



BEFORE THE ARIZONA CORPORATION CC

COMMISSIONERS

Arizona Corporation Commission

DOCKETED

- MIKE GLEASON, Chairman
- WILLIAM A. MUNDELL
- JEFF HATCH-MILLER
- KRISTIN K. MAYES
- GARY PIERCE

JUN 28 2007

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IN THE MATTER OF THE APPLICATION OF ARIZONA PUBLIC SERVICE COMPANY FOR A HEARING TO DETERMINE THE FAIR VALUE OF THE UILITY PROPERTY OF THE COMPANY FOR RATEMAKING PURPOSES, TO FIX A JUST AND REASONABLE RATE OF RETURN THEREON, TO APPROVE RATE SCHEDULES DESIGNED TO DEVELOP SUCH RETURN, AND TO AMEND DECISION NO. 67744.

DOCKET NO. E-01345A-05-0816

IN THE MATTER OF THE INQUIRY INTO THE FREQUENCY OF UNPLANNED OUTAGES DURING 2005 AT PALO VERDE NUCLEAR GENERATING STATION, THE CAUSES OF THE OUTAGES, THE PROCUREMENT OF REPLACEMENT POWER AND THE IMPACT OF THE OUTAGES ON ARIZONA PUBLIC SERVICE COMPANY'S CUSTOMERS.

DOCKET NO. E-01345A-05-0826

IN THE MATTER OF THE AUDIT OF THE FUEL AND PURCHASED POWER PRACTICES AND COSTS OF THE ARIZONA PUBLIC SERVICE COMPANY.

DOCKET NO. E-01345A-05-0827

DECISION NO. 69663

OPINION AND ORDER

DATES OF HEARING: October 5, (Pre-Hearing Conference), December 6, (Procedural Conference), October 10, 11, 12, 13, 16, 19, 20, 23, 24, 25, 26, 30, November 3, 6, 7, 8, 9, 20, 27, 28, 30, December 1, 4, 5, 6, 11, 12, 13, and 15, 2006.

PLACE OF HEARING: Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Lyn Farmer

IN ATTENDANCE: Jeff Hatch-Miller, Chairman
Mike Gleason, Commissioner
Kristin K. Mayes, Commissioner
William A. Mundell, Commissioner
Barry Wong, Commissioner

APPEARANCES: Mr. Thomas L. Mumaw, PINNACLE WEST CAPITAL CORPORATION, Ms. Deborah R. Scott, SNELL & WILMER, LLP, and Mr. William Maledon, OSBORN MALEDON, P.A., on behalf of Arizona Public Service

Company;

Mr. Scott Wakefield, Chief Counsel, and Mr. Daniel Pozefsky, on behalf of the Residential Utility Consumer Office;

Mr. Bill Murphy, MURPHY CONSULTING, on behalf of Distributed Energy Association of Arizona;

Ms. Laura Sixkiller, ROSHKA, DeWULF & PATTEN, PLC, on behalf of UniSource Energy Services;

Mr. Timothy Hogan, ARIZONA CENTER FOR LAW IN THE PUBLIC INTEREST, on behalf of Southwest Energy Efficiency Project and Western Resource Advocates;

Mr. Gary L. Nakarado, on behalf of Vote Solar and Arizona Solar Energy Industry;

Mr. Michael Grant, GALLAGHER & KENNEDY, P.A., on behalf of Arizona Utility Investors Association;

Mr. Kurt J. Boehm, BOEHM, JURTZ & LOWRY, on behalf of the Kroger Company;

Mr. C. Webb Crockett, FENNEMORE CRAIG, P.C., on behalf of the Arizonans for Electric Choice and Competition and Phelps Dodge Mining Company;

Lieutenant Colonel Karen S. White, on behalf of the Federal Executive Agencies;

Mr. Jay I. Moyes, MOYES STOREY, on behalf of Az-Ag Group;

Mr. Andrew W. Bettwy, on behalf of Southwest Gas Corporation;

Mr. Douglas V. Fant, on behalf of the Interwest Energy Alliance and Distributed Energy Association of Arizona;

Mr. Lawrence V. Robertson, Jr., MUNGER CHADWICK, on behalf of Southwestern Power Group II, LLC, Bowie Power Station, LLC and Mesquite Power, LLC.

Mr. Christopher Kempley, Chief Counsel, Ms. Janet F. Wagner, Senior Staff Attorney, and Mr. Charles Hains, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

1 APS did not agree with Staff's recommendations, stating that the Company's proposal was an
2 attempt to strike a delicate balance between providing incentives to promote distributed renewable
3 resources and the amount of the incentive being paid for by others who are not participants in the
4 program. APS believes that Staff's position would upset the balance and provide an even greater
5 subsidy to program participants. APS argues that the 10 kW cap on the generator size is appropriate
6 for net metering, "even in light of an expanded RES program because the Company already offers net
7 billing rate options for distributed generation systems up to 100 kW, which do not have any cap on
8 aggregate participation." (APS Exhibit No. 38, DeLizio Direct, p. 13) However, as clearly pointed
9 out by the Solar Advocates, APS customers do not find those net billing options a substitute for net
10 metering. We agree with most of Staff's recommendations and will adopt them, however, we believe
11 that APS should be able to require the use of a bidirectional meter. We do not agree that "uncollected
12 fixed costs" or "lost revenues", if they exist, should be collected through the EPS or RES surcharge.
13 Rather, we believe that the Company should be allowed to defer such costs and seek their recovery in
14 its next general rate case. APS should file its revised tariff consistent with this Decision within 30
15 days of the effective date of this Decision. This is a pilot program and we expect APS to provide
16 clear, quantifiable and verifiable information using actual results as to what are, if any, the net costs
17 (after calculating all benefits) of net metering.⁵⁴ We further note that this tariff is not being filed
18 pursuant to the RES rules, and that APS will be required to comply with the RES rules when they
19 become effective.

20 **E. Demand Side Management**

21 Pursuant to Decision No. 67744 and the Settlement Agreement, APS committed to spend \$48
22 million on demand-side management programs ("DSM") by year-end 2007. Base rates include \$10
23 million per year of funding, and expenditures above that are deferred and collected through a DSM
24 adjustor mechanism. This level of spending will continue at the current level until APS files, and the
25 Commission approves, modifications to the program design and budget requirements. According to
26 APS, as a result of delayed DSM approvals, the time it takes to ramp up DSM spending, and the lag

27
28 ⁵⁴ APS' use of "total uncollected fixed costs at \$0.04/kWh" in APS No. Exhibit 73 and in APS Exhibit No. 105, Appendix C is based on ballpark approximations. Tr. Vol. VIII, p. 1784.

1 inherent with spending on energy efficient new construction projects, APS will not spend the \$48
2 million by the end of 2007. APS and SWEEP propose that any unspent funds should be carried over
3 and spent in subsequent years. Staff opposes the "carry over" and cites to Decision No. 67744 which
4 requires that any unspent amount should be credited to the balance of the Demand Side Management
5 Adjustment Clause ("DSMAC") account if APS does not spend at least \$30 million of the base rate
6 allowance for approved and eligible DSM-related items during 2005-2007. According to Staff, this
7 "under-funding" is returned to ratepayers. We agree that to the extent that APS has not spent at least
8 \$30 million by year end, the DSMAC should be credited, as required by Decision No. 67744.

9 RUCO recommended that the Commission expand APS' DSM spending requirement
10 beginning in 2008, by requiring total annual spending of at least \$20 million (\$10 million in base
11 rates and \$10 through the DSM adjustor mechanism). RUCO argues that increasing the required
12 spending by \$4 million will encourage more new programs and savings to customers. APS opposes
13 requiring additional spending at this time. APS agreed with RUCO that the DSM programs have
14 been successfully rolled out, but disagreed that they are "up and running" and noted that the DSM
15 adjustor has flexibility to allow APS to spend more than the required amount. We agree with Staff
16 and APS that the current required level of \$16 million should not be increased at this time.

17 APS requests that it be allowed to accrue interest on the unrecovered DSM adjustor balance.
18 Staff did not oppose the request, but recommended that the applicable interest rate be the one-year
19 Nominal Treasury Constant Maturities rate that is contained in the Federal Reserve Statistical Release
20 H-15 or its successor publication. RUCO opposed APS' request to accrue interest, citing no
21 provision in the Settlement Agreement that would allow such accrual. RUCO argues that it would be
22 inappropriate to begin permitting APS to earn interest on uncollected DSM expenditures now, when
23 for the past several years APS has pre-collected funds from customers and no interest was credited to
24 customers. We agree with APS and Staff that APS should be allowed to accrue interest on the
25 unrecovered DSM adjustor balance, at the rate recommended by Staff. It is not inequitable to allow
26 interest to accrue now, because prior to approval of its DSM programs, APS was unable to use the
27 funds in the adjustor balance.

28 Staff concurred with APS' proposed performance incentive in its Portfolio Plan of DSM

1 programs which set the performance incentive at 10 percent of the net benefits achieved and capped it
2 at 10 percent of total DSM spending. Staff also recommended that APS include its request for a
3 performance incentive in each semi-annual DSM report, and that APS provide Staff with backup
4 workpapers and input data to substantiate the numbers for net benefits and performance incentives
5 included in its semi-annual DSM reports. Staff further recommends that APS use the most recent and
6 regionally similar energy savings data available, and not the program-filed savings numbers from
7 2005; that a time limit should be placed on energy use measurements from other regions; that APS
8 use measured savings obtained from APS customers by the Measurement, Evaluation, and Research
9 (“MER”) contractor beginning no later than July 1, 2007; and that the averages of actual measured
10 usage, for both standard and upgraded equipment, should be recalculated by the MER from usage
11 samples for each prescriptive measure based on new measurements from the field no less frequently
12 than every two years. (Staff Exhibit No. 16, Anderson Direct) SWEEP supported the DSM
13 performance incentive proposed by APS and the related recommendations made by Staff. APS
14 agreed with Staff’s recommendations and we will adopt them.

15 SWEEP believes that cost-effective energy efficiency DSM programs reduce total costs for
16 customers and are in the public interest. It proposed changes to APS’ DSM programs, including the
17 adoption of Energy Efficiency Standards (“EES”) to set DSM energy efficiency program goals; the
18 development of an implementation plan; and increases in funding to achieve the EES goals. SWEEP
19 argues that it is “important to focus primarily on the *effects and impacts* of energy and utility policies
20 for setting goals, not primarily on the funding or spending levels. . . . Simply spending money, even
21 cost-effectively, should not be the primary focus of future goals.” (emphasis original) (SWEEP
22 Exhibit No. 2, Schlegel Surrebuttal, pp. 3-4). APS argued that its DSM programs have only recently
23 been approved and APS needs time to get its DSM programs up to speed, to gauge the progress, and
24 to evaluate what is actually being achieved. APS and Staff believe that it is premature to make
25 substantial changes by implementing the EES or a savings target. In response to the SWEEP
26 recommendation of a 12 year implementation plan, APS suggested that the DSM Portfolio Plan’s
27 required biennial updates be used. While we see merit in the position that targets or goals, and not
28 just spending, is what should be important and driving DSM programs, we agree with APS and Staff

1 that we need time to evaluate our current DSM structure before we make such substantial changes as
2 recommended by SWEEP.

3 APS and WRA agree that urban heat island reduction measures should be taken. The large
4 concentration of pavement and buildings in urban areas such as Phoenix has created an urban heat
5 island effect and increasing temperatures, which strain the electric grid and require increased
6 generation from intermediate and peaking power plants. APS is a founding lifetime sponsor of the
7 Arizona State University Global Institute for Sustainability, which is designated as the EPA Center
8 for Excellence in working towards solutions to this problem. APS agrees that it should study the
9 benefits of a heat island reduction program but disagreed with WRA's recommendation that APS be
10 directed to move forward with developing and implementing a cost-effective urban heat island
11 program now. APS indicated that it was willing to hold a DSM Collaborative Working Group
12 meeting to further analyze the issues, and that using the DSM custom project option is a viable way
13 to address the urban heat island effect. Although APS and WRA do not agree on whether there is
14 sufficient research and information today to implement a program, we agree that APS should take
15 steps to address the urban heat island effect. We will require APS to convene a Collaborative
16 Working Group Meeting within the next 60 days and to present where APS believes the research
17 stands and what additional information is needed before a reduction plan can be implemented, and
18 when that information will be obtained.

19 **F. Renewable Procurement**

20 WRA made several recommendations concerning APS' procurement of renewables. WRA
21 argues that APS and its ratepayers face virtually unlimited cost exposure over the long run because of
22 APS' heavy reliance on natural gas. Natural gas prices over the next 20 to 30 years are
23 unpredictable, but the recent high prices are the major reason for APS' recent and proposed rate
24 increases and WRA believes that it is in the public interest to cap APS' exposure to high cost natural
25 gas and replace it with low cost, stably priced renewable energy. WRA witness Berry testified that
26 wind energy projects installed in 2006 or 2007, and geothermal energy contracts signed in 2005 or
27 2006, have prices that are cost competitive with natural gas fired power production at recent prices
28 for natural gas. (WRA Exhibit No. 1, Berry Direct, DB-3) WRA's witness testified that "low cost,