.C. R14-2-1603, 1605, 1610, 1612, 1614, 1617

22 This portion of the Rules was declared invalid simply because the Commission  
23 failed to obtain the Attorney General’s certification, as required under the APA. In  
24 fact, the court in *Phelps Dodge* was persuaded that “remand to the Commission with  
25 instructions to submit the invalid rules to the attorney general is more appropriate than  
26 vacating the entirety of the decisions approving the Rules.” In fact, the court said it

<sup>9</sup> Further, APS and TEP have been granted waivers to the invalid divestiture requirement in the Rules.

1 best when it found that “No reason appears why the Commission must repeat the  
2 process of crafting rules rather than simply allowing it to now submit the invalid  
3 provisions to the attorney general for the review required under the APA.” *Phelps*  
4 *Dodge* at 126, 604. AECC agrees, noting like the court in *Phelps Dodge* that repeating  
5 the entire process to craft rules which have already been vetted to the extent the Rules  
6 have is not necessary.

7 **14. Is retail electric competition compatible with the Commission’s Renewable**  
8 **Energy Standard that requires Arizona utilities serve at least 15% of their**  
9 **retail loads with renewable energy by 2025?**

10 **Response:** Direct access service is not incompatible with the Commission’s  
11 Renewable Energy Standard; however, modifications should probably be made to the  
12 Renewable Energy Standard to account for direct access service. AECC recommends  
13 that the Commission consider allowing an ESP the option of independently meeting  
14 this standard for its Arizona loads, in which case its direct access customers should be  
15 exempt from the RES surcharge and the applicable direct access load excluded from  
16 the “denominator” used for determining whether the incumbent utility is in compliance  
17 with the percentage requirement in the Commission’s rule. If ESPs are given the  
18 option not to meet this standard, then presumably the direct access customer would  
19 remain subject to the incumbent utility’s program, in which case some credit should be  
20 recognized for the portion of the customer’s generation service that is provided from  
21 the incumbent in the form of renewable energy.

22 **15. Is retail electric competition compatible with the Commission’s Energy**  
23 **Efficiency Standard that requires Arizona’s electric utilities to achieve a**  
24 **22% reduction in retail energy sales by consumption by 2020?**

25 **Response:** Direct access service is not incompatible with the Commission’s Energy  
26 Efficiency Standard. Direct access customers remain distribution service customers of  
the incumbent utilities that are subject to the requirements of this Rule, and therefore,

1 if the Commission wished to retain the program in its current form, it could do so  
2 irrespective of reinstating direct access service. At the same time, if the Commission  
3 is inclined to revisit the Energy Efficiency Standard, it may wish to consider the  
4 implications of direct access service, such as whether accommodation can be made for  
5 ESPs that wish to provide energy efficiency services for their customers.

6 **16. How should the Commission address net metering rates in a competitive**  
7 **market.**

8 **Response:** The subject of net metering should continue to be addressed on its merits.  
9 One of the issues of contention in the net metering discussion is whether net metering  
10 causes other customers to subsidize the program participants. To the extent such  
11 subsidies occur, they are primarily related to the provision of distribution service – a  
12 service from which direct access customers would not be exempt. If net metering is  
13 retained, the Commission may wish to consider treating any net subsidization as a  
14 distribution system cost, so as to not unfairly burden the incumbent utility or its  
15 bundled service customers.

16 **17. What impact will retail electric competition have on resource planning?**

17 **Response:** As discussed in AECC's Response to Question 9, above, long-term  
18 planning can still take place pursuant to IRP process. Through the IRP process,  
19 utilities can manage their exposure to direct access service by planning their long-term  
20 and short-term resource acquisitions and constructing resource portfolios in  
21 anticipation that certain levels of loads will either depart or re-enter utility service.  
22 Utility IRPs should incorporate reasonable assumptions about the level of incremental  
23 direct access load to be expected across the relevant planning horizon.

24 The terms of direct access service also have implications for long-term planning.  
25 For example, if migration of individual customers to 100% market prices occurs  
26 through a transition period (such as occurred in PGE's Multi-Year Opt-Out program

1 discussed in AECC's Response to Question 11) incumbent utilities have ample lead  
2 time to adjust their resource portfolios. Similarly, sufficient notice periods for  
3 customers indicating a wish to return to bundled service (e.g., three years) give  
4 incumbent utilities ample time to plan for any returning customers.

5  
6 **18. How will retail electric competition affect public power utilities,**  
**cooperatives and federal controlled transmission systems?**

7 **Response:** The Arizona Legislature passed legislation in 1998 which enabled public  
8 power entities such as SRP to transition to competition in electric generation  
9 service. (A.R.S Sections 30-801 to 30-813 – “Electric Power Competition”) A.R.S.  
10 Section 30-803 (A) provides: “Public power entities may participate in retail electric  
11 competition statewide and *shall open their entire service territories to competition to*  
12 *electricity suppliers certificated by the commission* pursuant to Section 40-207 and to  
13 providers of other services.” [Emphasis added.] Moreover, A.R.S. Section 30-802  
14 (A) further provides in part “... Public power entities and the commission shall  
15 coordinate their efforts in the transition to competition in electric generation service to  
16 promote consistent statewide application of their respective rules, procedures and  
17 orders.”

18 Thus, reinstatement of direct access by the Commission would have implications  
19 for SRP. AECC supports the reinstatement of direct access service in the SRP service  
20 territory. The Commission's current retail competition rules apply to electric power  
21 cooperatives under the Commission's jurisdiction, which are named as Affected  
22 Utilities in R14-2-1601(1). AECC recommends continuing this applicability. The  
23 reinstatement of direct access service in Arizona is unlikely to have any material  
24 implications for federally-controlled transmission systems.

24 ///

25 ///

26

1 CONCLUSION

2  
3 There are no legal or regulatory limitations to the ability of the Commission to  
4 reinstate retail electric competition, i.e. Direct Access, in Arizona at this time. As  
5 indicated above, the public interest would be served by the reinstatement of electric retail  
6 competition.

7 More importantly, there is no need for additional analysis concerning market  
8 structure, or the benefits of retail electric competition. The issues and objections raised by  
9 opponents to electric competition have been addressed numerous times in the workshops  
10 and Commission proceedings conducted over the years since the Commission opened its  
11 investigation on retail electric competition in 1994. The issues addressed during the  
12 workshops included but were not limited to, the following: (i) Stranded cost recovery; (ii)  
13 Unbundled services; (iii) Standard Offer Service; (iv) Provider of Last Resort Service; (v)  
14 Competitive meter and meter reading; (vi) Exit and return fees; (vii) Code and Conduct  
15 requirements; (viii) Establishment of an independent scheduling administrator to facilitate  
16 nondiscriminatory retail Direct Access using the transmission system in Arizona; (ix)  
17 Self-build option; and (x) Divestiture. There are therefore no workshops or formal  
18 rulemaking procedures required in order to reinstate retail electric competition in Arizona.

19 There is considerable support for electric retail competition in those States which  
20 have implemented electric competition. The Commission could proceed to reinstate retail  
21 electric competition in Arizona in either of two ways:

22 First the Commission could proceed with the processing of ESP applications for  
23 CC&Ns. The Commission has the authority to grant CC&Ns to ESPs under the  
24 provisions of A.R.S. § 40-202(B). This statute does not require a rule or regulation in  
25 order to transition to competition for electric generation service. An ESP is not precluded  
26 from obtaining a CC&N under the provisions of A.R.S. § 40-281(A). As discussed above

1 in the comments on the questions, the provisions of the rules that were invalidated did not  
2 preclude Commission authority to issue CC&Ns. In fact, the Court stated that “the  
3 remaining rules are workable and can therefore continue to exist intact” (emphasis  
4 original). *Phelps Dodge* at 95, 111, 587, 589.

5 Second, the Commission could establish a proceeding to adopt any required  
6 amendments to the Rules in order to correct the issues referenced by the Court in its  
7 Decision.

8 Its time for the Commission to reinstate retail electric competition, i.e. Direct  
9 Access in Arizona in order for the electric consumers to enjoy the same benefits and cost  
10 savings that consumers have enjoyed in other States where electric competition has been  
11 implemented.

12 RESPECTFULLY SUBMITTED this 15<sup>th</sup> day of July, 2013.

13 FENNEMORE CRAIG, P.C.

14  
15  
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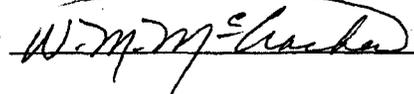
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Arizona Corporation Commission  
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**BEFORE THE ARIZONA CORPORATION COMMISSION**

IN THE MATTER OF THE  
COMMISSION'S INQUIRY INTO RETAIL  
ELECTRIC COMPETITION

DOCKET NO. E-00000W-13-0135

**FREEPORT-MCMORAN COPPER &  
GOLD INC. AND ARIZONANS FOR  
ELECTRIC CHOICE AND  
COMPETITION NOTICE OF FILING  
REPLY COMMENTS TO RESPONSES  
TO STAFF'S MAY 23, 2013 LETTER  
CONCERNING RETAIL ELECTRIC  
COMPETITION**

Freeport-McMoRan Copper & Gold, Inc. and Arizonans for Electric Choice and  
Competition (collectively, "AECC") hereby submits its Reply Comments to Responses to  
Staff's May 23, 2013 Letter Concerning Retail Electric Competition.

RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of August, 2013.

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By 

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15  
16 Freeport-McMoRan Copper & Gold, Inc. and Arizonans for Electric Choice and  
17 Competition (collectively, "AECC") hereby submit these Reply Comments to Responses  
18 to Staff's May 23, 2013 letter concerning Retail Electric Competition.

19 **INTRODUCTION**

20 In their opposition against the re-establishment of retail electric competition in  
21 Arizona, various entities, including Affected Utilities<sup>1</sup> and Salt River Project ("SRP"),  
22 raise issues that have already been thoroughly addressed by the Arizona Corporation  
23 Commission ("Commission") and interested stakeholders in numerous technical  
24 workshops and evidentiary hearings. Such issues include, but are not limited to:

25  
26 <sup>1</sup> Affected Utilities include all investor-owned utilities and electric cooperatives in Arizona. See R14-2-1601(1).

1 (1) Stranded cost recovery;<sup>2</sup> (2) Unbundled services; (3) Standard Offer Service; (4) Provider of  
2 Last Resort service; (5) Competitive meter and meter reading; (6) Independent scheduling  
3 administrator; (7) Exit and return fees; (8) Self-build options; (9) Code and Conduct  
4 requirements; and (10) Divestiture.

5 In addition, since the adoption of the Electric Competition Rules (“Rules”), the  
6 Commission has addressed in workshops or in Commission hearings the following energy  
7 and environmental issues: (1) Renewable Energy Standard Tariff and Rules; (2) Integrated  
8 Resource Planning Rules; (3) Energy Efficiency; (4) Demand-Side-Management; (5)  
9 System Benefit Charges; (6) Distributed Energy; (7) Process Standardization; (8) Net  
10 Metering; (9) Environmental risks. The resolution of these issues has not created any  
11 impediment to the reinstatement of retail electric competition in Arizona.

12 SRP estimates that addressing these issues once again would take several years.<sup>3</sup>  
13 Arizona Public Service Company (“APS”) and several electric cooperatives estimate that  
14 start up costs could run into the “hundreds of millions of dollars.”<sup>4</sup> However, these  
15 “conclusive” statements rest more on conjecture without any basis in fact. Nevertheless,  
16 Affected Utilities, SRP and their lobbyists have waged a relentless, extensive and  
17 expensive campaign (including the use of social media) to convince various civic,  
18 charitable and community organizations, in addition to several business groups and  
19 political leaders, that retail electric competition is bad for the State and Arizona  
20 consumers.<sup>5</sup>

21 Ironically SRP, who is one of the biggest opponents of competitive retail electric

---

22 <sup>2</sup> Hearings were held for the recovery of stranded costs by Affected Utilities and SRP. In addition, Affected Utilities  
23 and SRP have already recovered millions of dollars in transition costs as a result of the Commission’s first  
implementation of retail electric competition.

24 <sup>3</sup> SRP Initial Comments at 41.

25 <sup>4</sup> APS Initial Comments at 13.

26 <sup>5</sup> It is unclear why groups devoted to the development of business oppose the development of a competitive market  
in the generation of electricity. (The distribution and transmission of electricity is not subject to restructuring).

1 markets, is presently subject to retail competition pursuant to the Electric Competition  
2 Act of 1998 (“ECAct”). See A.R.S. §§ 40-202, 207, 208. The ECAct was passed as  
3 companion legislation to the Commission’s Rules, which SRP argues is outdated  
4 legislation that failed the passage of time.<sup>6</sup> Obviously, such is not the case since the  
5 ECAct has not been repealed. In fact, if the Commission were to issue a certificate of  
6 convenience and necessity (“CC&N”) to an electric service provider (“ESP”), which the  
7 Commission can do under existing authority, such ESP would have the right to compete  
8 with SRP in the provision of generation service.

9 Moreover, the Rules were left largely intact after several legal challenges and the  
10 Arizona Court of Appeals’ landmark decision in *Phelps Dodge v. Arizona Elec. Power*  
11 *Coop.*, 207 Ariz. 95, 83 P. 3d 573 (App. 2004)(“*Phelps Dodge*”). As discussed in more  
12 detail later herein, the *Phelps Dodge* case does not restrict the Commission from  
13 reinstating competitive retail electric markets. Frankly, Arizona law as currently written  
14 is structured to support competition, and much more effort would be needed to reverse  
15 the course than to complete the process by amending the Rules to address the issues  
16 raised by the *Phelps Dodge* decision, as discussed herein, so that – together with the  
17 ECAct – Arizona can move towards a competitive retail electric market.

18 Much attention has also been directed by APS and SRP to the alleged effect retail  
19 electric competition might have on coal-fired generation. There would be little change  
20 in a competitive environment provided for by the reinstatement of retail electric  
21 competition based on the historical pricing for coal. If anything, the costs of  
22 environmental retrofitting and emission control mandates by the U.S. Environmental  
23 Protection Agency (“EPA”) will push these coal units to become less economic, though  
24 by APS’ own admission, coal represents a lower-cost alternative to other traditional fuel  
25

---

26 <sup>6</sup> SRP Initial Comments at 44.

1 sources like natural gas – even when you add on environmental compliance costs.<sup>7</sup> As  
2 addressed in more detail herein, AECC will demonstrate why arguments involving EPA  
3 imposed requirements for coal-fired generation are irrelevant to the issue of retail  
4 electric competition.

5 The question must be asked; why are Affected Utilities and SRP so resistant to  
6 retail competition?<sup>8</sup> According to SRP and other parties, Arizonans currently (i) have a  
7 much better deal than most parts of the country, (ii) enjoy award-winning customer  
8 service, (iii) have low prices, (iv) can select from a wide array of price options and  
9 services, (vi) benefit from an excellent mix of generation, integrated planning and  
10 preparedness, and (viii) receive stable and reliable service.<sup>9</sup> These claims certainly set  
11 high standards for any competitor to meet. Rather than test their rates against those who  
12 wish to compete, Affected Utilities would rather keep the status quo of a captive  
13 customer group, pass-through surcharges and traditional rate of return regulation.  
14 Likewise, SRP (which is unregulated as to rates, charges or service) enjoys the benefit of  
15 a captive customer base, which only the Commission can take away at this time through  
16 the issuance of competitive CC&Ns to ESPs.

17 Through an extensive public campaign, Affected Utilities and SRP have  
18 orchestrated, to bring pressure to bear on members of the Commission to not even  
19 consider the matter on its merits, beyond stakeholders' written comments, or any  
20 competing claims.

21  
22 <sup>7</sup> Docket No. E-01345A-10-0474; APS Application at 25.

23 <sup>8</sup> In testimony on HB 2663 [Electric Power Competition] before the House Committee on Government Operations,  
24 then SRP Chairman Richard Silverman stated the following: "...I want to compliment the Committee first on your  
25 efforts to bring competition to the State along with the other speakers. It is a critical issue but it is incredibly  
26 important that we ensure that our customers receive the benefits of competition. Some two years ago, the publicly  
elected Board of Directors of SRP adopted a plan for competition, the first point we embrace it, it is what our  
customers want and the best thing we can do for them..." February 20, 1998.

<sup>9</sup> SRP Initial Comments at 6.

1 AECC urges the Commission to take the time necessary to address the question  
2 of whether retail electric competition is in the public interest and will benefit Arizona  
3 consumers.

## 4 DISCUSSION

### 5 I. The Phelps Dodge Decision.

#### 6 A. Legal Principles

7 The *Phelps Dodge* decision stands for the following legal principles:

- 8 1. Even though Rule R14-2-1611(A), which allowed the market alone to  
9 determine rates, was declared unconstitutional, **the remaining rules can**  
10 **be applied in a manner consistent with the Constitution.**
  - 11 a. Even though R14-2-1611(A) is invalid under the Constitution, **the**  
12 **remaining rules are workable and can therefore continue to**  
13 **exist.**
  - 14 b. **The Rules are independent of R14-2-1611(A) and are**  
15 **enforceable standing alone.**
  - 16 c. **The invalid portion of the Rules can be severed with the**  
17 **remaining Rules intact and enforceable.**
- 18 2. The fair value provision in the Constitution is **self-executing** as it  
19 affirmatively requires the Commission to determine fair value in setting  
20 rates, **and a rule is therefore not required to impose this requirement.**
- 21 3. No rule specifically requires the Commission to determine and consider  
22 the fair value and that omission does not invalidate the Rules.
- 23 4. The Rules empower the Commission to gather sufficient information to  
24 make the fair value determination.
- 25 5. **Nothing in the Constitution requires the Commission to prescribe a**  
26 **single rate rather than a range of rates.**
6. Assuming the Commission establishes a range of rates that is just and  
reasonable, **the Commission does not violate the Constitution by**  
**permitting competitive market forces to set specific rates within that**  
**approved range.**

1                   7.     The APA does not require the Commission to conduct any evidentiary  
2                   hearings before promulgating the Rules.

3                   B.     Constitutionality

4                   The provisions of the *Phelps Dodge* decision, and arguments used by opponents to  
5                   conclude that retail electric competition is contrary to Arizona law, can be summarized as  
6                   follows:

- 7                   1.     The setting of rates requires a determination of fair value;  
8                   2.     The Commission cannot set a broad range of rates within which the  
9                   competitive market place can operate;  
10                  3.     Mandatory divestiture is unconstitutional;  
11                  4.     The Commission has no authority to require affected utilities to  
12                  participate in the AzISA; and  
13                  5.     Certain portions of the Rules required certification by the Attorney  
14                  General.

15                  C.     Analysis of Fair Value Finding Requirement

16                  Grand Canyon State Electric Cooperative Association (“Co-ops”) and Arizona  
17                  Investment Council (“AIC”) argue that the Commission is required to find fair value and  
18                  use fair value in setting rates.<sup>10</sup> Implicit in their argument is a requirement that the  
19                  Commission must set the rate on the basis of the fair value finding. This argument  
20                  ignores specific language in the *Phelps Dodge* decision, which states:

21                                 “...the Commission should consider fair value when setting  
22                                 rates within a competitive market, although the Commission  
23                                 has **broad discretion in determining the weight to be given**  
24                                 that factor in any particular case...”<sup>11</sup> [Emphasis added]

25                                 <sup>10</sup> See Initial Comments – Exhibit A at 2.

26                                 <sup>11</sup> *Phelps Dodge* at 207 Ariz. 95, 105, 83 P. 3d 573, 585.

1 Moreover, “the fair value provision in the Constitution is self-executing” and “a Rule is  
2 not required to impose the requirement.” In fact, the court found that “The Rules  
3 empower the Commission to gather sufficient information to make the fair value  
4 determination.”<sup>12</sup>

5 By focusing on the constitutional requirement for the Commission to make a fair  
6 value determination, the Co-ops and AIC erroneously conclude that “fair value  
7 ratemaking is inherently antithetical to the concept of rates established by a competitive  
8 market.” This position ignores the power of the Commission to consider fair value at  
9 the time it considers an ESP’s application for a CC&N, yet use its broad discretion in  
10 determining what weight fair value should be given “when setting rates within a  
11 competitive market.”

12 D. Range of Rates

13 In order to support their conclusion, the Co-ops and AIC are forced to argue that  
14 the Commission cannot set a “broad” range of rates within which the competitive market  
15 place can operate.<sup>13</sup> Although the *Phelps Dodge* case did not define the word “broad”,  
16 the Co-ops and AIC have defined the word to mean “open-ended.”<sup>14</sup> There is no  
17 discussion in the *Phelps Dodge* decision of an open-ended rate. The decision does,  
18 however, state that the Commission may establish a range of rates in setting just and  
19 reasonable rates.<sup>15</sup>

20 In the *Phelps Dodge* case, the Co-ops and AIC argued that Article 15, Section 3  
21 of the Arizona Constitution required the Commission to prescribe a single rate rather  
22 than a range of rates. The Court rejected this argument, stating that:

23 \_\_\_\_\_  
24 <sup>12</sup> *Phelps Dodge* at 207 Ariz. 95, 110, 83 P. 3d 573, 588.

25 <sup>13</sup> Initial Comments, Exhibit A at 3.

26 <sup>14</sup> *Id.*

<sup>15</sup> In fact A.R.S. § 40-368 provides for a “sliding scale of charges.”

1  
2 “Nothing in the plain language of Article 15, Section 3 requires the  
3 Commission to prescribe a single rate rather than a range of rates.”

4 The Court then stated that:

5  
6 “Consequently, assuming the Commission establishes a range of  
7 rates that is “just and reasonable”, the Commission does not violate  
8 Article 15, Section 3 by permitting competitive market forces to set  
9 rates within that approved range.”<sup>16</sup>

9 The authority to prescribe a range of rates is consistent with the analysis provided by the  
10 Arizona Center for Law in the Public Interest (“ACLPI”). In reviewing the *Phelps*  
11 *Dodge* decision on the narrow issues of fair value and just and reasonable rates, ACLPI  
12 determined that:

13 “The Court held that assuming the Commission establishes a range  
14 of rates that is “just and reasonable,” the Commission does not  
15 violate Article 15, § 3 by permitting competitive market forces to set  
16 specific rates within that approved range.”<sup>17</sup>

16 E. *Monopoly Service and the Electric Competition Act of 1998*

17 SRP contends that the Arizona Constitution mandates a system of regulation, and  
18 that this is inapposite to “de-regulation.” Furthermore, SRP argues that the Electric  
19 Competition Act of 1998 (“ECAct”) is outdated and no longer applicable. SRP is  
20 incorrect on both counts.

21 First, SRP’s notion that a competitive market is antithetical to Arizona’s  
22 mandated system of regulation (just and reasonable rates) implies a regulatory scheme  
23 centered around monopolies, and completely ignores the fact that competitive forces in  
24

25 <sup>16</sup> *Phelps Dodge* at 207 Ariz. 95, 109, 83 P. 3d 573, 587

26 <sup>17</sup> See ACLPI Initial Comments at 4, ln. 1-4.

1 the telecommunications industry are already being used in Arizona to ensure just and  
2 reasonable rates. In *The Mountain States Telephone and Telegraph Company v. Arizona*  
3 *Corporation Commission*, 132 Ariz. 109, 113, 644 P.2d 263, 276, the court stated that:

4           The constitutional provision which granted this authority [to prescribe  
5 just and reasonable rates] and hence jurisdiction is silent as to any  
6 concepts of "regulated monopoly." The concept of the regulated  
7 monopoly arose from the legislature in granting the Commission the  
8 authority to issue certificates of convenience and necessity to public  
9 service corporations."

9 The Arizona Constitution does not mandate a system of regulated monopolies, but rather  
10 leaves to the Commission and Legislature the discretion to structure a regulatory system,  
11 as long as a finding of fair value is required when setting rates.<sup>18</sup> In fact, the ECAct is  
12 predicated on a system of open competition in generation (A.R.S. §40-202), and  
13 permitting electric generation service prices to be established "in a competitive market"  
14 requires the Commission to first adopt rules on retail electric competition,<sup>19</sup> and then  
15 issue individual CC&Ns to ESPs (after a finding of fair value) with the discretion to  
16 impose conditions such as a range of rates.<sup>20</sup> Finally, if the ECAct were outdated and  
17 no longer applicable as SRP suggests, then it would have been repealed years ago.

18       F.     *Rate Discrimination, Price Transparency and a Bi-furcated Market*

19       APS suggests that even if all the problems with *Phelps Dodge* are resolved, there  
20 exist a few more impediments unaddressed by the opinion; namely, rate and service  
21 discrimination (Arizona Constitution -Article 15, Section 12; A.R.S. § 40-374)<sup>21</sup>, price  
22 transparency (A.R.S. §40-367) and the potential for a bi-furcated system of regulation

23 <sup>18</sup> SRP is not subject to the same fair value finding requirement, as its Board of Directors sets SRP's rates.

24 <sup>19</sup> A.R.S. §.40-207.

25 <sup>20</sup> The Rules were found sufficient to make a fair value determination. *Phelps Dodge* at 207 Ariz. 95, 110, 83 P. 3d  
573, 588.

26 <sup>21</sup> The Co-ops makes the same argument concerning rate discrimination.

1 between APS and SRP. These arguments are without merit for the following reasons:

- 2 • Article 15, Section 12 of the Arizona Constitution prohibits  
3 discrimination in charges and rates for “like and contemporaneous  
4 service.” Offering different rates for different services and products  
5 within a range of rates does not violate this principle; otherwise, time-  
6 of-use rates and other rate classifications would be subject to the same  
7 prohibitions.
- 8 • A.R.S. § 40-374 prohibits the use of rebates and agreements, “except  
9 such as are regularly and uniformly extended to all persons and except  
10 upon order of the Commission.” Any concerns about violations of this  
11 statute can be addressed in the normal course of regulatory oversight  
12 the Commission has over public service corporations and ESPs.
- 13 • A.R.S § 40-367 prohibits a public service corporation from changing  
14 rates without notice. By establishing a permissible range of rates in a  
15 CC&N order, any change to such tariffed rate on file with the  
16 Commission would require Commission approval, as is currently the  
17 case with telecommunication companies seeking to raise or lower price  
18 caps for competitive services.

19 APS also raises the issue of a bifurcated competitive market in which APS and  
20 SRP must each provide electric service according to different rules and policies. This  
21 perspective views a Commission decision to adopt retail electric competition as taking  
22 the industry only halfway towards competition. In reality, such a Commission decision  
23 will take Arizona all the way towards competitive markets in generation, since the  
24 ECAct already allows for competition in SRP’s service territory. AECC does not  
25 consider the 1955 Territorial Agreement between APS and SRP to be an impediment to  
26 the introduction of retail electric competition, nor should the Commission.

22 G. The Rules

23 The electric competition Rules which the *Phelps Dodge* decision held to be  
24 invalid by the Court did not eliminate the remaining regulatory framework which  
25 governs Retail Electric Competition.

1           1.     As previously discussed, the Court held that Rule R14-2-1611(A)  
2 (“market determined rates”) was unconstitutional because the Commission had not  
3 taken into consideration fair value in approving rates.

4                     The Court, however, specifically found that R14-2-1611(A) could be  
5 severed from the remainder of the Rules and that “the remaining Rules,  
6 however, can be applied in a manner consistent with the Constitution.”  
7 Furthermore, the Court stated: “... we have no difficulty concluding that  
8 the Rules are independent of R14-2-1611(A) and are enforceable standing  
9 alone.”

10           2.     The Court also held that R14-2-1615(A) and (C) (involving Separation of  
11 Monopoly and Competitive Services - “divestiture”) “are aimed at controlling the  
12 Affected Utilities rather than rates and are therefore outside the Commissions plenary  
13 rulemaking authority.”

14                     However, this issue became moot because both APS and TEP applied to  
15 the Commission for a waiver of the requirements of the Rule, which the  
16 Commission granted, and the Rule was therefore never applied. In  
17 addition, the Court concluded that “... the Commission can permissibly  
18 require an Affected Utility that chooses to transfer competitive assets to  
19 an affiliate to do so at a fair and reasonable price, as determined by the  
20 Commission.”

21                     The reinstatement of retail electric competition does not require  
22 divestiture of generation assets by Affected Utilities. Divestiture is not a  
23 necessary component of allowing direct access to proceed.  
24  
25  
26

1           3.     The Court held that the provisions of R14-2-1609(C)-(J) which direct  
2 Affected Utilities to create an independent scheduling administrator and a scheduling  
3 coordinator (AzISA) to oversee fair access to transmission services were not reasonably  
4 necessary steps to ratemaking and consequently the Commission was without  
5 constitutional or legislative authority to promulgate these provisions of the Rules.  
6 However, R14-2-1609(A) which states that Affected Utilities must provide non-  
7 discriminatory open access to transmission and distribution facilities, was not  
8 challenged.<sup>22</sup> In a subsequent Commission proceeding following the *Phelps Dodge*  
9 decision involving the AzISA, the Commission stated:

10                                 “We find that Phelps Dodge had no impact on the continuing  
11 economic viability of the AISA, and that it does not reduce the  
12 continued public benefit associated with maintaining Commission  
13 support of the AISA at its current level of operations. The AISA  
14 currently provides the important public benefit of keeping the  
15 possibility of retail access available in Arizona to consumers at a  
16 minimal cost by providing potential competitors with the  
necessary assurance that they will have fair and equitable access  
to transmission until an RTO is formed and approved by FERC  
to take over that function.”<sup>23</sup>

17           Protocols established by the AzISA on file with the FERC can facilitate direct  
18 access in the absence of R14-2-1609(C)-(J). Moreover, APS’s flippant comment that the  
19 AzISA was “unlawfully created in the first instance” is simply wrong and belies APS’s own  
20 role in helping to create the organization. Efforts by Arizona stakeholders, including APS, to  
21 lawfully form the AzISA predated the adoption of the mandate in the Commission’s Rules.  
22 Moreover, APS further bound itself to development of this organization independently of R14-  
23 2-1609(C)-(J) by agreeing in its Settlement Agreement in Docket No. E-01345A-98-0473 *et al*

24 <sup>22</sup> In fact, A.R.S. 40-332(B) specifically provides that: “Every public service corporation shall allow every electricity  
25 supplier and self-generator of electricity access to electric transmission service and electric distribution service under  
26 rates and terms and conditions of service that are just and reasonable as determined and approved by regulatory  
agencies that have jurisdiction over electric transmission service and electric distribution service...”

<sup>23</sup> Decision No. 68485 at 15.

1 to "actively support the Arizona Independent Scheduling Administrator" and "to modify its  
2 OATT to be consistent with any FERC approved AISA protocols."<sup>24</sup> As demonstrated in this  
3 agreement, the AZISA was always intended to be a FERC-jurisdictional entity. APS's attempt  
4 to rewrite the history of the origins of the AzISA should be disregarded.

5 4. The Rules that were invalidated by the *Phelps Dodge* decision because  
6 they were not submitted to the Arizona Attorney General for Certification under the  
7 APA are not indispensable to the reinstatement of retail electric competition for the  
8 following reasons:

- 9 - First, most, if not all, of the subject matter covered by the Rules  
10 that were invalidated are covered by "Arizona law and the General  
11 Rules of the Commission" which are applicable to public service  
12 corporations in general, and could be applied with the  
13 reinstatement of retail electric competition;
- 14 - Second, by including any required conditions or requirements in  
15 decisions granting ESP's CC&Ns;
- 16 - Third, by submitting the invalidated Rules to the Arizona Attorney  
17 General for Certification. There is no time limit within which the  
18 Commission must submit Rules adopted by the Commission for  
19 Certification. Furthermore, the APA does not require the  
20 Commission to conduct any evidentiary hearing before  
21 promulgating rules. Hence, no further evidentiary proceeding  
22 would be required for submitting the Rules to the Attorney General  
23 in their present form.

24  
25  
26 <sup>24</sup> APS Settlement Agreement, Paragraph 7.6.

1 **II. Coal-Fired Generation**

2  
3 AECC appreciates the serious threat to Arizona, the Navajo Nation and electric  
4 consumers when it comes to coal-fired generation. However, arguments that retail  
5 electric competition will cause the closure of coal-fired units at the Navajo Generating  
6 Station (“NGS”) and Four Corners Power Plant (“FCPP”) are clearly red herrings,  
7 targeted at deflecting the primary and real threat to the continued operation of these  
8 plants – environmental mandates being implemented by the EPA.

9 A. Navajo Generating Station

10 Just a few weeks ago, SRP announced a plan to close one of three 750-megawatt  
11 generators by 2020 in order to satisfy environmental mandates being pushed by the  
12 EPA, and delay the installation of costly nitrogen oxide-reducing catalytic converters to  
13 cut emissions.<sup>25</sup> Several interested “parties” have signed onto this proposal, including  
14 entities from California facing state-imposed limitations on coal-fired generation.  
15 Nowhere was it indicated that this proposal was a result of the threat of retail electric  
16 competition. Furthermore, had this been an Affected Utility rather than SRP, the  
17 process for coming to a ‘solution’ would have been fully vetted in a public process.  
18 Who is to say this is the right solution for Arizona electric consumers? In fact, Sid  
19 Wilson, chairman of the Arizona Coalition for Water, Energy and Jobs and former  
20 general manager of the Central Arizona Project, writes:

21 “The latest “proposal” developed with activists during closed-door  
22 negotiations calls for the early shutdown of a unit and the use of \$100  
23 million in taxpayer funds from the U.S. Department of Interior to help  
24 compensate the tribes. Of course that won’t come close to replacing the  
25 loss of hundreds of jobs and hundreds of millions of dollars in revenue that  
26 are central to these economies. It does little to address higher water costs,  
the increased cost of replacement power or the dramatic economic loss we

<sup>25</sup> The Arizona Republic, Friday, July 26, 2013.

1 face. Until we fully understand the ramifications of any proposed plan on  
2 our state's water supply strategies, we should not approve or support  
3 implementation....The Navajo Generating Station must continue to operate  
4 at full capacity over the plant's full term as our early leaders envisioned.  
5 Discussions about the plant must involve all Arizonans for the benefit and  
6 the future of our state."

7 Ironically, it is government overregulation – not competition – that is responsible  
8 for the extreme pressure being placed on coal generation at the NGS. In his writing, Mr.  
9 Wilson discusses the threat that is jeopardizing Arizona's long-term water supply,  
10 stating:

11 "Today, our primary water-delivery system is facing a serious threat that  
12 jeopardizes Arizona's long-term water supply strategy. The threat comes  
13 from the U.S. Environmental Protection Agency's proposed regional haze  
14 rule that would require the Navajo Generating Station operators to install as  
15 much as \$1.1 billion in emission controls to improve Grand Canyon  
16 visibility. This will drive up energy and water costs and put thousands of  
17 jobs and tens of billions of dollars of economic activity at risk for  
18 potentially no change we will ever see."<sup>26</sup>

19 Again, it must be pointed out that the events that will result in increased electric  
20 rates, and corresponding increase in water rates, will not be the result of the  
21 reinstatement of retail electric competition, but rather, requirements imposed by the  
22 EPA.

23 B. Four Corners Power Plant

24 The threats facing the FCPP are similar to those facing the NGS. However, there  
25 appeared to be a long-term solution to the problem – until APS chose to use its pending  
26 acquisition as political leverage in this proceeding. AECC questions why APS'  
27 proposal to purchase Southern California Edison's ("SCE") ownership interests in  
28 generating Units 4 and 5 at the FCPP and retire older, less efficient generating Units 1, 2

<sup>26</sup> The Arizona Republic, 'My Turn' by Sid Wilson. August 9, 2013.

1 and 3, is not the win/win/win proposition it was in 2010, when the company sought  
2 approval from the Commission to move forward. Even in a competitive retail electric  
3 market, APS and its customers will have use for lower-cost, baseload generation. In its  
4 2010 application, APS stated among other things, that the proposal:

- 5 • saves APS customers money, providing them a nearly \$500 million net  
6 present value benefit.
- 7 • has a lower customer bill impact than that of every other likely  
8 alternative.
- 9 • significantly reduces Four Corners' regional carbon dioxide ("CO2") and  
10 other pollutant emissions by retiring three less efficient coal units and  
11 installing environmental upgrades on more efficient units.
- 12 • saves hundreds of jobs and millions of dollars of revenue that are critical  
13 to the Navajo Nation and the local economy.
- 14 • preserves the diversity of APS's current generation portfolio while  
15 tempering the Company's exposure to volatile natural gas prices.
- 16 • maintains APS' mix of reliable baseload energy. By providing a  
17 marginal 179 MW baseload capacity increase, it hedges the Company's  
18 energy mix against the possibility that output from other coal units also at  
19 risk could be retired and helps further defer the need for future baseload  
20 resources. [Emphasis added]

21 In supporting the long-term benefits of the proposal, APS stated that while Units  
22 1, 2 and 3 were cost effective now, spending a total of \$586 million in five short years to  
23 keep them online changes the math "markedly." As it was then, today's threats to the  
24 viability of the FCPP are the impact of costs to implement environmental mandates, and  
25 not retail electric competition. In reviewing the benefits of Units 4 and 5, APS provided  
26 a detailed analysis in its 2010 application demonstrating why none of the alternative

1 resources (including natural gas) were “realistically available” to fill the void if Units 4  
2 and 5 were shut down in 2016 – even with the cost of environmental control technology  
3 additions required to meet USEPA mandates. [p. 11-16]. APS argued:

4 “As discussed above, gas-fired generation, the most practical  
5 alternative to Four Corners in these circumstances, would further  
6 expose APS customers to uncertain gas prices and require that new  
7 transmission be built for any new gas-fired power to reach the  
8 Company’s primary load center in the Metropolitan Phoenix area.  
9 Moreover, as discussed in detail above, the gas generation option  
10 will likely be more expensive to APS customers in the end, even  
11 after factoring in the acquisition price and cost of SCRs and  
12 other environmental upgrades.” [Emphasis added].

11 In addition to being the lowest-cost alternative, other benefits of APS’ proposal  
12 include; (i) the continued economic benefit to the surrounding community, especially the  
13 Navajo Nation, (ii) a “cleaner” environment resulting from the retirement of inefficient  
14 Units 1, 2 and 3, and (iii) a diverse generation portfolio mix for reliability purposes.  
15 How is it, then, that retail electric competition suddenly eliminates all these benefits?

16 APS responds by stating that “with uncertain customer relationships, utilities’  
17 inability to safely invest much needed capital in coal plant emission technology would  
18 threaten the viability of existing coal plants.”<sup>27</sup> This response seems to contradict the  
19 notion that the pending proposal would secure APS its lowest cost alternative power  
20 source at this time, which obviously would impact APS profits. Furthermore, it  
21 completely ignores the other benefits of this specific proposal. AECC has been  
22 supportive of APS’s efforts to proceed with its plans at FCPP. But if the possibility of  
23 direct access causes APS to re-evaluate its options at FCPP, then perhaps that option is  
24 not as cost-effective as APS has maintained.

25 Even if it acquires SCE’s share of FCPP Units 4 and 5, APS will need over

26 <sup>27</sup> APS Initial Comments at 11.

1 545MW of new resources by the 2017 timeframe. Without the proposed transaction,  
2 APS' need for new resources could increase to over 1,500 MWs in 2017.<sup>28</sup> Whether  
3 operating in traditional regulated market or a competitive retail electric market, a  
4 demand for lower cost electricity will always ensure that generation from coal-fired  
5 facilities will continue – provided the EPA (not retail electric competition) does not  
6 overburden plant owners/operators with costly environmental mandates unlikely to make  
7 any difference in the quality of air surrounding the Grand Canyon.

### 8 **III. Divestiture**

9 Much of the critique that opponents level at direct access concerns the presumed  
10 divestiture of utility generation assets. For example, APS warns the Commission against  
11 relinquishing its jurisdiction over generation and surrendering it to FERC.<sup>29</sup> Yet direct  
12 access in no way requires such a transfer of jurisdiction. Other states, such as Oregon  
13 and Michigan, permit direct access without requiring divestiture and without having  
14 transferred state jurisdiction over utility generation assets to FERC. Such a transfer  
15 would only occur in Arizona if the Commission voluntarily and expressly ceded  
16 jurisdiction as part of an approved divestiture plan. In its Initial Comments, AECC  
17 advocated for implementation of direct access without requiring divestiture. And despite  
18 the fact that most of the concerns that APS expressed in opposition to direct access relate  
19 to divestiture and its implications, APS acknowledges that implementation of direct  
20 access will not require divestiture.<sup>30</sup> Salt River Project also acknowledges that  
21 implementation of direct access would not require divestiture.<sup>31</sup>

22 One of the legal objections raised by opponents is the unconstitutionality of  
23

24 <sup>28</sup> Docket No. E-01345A-10-0474; APS Application at p. 12.

25 <sup>29</sup> APS Initial Comments at 7-9.

26 <sup>30</sup> APS Attachment A at 11.

<sup>31</sup> SRP Initial Comments at 31.

1 mandating utility divestiture of generation assets.<sup>32</sup> This objection is rendered moot by  
2 adopting AECC's recommendation not to require divestiture as a component of re-  
3 implementing direct access service in Arizona.

4 The presumption that direct access requires divestiture extends to opponents'  
5 assertions regarding the need for Arizona's participation in an RTO as a precondition of  
6 direct access – and the litany of supposed obstacles to RTO formation in this region  
7 cited by opponents.<sup>33</sup> To be sure, opponents concede – and AECC agrees – that RTOs  
8 facilitate markets<sup>34</sup>; further, if the Commission *were* to approve a voluntary divestiture  
9 of utility generation, an RTO would play an important role in supporting wholesale  
10 competition. However, as divestiture is **not** a requirement of direct access, Arizona's  
11 participation in an RTO is also **not** a necessary condition for direct access in Arizona to  
12 proceed. As noted, in AECC's Initial Comments, Arizonans anticipated this concern  
13 and formed the AzISA specifically to address issues of ensuring retail access to the  
14 transmission system prior to – or in the absence of – an RTO.

#### 15 **IV. Pricing**

16 Opponents of direct access emphasize that average electric prices in restructured  
17 states are generally higher than in regulated states. However, this simple comparison  
18 does not account for the fact that electricity prices in the United States have always  
19 varied significantly by region and that the states with higher regulated prices tended to be  
20 the ones that turned to competitive markets for pricing relief. Thus, while the states that  
21 restructured still tend to have higher rates on average, competition is helping to close the  
22 gap with the historically-lower cost states.

23 <sup>32</sup> APS Initial Response at 15.

24 <sup>33</sup> APS Initial Comments at 12-14; SRP Initial Comments at 29-30.

25 <sup>34</sup> The Commission concluded that seams issues between California and Arizona pose challenges to major growth in  
26 renewable exports, despite FERC Order 1000, which encourages improved regional planning. Decision No. 73625 at  
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By citing to national average rate for regulated states, opponents of direct access are trying to take “credit by association” for the lower average rates nationwide among regulated jurisdictions. However, Arizona customers are not actually beneficiaries of that national average. The table on page 5 of APS’s Initial Responses demonstrates that among the 33 states with regulated rates, Arizona has the 6<sup>th</sup> highest residential rates. Indeed, as a high-cost regulated state, Arizona has more in common with the states that turned to the competitive market for relief than the states that opted to deny customers access to the market.

APS’s comments single out the competitive market experience in Texas and Illinois for especially strong criticism, painting a dire picture of each.<sup>35</sup> But one need only to examine the table on page 5 of APS’s Initial Responses to see that the retail rates of both Texas and Illinois are lower than those in Arizona. So, if the competitive customers in Texas and Illinois are suffering as much as APS contends – then customers taking regulated service in Arizona must be even worse off. Alternatively, if Arizona customers are faring as well as APS contends, the evidence shows that the competitive customers in Texas and Illinois are doing even better. What is not true, however, is the impression conveyed by opponents that the customers taking competitive service in Texas and Illinois – with their lower rates – are somehow worse off than customers in Arizona.

V. **System Reliability**

A. **Transmission**

Transmission reliability concerns should be completely unaffected by implementation of direct access, as Arizona transmission owners routinely participate in

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<sup>35</sup> APS Initial Comments at 4, APS Attachment A at 17, 24.

1 long-term transmission planning. For instance, the Southwest Area Transmission  
2 (“SWAT”)<sup>36</sup> Planning group, which is a subgroup of WestConnect, routinely assesses  
3 and develops cost-effective enhancements for wholesale market needs. In addition, the  
4 Western Electricity Coordinating Council (“WECC”), which has a delegation agreement  
5 with the North American Electric Reliability Corporation (“NERC”), oversees reliability  
6 issues on the western grid, from Canada to Mexico and the fourteen western states in  
7 between.

8 The Commission also issues a Biennial Transmission Assessment (“BTA”) every  
9 two years. In its most recent BTA (seventh), the Commission found that Arizona  
10 transmission owners have “implemented steps to address regional transmission planning  
11 issues, provide transmission enhancements and additions, develop solutions for  
12 transmission import constraints in various load pockets, support the growth of renewable  
13 resources in Arizona, and address local transmission system mitigation measures where  
14 needed.”<sup>37</sup>

15 Given this conclusion, it should be clear that even in the absence of a Regional  
16 Transmission Organization (“RTO”), the AzISA can facilitate the development of a  
17 competitive retail electric market without a negative impact to reliability. Affected  
18 Utilities have been central participants in the discussions over RTO formation dating  
19 back to the 1990s and share responsibility for the lack of progress that has been made in  
20 this area. The failure of western utilities to form an RTO (outside the California ISO)  
21 should not now be used as a pretext to serve the agenda of those wishing to thwart  
22 implementation of direct access in Arizona.

23 B. Generation

24  
25 <sup>36</sup> There is also the Central Arizona Transmission System (“CATS”) study group, and the Southeast Arizona  
Transmission (“SATS”) study group.

26 <sup>37</sup> Decision No. 73625 at 2.

1 Affected Utilities and SRP cite the potential lack of incentive to build new  
2 generation in a competitive retail market as one threat to reliability.<sup>38</sup> However, there  
3 does not appear to be an immediate need for the market to incent new builds in order to  
4 meet Arizona demand. Earlier this year, Commissioner Pierce submitted a letter in the  
5 Integrated Resource Planning docket questioning whether “our utilities have more  
6 generation capacity than they reasonably need and/or can put to beneficial use.”<sup>39</sup> His  
7 question was based on a key finding in the 7<sup>th</sup> BTA, which stated: “As a result of current  
8 economic conditions, the statewide demand forecast for the 2012-2021 ten year planning  
9 period has shifted by about six years since the 6<sup>th</sup> BTA (e.g. it will take about six years  
10 longer to reach the previous 2012 demand forecast level).”

11 In response to his inquiries, APS indicated that it had approximately 28% in  
12 generation reserves (including call options). TEP and SRP were closer to 12% operating  
13 reserves. Clearly, Affected Utilities and SRP would still be able to address demand  
14 growth if direct access was implemented, and ESPs chose not to participate. However,  
15 one of the key tenants of direct access is to allow a competitive market to put downward  
16 pressure on retail rates, and in a region that appears to have excess generations,  
17 consumers win.

## 18 CONCLUSION

19 Henry Ford once said, “Competition is the keen cutting edge of business, always  
20 shaving costs.” Jack Welch, former CEO of General Electric, had this to say about  
21 competition: “If you don’t have a competitive advantage, don’t compete.” More  
22 recently, Arizona Attorney General Tom Horne explained why Arizona filed suit to  
23 block the proposed merger between U.S. Airways and American Airlines.

24  
25 <sup>38</sup> APS Initial Comments at 9; SRP Initial Comments at 34.

26 <sup>39</sup> January 11, 2013 letter submitted in Docket No. E-00000A-11-0113.

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“Competition is crucial for a vital economy...As the state’s chief legal officer, it is my duty to maintain competitive markets in Arizona for the benefit of our citizens.”<sup>40</sup>

AECC believes that a competitive retail electric market will provide many benefits besides cost savings to Arizona consumers; innovative products and services designed to fit individual residential and business needs, the continued expansion of renewable and distributed energy options for all classes of customers and the development of other businesses and industries (i.e. electric vehicles, energy efficient products) all competing for customers.

RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of August, 2013.

FENNEMORE CRAIG, P.C.

By 

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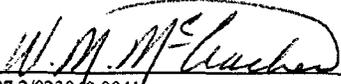
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<sup>40</sup> Arizona Attorney General Office, Press Release, August 13, 2013.

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**EXHIBIT B**

ORIGINAL

COMMISSIONERS  
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Re: Generic Docket No.: E-0000W-13-0135 / In the Matter of the Commission's Inquiry into Retail Electric Competition

Dear Stakeholders:

The purpose of this letter is to invite you to provide detailed comments communicating your views on retail electric competition in Arizona.

At the May 9, 2013 Staff Meeting, the Commission expressed a desire to receive and consider comments from any and all interested parties regarding whether it is in the public interest to implement retail electric competition in Arizona. The Commission plans to take the material filed in the above referenced generic docket and consider it in an upcoming Open Meeting.

The Commission needs input from electric industry stakeholders and customers to assist in the evaluation of the potential benefits versus the potential pitfalls of any possible transition to retail electric competition. The Commission takes seriously its obligations to understand and plan for Arizona's future energy needs and to look at viable production options now in the energy generation pipeline. The Commission finds it critical to stay abreast of energy generation developments and to stay engaged in this development curve.

It is clear that the Commission must undertake a rigorous examination of the complex issues surrounding electric retail competition in order to reach an informed decision. To help facilitate an organized and prudential examination of the matter, Commission Staff recommends that parties address, at a minimum, the following matters:

- 1) Will retail electric competition reduce rates for all classes of customers – residential, small business, large business and industrial classes?
- 2) In addition to the possibility of reduced rates, identify any and all specific benefits of retail electric competition for each customer class.
- 3) How can the benefits of competition apply to all customer classes equally or equitably?
- 4) Please identify the risks of retail electric competition to residential ratepayers and to the other customer classes. What entity, if any, would be the provider of last resort?

- 5) How can the Commission guarantee that there would be no market structure abuses and/or market manipulation in the transition to and implementation of retail electric competition?
- 6) What, if any, features, entities or mechanisms must be in place in order for there to be an effective and efficient market structure for retail electric competition? How long would it take to implement these features, entities, or mechanisms?
- 7) Will retail electric competition require the divestiture of generation assets by regulated electric utilities? How would FERC regulation of these facilities be affected?
- 8) What are the costs of the transition to retail electric competition, how should those costs be quantified, and who should bear them?
- 9) Will retail electric competition impact reliability? Why or why not?
- 10) What are the issues relating to balancing area authorities, transmission planning, and control areas which must be addressed as part of a transition to retail electric competition?
- 11) Among the states that have transitioned to retail electric competition, which model best promotes the public interest for Arizonans? Which model should be avoided?
- 12) How have retail rates been affected in states that have implemented retail electric competition?
- 13) Is retail electric competition viable in Arizona in light of the Court of Appeals' decision in *Phelps Dodge Corp. v. Ariz. Elec. Power Coop.*, 207 Ariz. 95, 83 P.3d 573 (App. 2004)? Are there other legal impediments to the transition to and/or implementation of retail electric competition?
- 14) Is retail electric competition compatible with the Commission's Renewable Energy Standard that requires Arizona's utilities serve at least 15% of their retail loads with renewable energy by 2025? (See A.A.C. R14-2-1801 et seq.)
- 15) Is retail electric competition compatible with the Commission's Energy Efficiency Standard that requires Arizona's electric utilities to achieve a 22% reduction in retail energy sales by consumption by 2020? (See A.A.C. R14-2-2401 et seq.)
- 16) How should the Commission address net metering rates in a competitive market?

May 23, 2013

Page 3

- 17) What impact will retail electric competition have on resource planning?
- 18) How will retail electric competition affect public power utilities, cooperatives and federal controlled transmission systems?

By no means should you consider these questions an exhaustive list. If there are any other matters related to the advantages or disadvantages of retail electric competition that you would like to address, that information is welcome.

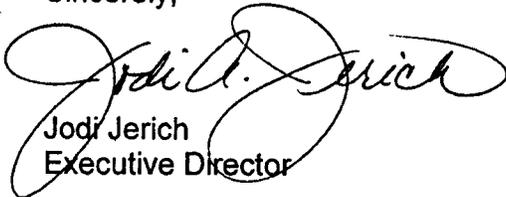
**Initial comments should be filed in Docket No.: E-00000W-13-0135 by July 15, 2013. Responsive comments should be filed by August 16, 2013. Instructions for filing written comments in the docket may be found at [www.azcc.gov](http://www.azcc.gov), or you may call (602) 542-4251 or 1-800-222-7000 for information about how to file comments. Anyone intending to file comments is reminded that such filings are matters of public record, and should not contain information, including personal information, that is not intended for public disclosure.**

If you would like to receive information about this docket on an ongoing basis, please file a notice with Docket Control indicating that you would like to be on the service list. Your notice should include your name, address, and email address. Future notices regarding this docket will be sent only to those individuals/entities that have asked to be included on the service list.

After the Commission has had an opportunity to review the written comments, it plans to convene an Open Meeting to discuss the issues and information filed in this docket. Please consult the Commission's website after the comment period to ascertain the scheduled date. All Commission hearings, workshops, and Open Meetings for this docket and all others are posted on the Commission website

Your comments will be vital to the Commission's consideration of these important issues, and I thank you in advance for your thoughtful contributions to this process.

Sincerely,



Jodi Jerich  
Executive Director

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