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April 14, 2003

Ernest G. Johnson, Director
Utilities Division
Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007



Re: *AEPCO's Issues List for the Electric
Competition Advisory Group ("ECAG")*

Dear Earnest:

As you requested in your March 19, 2003 request to the ECAG, enclosed are AEPCO's Electric Competition Rules Issues. They are submitted without waiver of the positions taken and issues stated in Phelps Dodge et al. v. AEPCO et al., No. CA-CV01-0068 and No. CV1977-03748 (Consol.). A copy was e-mailed to Rodica Pasula today.

As an initial filing AEPCO has focused the enclosed on several major issues in relation to the Rules, rather than a detailed line-by-line review. Comments by others in the ECAG or further developments in the process generally may lead AEPCO to supplement or modify its positions on the issues raised or issues raised by others. AEPCO also generally supports the comments which will be submitted by the Grand Canyon Electric Cooperative Association and the Trico Electric Cooperative.

If you or any other Staff member have any questions concerning the enclosed, please call.

Very truly yours,

GALLAGHER & KENNEDY, P.A.

A handwritten signature in cursive script that reads "Mike".

By:
Michael M. Grant

Letter to Ernest G. Johnson
April 14, 2003
Page 2

MMG:bo
Enclosure
10421-0031/1094800v1

cc with enclosure:

Erinn Andreasen, Utilities Division-ACC
Patricia Cooper
John Wallace
Russ Jones
Chris Hitchcock

AEPCO's Electric Competition Rules Issues

The Arizona Electric Power Cooperative, Inc. ("AEPCO") submits this response to Staff's March 19, 2003 request for comments concerning the Commission's Retail Electric Competition Rules (A.A.C. R14-2-1601 et seq.). This response is submitted without waiver of the positions taken and the issues stated in Phelps Dodge et al v. AEPCO, et al., No. CA-CV01-0068 and No. CV 1977-03748 (Consol.) which is currently pending before the Arizona Court of Appeals.

Because AEPCO is not certain as to how broad an inquiry into retail competition the Staff and Commission want to conduct, we will confine these initial comments to certain specific provisions of the Electric Competition Rules (the "Rules") which are most in need of revision or clarification. AEPCO believes, however, that the entire concept of retail competition should be re-examined. We stated several of the reasons for doing that in our February 25, 2002 responses to the Commissioners' questions. The Rules should not be revised, but instead should be repealed for three primary reasons. First, voter approved amendments to Article 15 of Arizona's Constitution are required to enact competition. Second, a completely different set of assumptions about the market have proven true over the past almost seven years than the assumptions upon which the Rules were initially crafted in the summer of 1996. Finally, that same historical experience has confirmed the initial doubts of the cooperatives about the minimal, if any, consumer benefits and, conversely, the substantial consumer risks involved in the competitive model. As Virginia's Corporation Commission recently noted, "With rare

exceptions, retail competition is not providing meaningful benefits anywhere in the nation. It has been tried now for several years and has yet to yield sustained savings."

Specific Rules Issues

R14-2-1603.A. This subsection should be revised to provide that ESP's shall obtain a certificate of convenience and necessity from the Commission pursuant to this article. But, existing Affected Utilities and Utility Distribution Companies should not be required to secure another CC&N to supply competitive, non-competitive or standard offer services, as appropriate.

R14-2-1604. Most of this rule is outdated and should be repealed.

R14-2-1605. This rule in combination with R14-2-1603.A and R14-2-1615 prohibit Affected Utilities and Utility Distribution Companies from offering Competitive Services. AEPCO strongly urges Staff and the Commission to reconsider and then reject that prohibition. There is no reason why existing utilities should not be allowed to offer all utility services. The prohibition arbitrarily eliminates from the market some of the most competent and qualified competitors. It deprives both the competitive and standard offer customer various efficiencies and economies of scale. It should be repealed.

R14-2-1606. AEPCO raises two issues in relation to this rule.

First, AEPCO urges the Commission to continue the cooperatives' exemption from the competitive procurement requirements of R14-2-1606.B. AEPCO has all-requirements power supply agreements with four of its Arizona Class A member distribution cooperatives and a partial requirements agreement with the fifth. Those agreements currently extend through 2020 and require that the member distribution cooperative either purchase all or, in one case, a substantial and fixed amount of capacity and energy from AEPCO. Those agreements are critical both to existing compliance with RUS' mortgages and the cooperatives' ability to obtain future financing for necessary system improvements and expansion. A requirement that the distribution cooperatives instead secure some portion of their system power needs from an entity other than AEPCO would impair those contractual arrangements, create a default as to the mortgages and imperil the cooperatives' future ability to obtain additional financing. These are the reasons why the existing R14-2-1606.B applies only to an "investor owned" Utility Distribution Company and why the cooperatives' exclusion from the competitive bidding requirement should be maintained.

Second, as to R14-2-1606.C.6, the Commission should clarify the intent of that provision. AEPCO believes it was only intended to prohibit tariffs which required that a standard offer customer forego for a fixed time competitive service in order to qualify for a particular tariffed rate. Staff, instead, has argued that the provision precludes a standard offer customer from voluntarily entering into a long term contract. If, after assessing all options, the standard offer customer chooses to enter into a long term arrangement with the UDC that should be the customer's right. Such arrangements benefit the individual

consumer as well as others on standard offer service. Staff's interpretation actually interferes with customer choice and unreasonably favors competitive service providers.

R14-2-1607. Much of this rule is either outdated or the requirements have been completed.

R14-2-1609. Sections C through J of this Rule should be repealed. The AISA simply is not needed. As for RTO's or ISO's, AEPCO strongly believes that the costs of the FERC RTO and Standard Market Design proposals will far exceed their limited benefits, if any, to cooperative customers.

R14-2-1613. Even though AEPCO does not supply service at retail and has nothing to report, Staff has required that AEPCO submit reports under this rule. This represents an unnecessary expenditure of time and resource for both the Commission and AEPCO. We would recommend adding the words "which supply service at retail" after "Affected Utilities" in section A of the rule.

R14-2-1615. For the reasons discussed previously in relation to R14-2-1605, this Rule and its prohibition against Affected Utilities and Utility Distribution Companies providing Competitive Services should be repealed. If the Commission is not willing to repeal the restriction, section C should be retained which at least allows distribution cooperatives to offer such services inside their service territories.