



A subsidiary of Pinnacle West Capital Corporation

Justin H. Thompson
Manager
Regulation, Policy & Analysis

Tel. 602-250-2060
Fax 602-250-3003
e-mail Justin.Thompson@aps.com

Mail Station 9708
PO Box 53999
Phoenix, Arizona 85072-3999

August 4, 2005

Docket Control
Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007

RE: Arizona Public Service Company's Initial Comments - Resource Planning Workshops
Docket No. E-00000E-05-0431

Dear Sir/Madam:

Arizona Public Service Company ("APS" or "Company") is providing the attached comments in response to a request for written comments that emerged from discussions at the July 6, 2005 Resource Planning Workshop ("RP Workshop"). APS appreciates the opportunity to work with Staff and the interested parties to develop a new resource planning process that better fits the electric industry in Arizona today.

The population in the APS service territory continues to grow at a rapid pace, and it is anticipated that the demand for electricity for Arizona customers will increase approximately 5,000 MW over the next ten years. In light of the projected population growth and the changes in the electric utility industry over the last several years, the upcoming RP Workshops provide a forum to develop a streamlined resource planning process to address the future capacity needs of Arizona and APS customers. Such a process will require flexibility in implementation, explicit timelines for filing plans and receipt of prompt Commission approval, and regulatory certainty for cost-recovery.

If you have any questions, or wish to discuss these matters further, please call me at 602-250-2060.

Sincerely,

Justin H. Thompson
Manager
Regulation, Policy & Analysis

Attachment

JHT/jms

Docket Control (Original plus 13 copies)
Electronic Copy to: W. Gehlen
L. Miller

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Introduction

The current workshops relating to resource planning are a result of Arizona Corporation Commission (“Commission”) Decision No. 67744 (April 7, 2005), which adopted a Settlement reached among Arizona Public Service Company (“APS” or “Company”), Staff and interveners in APS’ most recent rate case. That Decision directed Staff to schedule workshops on resource planning issues, with a particular focus on developing needed infrastructure and a flexible, timely and fair competitive procurement process. The Decision anticipated that the workshops may be followed by a rulemaking.¹

During the RP Workshop on July 6th, Staff requested that the participants provide written comments on several issues, including both the RP Workshop process and substantive issues that would need to be addressed in further detail. Staff specifically asked:

- To what degree are participants supportive of reviewing and changing the current rules?
- What issues need to be addressed?
- What is the proposed timeframe?
- What is the expected outcome?
- What should a resource plan look like?

The following sections provide APS’ response to the specific questions raised, as well as the Company’s comments regarding the RP Workshop process.

To What Degree Are Participants Supportive of Reviewing and Changing the Current Rules?

The current Commission resource planning rules (“IRP Rules”)² are not appropriate in today’s electric industry environment. New rules that address the issue of resource planning should be developed. The IRP Rules were adopted in 1989, long before retail electric competition and the resultant changes to the industry were even contemplated. In 1999, as the distinct changes in the industry began to unfold, many sections of the IRP Rules were suspended until further order of the Commission.³ It was recognized then that the IRP Rules no longer worked and they are even less applicable today due to further changes in the industry. For example, the IRP Rules do not recognize the following new factors: energy supplies from merchant generators are an important component of the competitive wholesale market; APS is currently prohibited for the next ten years from building additional generating plants

¹ Decision No. 67744, Attachment A at 17-18, para. 79.

² A.A.C. R-14-2-701, *et seq.*

³ *In the Matter of the A.A.C. R-14-2-704 Hearing for Resource Planning*, Docket No. E-00000A-95-0506, Procedural Order issued March 15, 1999.

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except in explicit circumstances; and in the current financial markets, regulatory certainty of cost-recovery is an important consideration both to the utilities and merchant providers in order to finance needed resources or construct necessary infrastructure.

Furthermore, the current IRP Rules required the electric utilities to provide volumes of data that not only would be largely irrelevant to the development of resource plans but could put the utility and its customers at a disadvantage in the procurement of power. In addition, the IRP Rules failed to provide specific time lines for Commission review of resource plans, which adds to the uncertainty of the rules. Finally, the outcome of the process under the IRP Rules is a “consistency determination,” where the Commission simply determined the degree of consistency of the utility's information with analyses provided by Staff and other parties, but did not provide the utility with any certainty that its plan, if implemented, would lead to a prudence determination. APS believes that the existing rules would fail to produce a valuable resource planning process in today's environment.

In addition to the above factors, the IRP Rules do not take into account changes that have occurred in the regulatory environment over the last several years. Since the IRP Rules were promulgated, new regulatory restrictions have been imposed on the industry. Of particular importance are the Federal Energy Regulatory Commission's (“FERC”) Standards of Conduct requirements that dramatically restrict the ability of the electric utility's transmission and generation functions from sharing information. These FERC rules pose challenges in developing an integrated resource plan.

For all of the above reasons, APS believes that the RP Workshops should be utilized to develop new resource planning rules that assist in the development and implementation of resource plans to reliably meet the state's growing demands for energy. The initial and most critical step in the RP Workshops is for the participants to determine the objective(s) and ultimate outcome of the workshops. APS believes that the objective should be to assure an adequate and reliable power supply for the future by developing a process that provides for certainty, including timely and relevant Commission approval that allows the utilities and participants to act on the resource plans. Some essential elements are specific, short timeframes for Commission approval, an effective, efficient process for resource plan modifications, and a presumption of prudence for the utility's resource procurements made in conformance with an approved resource plan.

What Issues Need to be Addressed?

APS believes several issues need to be addressed over the course of the upcoming workshops.

1. First and foremost, the participants must identify the objectives of the resource planning process.

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2. Regulatory time frames should be established for the initial review and approval of the utility's resource plan. For example, resource plans should be filed every three years, with Commission approval in no more than six months of the initial filing.
3. The resource planning process should allow for flexibility to take into account the normal fluctuations that occur in demand, supply and energy markets. For example, during the three year period, proposed plan modifications should be addressed by the Commission within a timely manner.
4. The resource planning process should provide regulatory certainty. Regulatory approval of a utility's resource plan that ensures adequate cost recovery will in turn provide the financial community and the participants with the assurances they need to secure the capital for the acquisition or construction of new resources. All of the participants in today's market, including customers, will benefit from such certainty.
5. Each utility must develop its own resource plan based on analyses of its customers' needs, including the appropriate fuel and resource mix. Each utility is uniquely situated and the resource plan for one company likely will not work for another.

What is the Expected Outcome?

The outcome of these workshops should be a long-term resource planning process that addresses the future capacity needs of Arizona, provides flexibility in how the plans are implemented, sets timelines for when utilities must file and when the Commission must review and approve the resource plans, and provides a presumption of prudence if the approved resource plan is implemented. APS anticipates that the resource planning process would be codified into new rules as a result of the RP Workshops.

What Should a Resource Plan Look Like?

APS believes that a resource plan should include a defined planning horizon and address five general areas:

1. Long-term load forecast
2. Existing generation and contract capacity
3. System reliability and reserve margin planning
4. Needs Assessment based on supply/demand balance
 - Should take into account resource diversity and fuel mix.
5. Procurement plan

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- Should provide for separate scenarios that take into account, among other things, fluctuating fuel costs, load forecast variability, transmission availability, and renewable tax credit uncertainty.

The RP Workshop Process

The upcoming RP Workshops will provide an opportunity for interested parties and market participants to participate in the development of a resource planning process. To facilitate the workshop process, APS recommends the following:

- Participants should come to a clear consensus on the objectives of the workshop and develop a list of the issues that need to be addressed.
- Each scheduled workshop should have a defined agenda that focuses on a finite number of issues to be discussed with the goal of finding consensus. At the conclusion of each workshop, a list should be compiled of (1) issues where group consensus was reached, and (2) issues where the group “agrees to disagree”.
- All market participants should have a voice during these proceedings.
- Workshops should be scheduled on a regular basis so the workshop process can be completed in a timely manner.
- Once the workshop process is completed, a written report should be prepared for the Commission, which sets out the recommendations and addresses those issues where a consensus could not be reached.
- After receiving the report, the Commission should review the recommendations of the participants and take appropriate action, such as opening a rulemaking docket.