

MEMORANDUM

TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

DATE: September 27, 2004

RE: STAFF REPORT ON RATE DESIGN, LOW INCOME PROGRAMS, AND SERVICE SCHEDULES CONTAINED IN THE PROPOSED SETTLEMENT AGREEMENT OF ARIZONA PUBLIC SERVICE COMPANY'S REQUEST FOR RATE ADJUSTMENT (DOCKET NO. E-01345A-03-0437)

Attached is the Staff Report on Rate Design, Low Income Programs, and Service Schedules contained in the proposed settlement agreement of Arizona Public Service Company's request for rate adjustment. Staff recommends approval of the settlement agreement.

EGJ:EAA:BEK :rdp

Originator: Erinn Andreasen and Barbara Keene

Attachment: Original and thirteen copies

Service List for: Arizona Public Service Company
Docket No. E-01345A-03-0437)

Christopher C. Kempley
Chief, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ernest G. Johnson
Director, Utilities Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Lyn Farmer
Chief, Hearing Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

ARIZONA PUBLIC SERVICE COMPANY

DOCKET NO. E-01345A-03-0437

**RATE DESIGN, LOW INCOME PROGRAMS AND, SERVICE SCHEDULES
CONTAINED IN THE PROPOSED SETTLEMENT AGREEMENT**

SEPTEMBER 27, 2004

STAFF ACKNOWLEDGMENT

The Staff Report on Rate Design, Low Income Programs, and Service Schedules Contained in the Proposed Settlement Agreement of Arizona Public Service Company's Request for Rate Adjustment, Docket No. E-01345A-03-0437, was the responsibility of the Staff members listed below.

Erinn Andreasen
Public Utilities Analyst
Rate Design

Barbara Keene
Public Utilities Analyst
Low Income Programs and Service Schedules

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Introduction

On August 18, 2004, a proposed settlement agreement of Arizona Public Service Company's ("APS") pending rate case was docketed. The proposed agreement addresses certain rate design, service schedule, and low income provisions. These provisions are the result of settlement negotiations on a wide variety of issues in this case. As part of the overall settlement agreement, these provisions are in the public interest.

Overall Increase

The proposed settlement agreement would allow APS to recover an additional \$67.5 million in base revenues. The base revenue increase reflects a system average increase of 3.77 percent.

Principles that Influenced Rate Design

One of the principles considered in the settlement process is to adopt rates that reflect cost or movement toward cost. Moving toward cost promotes efficient cost recovery and customer equity by reducing subsidizations among customer classes. With that goal in mind, the rates and provisions adopted by the settlement generally reflect certain cost of service considerations.

While cost of service was an important factor in setting rates, other factors were also considered in the process. These factors include; rate continuity for the customer, adopting rate structures that promote conservation, designing rates that are transparent in nature to promote customer understandability, and the reduction of duplicative and underperforming rate structures.

Rate Unbundling

Under the provisions adopted in the settlement agreement, unbundled rates would be adopted for most rate schedules and cost-based unbundling would be permitted. Unbundling standard offer rates and pricing certain competitive service rate elements to reflect cost enhance the opportunity for retail access in APS' service territory by providing ratepayers with the price signals they need to make informed decisions about shopping for competitive services.

The residential rate design reflects cost-based unbundling of distribution and revenue cycle services. The general service rate design reflects cost-based unbundling of generation and revenue cycle services. With regard to E-32, E-34, and E-35, the revenue requirement was allocated to establish first the unbundled component of generation at cost and then the unbundled component of revenue cycle services.

Residential Rates

Under the proposed settlement agreement, the residential rate class would generate an additional 3.94 percent in revenues from base rates. The residential class as a whole would

receive an increase that is only slightly more than the system average increase. The following table summarizes the residential revenue increases by rate schedule as proposed by the settlement agreement.

Residential Rate Schedules		
Rate Designation	Description	Proposed Revenue Increase
E-10	Classic Rate	4.82%
E-12	Standard Rate	3.80%
ET-1	Time-of-Use	3.80%
EC-1	Service with Demand Charge	4.82%
ECT-1R	Time-of-Use with Demand Charge	3.80%

In order to avoid the potential for disproportionate rate impacts to customers, the current residential rate structures, such as the number and size of rate blocks and the time-of-use periods, would be retained.

In order to mitigate the rate impacts of eliminating schedules at the time of the next rate case, rates E-10 and EC-1 would receive a slightly higher increase than the other residential rate schedules. To provide a period for phase out, Schedule E-10 and EC-1 would remain frozen and not be eliminated in this proceeding. However, these rate schedules would be eliminated in APS' next rate proceeding. In order to provide customers with notice of intent to cancel these rate schedules, APS would provide a Staff-approved notice to customers on E-10 and EC-1 at the conclusion of this proceeding and at the time APS files its next rate case.

Residential Time-of-Use

APS would maintain its current on-and-off peak rates for the winter billing period. In response to the concern for flexibility in implementing changes to certain time-of-use provisions, within 180 days of a decision in this matter, APS would submit a study to Staff that would examine the ways in which APS can implement flexibility in changing on- and off-peak time periods and other time-of-use characteristics. APS would also consult with Staff prior to designing its study to ensure that the study addresses all relevant issues. Time-of-use issues would specifically be addressed in APS' next rate case.

In order to enhance time-of-use options for residential customers, experimental time-of-use periods for ET-1 and ECT-1R would be adopted. The experimental periods would provide a limited number of customers with the option of selecting alternative on-peak time periods of 7:00 a.m. to 7:00 p.m. or 8:00 a.m. to 8:00 p.m. The experimental program would be limited to a maximum of 10,000 customers due to the costs associated with the implementation of the program. APS would be required to submit annual reports to Staff evaluating the outcomes of the program and making a recommendation regarding the continuation of the program.

General Service and Classified Rates

Under the proposed settlement agreement, revenues from E-32, E-32R, E-34, E-35, E-53, E-54, and general service contracts would generate an additional 3.5 percent in revenues from base rates. The following table summarizes the revenue increase to general service and classified rate schedules proposed by the settlement agreement.

General Service Rate Schedules		
Rate Designation	Description	Proposed Revenue Increase
E-21	Frozen Time-of-Use, Small less than 100 kW	5%
E-22, E-23, E-24	Time-of-Use, Small, Medium, and Large	5%
E-30	Extra Small Unmetered	5%
E-32, E-32R	General Service and Partial Requirements Rider	3.5%
E-34, E-35	Extra Large and Extra Large Time-of-Use	3.5%
E-53	Athletic Stadiums and Sports Fields	3.5%
E-54	Seasonal Service	3.5%
	Special Contracts	3.5%

Classified Rate Schedules		
Rate Designation	Description	Proposed Revenue Increase
E-20	Time-of-Use Religious Houses of Worship	5%
E-38, E-38T	Frozen Agricultural Irrigation Service and Time-of-Use option	5%
E-40	Agricultural Wind Machine Service	5%
E-47	Dusk to Dawn Lighting Service	5%
E-51	Frozen Cogeneration and Small Power Production Under 100 kW	5%
E-58	Street Lighting Service	5%
E-59	Government Owned Street Lighting Systems	5%
E-67	Municipal Lighting Service, City of Phoenix	5%
E-221, E-221-8T	Water Pumping Service and Time-of-Use Option	5%

The majority of APS' general service customers are served on rate schedule E-32, and customers on this rate have diverse usage characteristics. Due to the complexity of the current rate, schedule E-32 would be modified in an effort to simplify its design and improve customer understandability. When designing the rate, consideration was given to smoothing out the rate impacts across customers of varying sizes. Changes include the addition of an energy block for customers with loads under 20 kW and the addition of a demand billing block for customers with loads greater than 100 kW.

To provide a period for phase out, frozen rates E-38 and E-38T would not be eliminated in this proceeding. However, these rate schedules would be eliminated in APS' next rate proceeding. In order to provide customers with notice of intent to cancel these rate schedules, APS would provide a Staff-approved notice to customers on these schedules at the conclusion of this proceeding and at the time APS files its next rate case.

Under the proposed settlement agreement, the changes to the rate structure for lighting tariffs E-47 and E-58 proposed in APS' application would be adopted. These changes allow for a greater menu of options available to lighting customers.

General Service Time-of-Use

The existing 11:00 a.m. to 9:00 p.m. on-peak time periods would remain in effect for general service time-of-use customers, and the summer rate period would begin in May and conclude in October.

APS' current time-of-use rate schedule, E-20, would be frozen. To provide a period for phase out, experimental time-of-use schedules E-22, E-23, and E-24, which are all limited by caps on customer participation, would be frozen. Experimental time-of-use schedule E-21, which had previously been frozen, and E-22, E-23, and E-24 would be eliminated in APS' next rate proceeding. In order to provide customers with notice of intent to cancel E-21, E-22, E-23, and E-24, APS would provide a Staff-approved notice to customers on these schedules at the conclusion of this proceeding and at the time APS files its next rate case.

Under the proposed settlement agreement, a new rate schedule, E-32 TOU, would be adopted to provide general service customers with an additional time-of-use rate.

Voltage Discounts

The settlement adopts transmission and primary voltage discounts for certain general service rates. Customers that take service at transmission and primary voltage levels require less utility funded facilities and equipment. Under the proposed settlement, military base customers that are served directly from APS substations would receive an additional primary service discount of \$2.74 per kW due to certain cost of service considerations.

Compliance

As part of APS' compliance filing in this matter, APS would be required to meet and confer with Commission Staff to review APS' rate schedules for consistency with the provisions adopted by the proposed settlement agreement.

Low Income Programs

The settlement agreement provides for expansion of the low income weatherization program, including bill assistance, as discussed in the Staff Report on Demand-side Management, Renewables, and Distributed Generation issues.

It was the intention of the parties to this case that low income customers be insulated from the rate increase proposed in the settlement agreement. Therefore, the discount levels were increased for both the E-3 and E-4 tariffs. In addition, APS would increase its annual funding for marketing its E-3 and E-4 tariffs to \$150,000.

Service Schedules

Attached to the settlement agreement are revised versions of Schedules 1, 3, 4, 7, 10, and 15. The proposed changes to each schedule are described below.

Schedule 1 - Terms and Conditions for Standard Offer and Direct Access Services

Schedule 1, contains charges for various services. The settlement agreement proposes to change these charges to be primarily cost-based. The revised charges are summarized in the following table:

Description (Schedule 1 Section)	Current Charge	Proposed Charge
trip charge (2.2.1)	none	\$16.00
after-hour service establishment (2.2.2)	\$50	\$75.00
after-hour other services (2.2.3)	none	\$75.00
overhead reconnection (4.5.1)	\$87.50	\$96.50
underground reconnection (4.5.1)	\$125.00	\$115.00
on-site energy evaluation (4.6)	\$50.00	\$82.00
joint site meeting (6.2.3)	\$30.00 metro area \$75.00 outside metro \$30/hr after 30 minutes	\$62.00 all areas \$53/hr after 30 minutes
reread charge (6.4.4 and 6.4.5)	\$10.00	\$16.50
meter test (6.5)	\$25.00	\$30.00 meter shop \$50.00 field

Other changes to Schedule 1 include adding a provision for electronic bills, adding provisions regarding enforcement of meter access requirements, clarifying language regarding power factor requirements, and making editorial changes.

Schedule 3 - Conditions Governing Extensions of Electric Distribution Lines and Services

The settlement agreement proposes modifications to Schedule 3 that include the following:

1. For extensions with construction costs not exceeding \$25,000, the extension is provided for free if "two times the customer's expected annual revenue" is more than the cost of the extension. To make no distinction between Standard Offer and Direct Access customers, the calculation would be changed to use "six times the customer's expected annual distribution revenue."
2. The economic feasibility analysis for extensions with construction costs exceeding \$25,000 examines the return on investment for a particular extension. The extension is free if the extension is determined to be economically feasible. The calculation would be changed to use only distribution revenue.
3. In calculating the economic feasibility of real estate developments, the methodology would be changed to use only distribution revenue and to estimate sales volume by not assuming that all residential customers in a development are all-electric.
4. Currently, irrigation pumping customers advance the total construction cost of extensions. This provision would be changed so that non-agricultural irrigation pumping extensions would be handled in the same manner as other non-residential customers.
5. Language specific to customers served on network distribution systems would be deleted.
6. Language would be added to provide for a customer contribution when the customer requests an additional primary feeder.
7. Language would be added to allow customers to design and construct facilities.

Schedule 4 - Totalized Metering of Multiple Service Entrance Sections at a Single Site for Standard Offer and Direct Access Service

The settlement agreement proposes to change Schedule 4 to make totalizing of meter readings available to residential customers and single-phase commercial customers, to allow customers to request that meters no longer be totalized, and to make editorial changes.

Schedule 7 - Electric Meter Testing and Maintenance Plan

The settlement agreement proposes to change Schedule 7 by adding language for performance monitoring of solid-state meters and by making editorial changes.

Schedule 10 - Terms and Conditions for Direct Access

The settlement agreement proposes to make editorial changes to Schedule 10.

Schedule 15 - Conditions Governing the Provision of Specialized Metering

The settlement agreement proposes to change Schedule 15 by modifying the schedule title to be applicable to additional technology, by better defining cost responsibility, by addressing technical aspects of meter installations, and by making editorial changes.

Public Interest

Staff believes that the provisions regarding rate design and service charges are in the public interest for the following reasons.

- The provisions in the settlement adopt rates and charges that generally move toward cost while minimizing the potential for adverse rate impacts. Moving toward cost for promotes efficient cost recovery and customer equity by reducing subsidizations among customer classes.
- Under the settlement, the opportunity for retail access in APS' service territory is enhanced through the unbundling of standard offer rates and the pricing of certain competitive service rate elements to reflect cost. Such cost based competitive service rate elements will provide ratepayers with the price signals they need to make informed decisions about shopping for competitive services.
- In order to mitigate the potential for disproportionate impacts to customer bills, the current residential rate structures including rate blocks and time-of-use provisions are maintained.
- The settlement promotes efficiency through the phasing out of duplicative and underperforming rate structures.
- In order to address concerns regarding APS' ability to change its on- and off-peak time periods to be more reflective of times of actual system peak, APS would conduct a study to evaluate ways in which it can implement more flexibility. In order for a thorough examination, time-of-use issues would be reexamined in APS' next rate case.
- The settlement enhances time-of-use options through the adoption of experimental on-peak periods for residential time-of-use customers and the adoption of a new general service time-of-use rate, E-32 TOU.
- General service rate schedule E-32 has been redesigned in an effort to simplify the current rate and improve customer understandability. In designing the rate, consideration

was given not only to cost, but also to smoothing out the rate impact to customers of varying sizes.

- Qualifying low income customers will benefit from an increase in the available low-income discount.