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March 23, 2006

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Parties to the Docket

Re: Arizona Public Service Company Emergency Rate Case (Docket No. E-01345A-06-0009)

Dear Colleagues and Parties to the Docket:

During the course of the testimony offered in this proceeding, it occurs to me that we need to cover one critical aspect in more depth. Does APS have the necessary financial means to provide adequate and reliable electric service to its current and future customers? According to testimony, not granting any interim relief would put APS in a precarious financial position. While I look forward to hearing all the evidence, it appears at this time that APS would be forced to carry more of its deferred costs for fuel and purchased power while trying to add enough infrastructure to meet customer growth in its rapidly expanding service territory.

According to APS, from 2006 to 2009, it will spend $3.1 billion in capital expenditures (CAPEX) for plant, transmission and distribution improvements. Of that amount, APS will have to go to the bond market to issue $1.1 billion in debt. These capital improvements appear to be necessary for APS to maintain the adequacy and reliability of its existing system and meet next year's estimated annual load growth of 4%.

APS has further indicated that any downgrade to junk status would likely result in high borrowing costs for APS, which in turn would be rolled into customer rates. More concerning, however, it would potentially limit APS' ability to access the bond market to fund its required CAPEX budget. In that event, maintaining the adequacy and reliability of APS' system in addition to meeting new growth could be extremely taxing or perhaps jeopardized.

Various investment firms and financial analysts covering APS have also expressed concern about APS' ability to fund its needed CAPEX program in the midst of mounting under-collected balances for fuel and purchased power expenses. The primary concern for APS centers on the **timing** of recovery of prudently incurred costs.

During the evidentiary hearing, Commissioner Gleason questioned APS on the positive effect of expanding the 4 mill bandwidth governing the operation of the PSA. I would like APS, Commission Staff, RUCO and any other interested party to analyze the effect of expanding the 4 mill bandwidth to 5 mills, 6 mills, 7 mills, 8 mills, 9 mills and 10 mills. In particular, how would increasing the bandwidth to these various levels:

- Improve the Funds from Operation (FFO) to Debt ratio?
- Decrease the 2006 projected year-end balance for under-collected fuel and purchased power expenses?
- Increase 2006 revenues for fuel and purchased power expense recovery?
- Improve internal cash flow to fund APS' CAPEX program in 2006?

I would like this proposal added to the mix of the other five proposals being considered at the evidentiary hearing.

Thank you for your prompt attention to this matter.

Sincerely,

Jeff Hatch-Miller
Chairman

CC: Ernest Johnson
Lyn Farmer
Chris Kempley
Brian C. McNeil