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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

GARY PIERCE, Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF ARIZONA PUBLIC SERVICE COMPANY FOR A HEARING TO DETERMINE THE FAIR VALUE OF THE UTILITY 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	DOCKET NO. E-01345A-11-0224 **NOTICE OF FILING OF PREPARED DIRECT TESTIMONY OF MARY LYNCH IN SUPPORT OF THE SETTLEMENT AGREEMENT AND RATE SCHEDULE AG-1**

Noble Americas Energy Solutions LLC, Constellation NewEnergy, Inc., Direct Energy, LLC and Shell Energy North America (US), L.P. hereby provide notice of filing of the Direct Testimony of Mary Lynch in support of the Settlement Agreement and Rate Schedule AG-1.

Dated this 18th day of January 2012.

Respectfully submitted,

Lawrence V. Robertson, Jr.

Lawrence V. Robertson, Jr.
Attorney for Noble Americas Energy Solutions LLC, Constellation NewEnergy, Inc., Direct Energy, LLC and Shell Energy North America (US), L.P.

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The original and thirteen (13) copies of the foregoing will be filed this 18th day of January 2012 with:

Docket Control Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

A copy of the same served by e-mail or first class mail this same date to:

All Parties of Record

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PREPARED DIRECT TESTIMONY
OF
MARY LYNCH
IN SUPPORT OF THE SETTLEMENT AGREEMENT
AND RATE SCHEDULE AG-1

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Q.1 Please state your name and business address.

A.1 My name is Mary Lynch. I am based in El Dorado Hills, California where I work from a home office. My corporate address is 100 Constellation Way, Suite 500, Baltimore, Maryland 21202.

Q.2 By whom are you employed and in what capacity?

A.2 I am employed by Constellation NewEnergy, Inc. ("CNE") as Vice President, Regulatory and Legislative Affairs, West Region. In this capacity, I am responsible for CNE's regulatory and legislative affairs in the WECC region, with a particular focus on market development issues, including retail choice, resource adequacy, capacity markets, utility procurement practices, and emerging environmental requirements.

Q.3 Please describe your educational background and experience.

A.3 I graduated from California State University at Northridge with a Bachelor of Arts degree in Biology in 1981 and from Northeastern University (Boston, Massachusetts) with a Masters in Business Administration in 1985. Prior to assuming my current responsibilities in the West in 2005, I had lead regulatory responsibilities for CNE's business in the PJM region, and participated extensively in working groups and committees at PJM that focused on electric market design and operation. I have also participated extensively in state regulatory proceedings dealing with the development and design of wholesale competitive energy

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procurement practices in Maryland, New Jersey, the District of Columbia, Pennsylvania, Illinois, Delaware, Ohio, and New York.

Prior to joining CNE, from 1998 through May of 2002, I served as a vice president with Orion Power Holdings with responsibility for managing the procurement of fossil fuel supplies as well as managing regulatory affairs, with a primary focus on the New York state electric markets. From 1983 through 1998, I held various positions with New England Power Company and U.S. Generating Company managing natural gas supplies procurement operations.

Q.4 Upon whose behalf are you testifying in this proceeding?

A.4 I am testifying on behalf of Noble Americas Energy Solutions LLC, Constellation NewEnergy, Inc., Direct Energy, LLC and Shell Energy North America (US), L.P. ("GSP Parties"). I am providing testimony in support of proposed Rate Schedule AG-1, which is Attachment "J" to the Settlement Agreement.

Q.5 Are the GSP Parties signatory parties to the January 6, 2012 Settlement Agreement?

A.5 Yes.

Q.6 Please summarize the nature of the testimony that you are presenting.

A.6 My testimony addresses various topics relative to the proposed Experimental Rate

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Rider Schedule AG-1 ("Rate Schedule AG-1") from the perspective of prospective Generation Service Providers ("GSP"), as that term is defined in Rate Schedule AG-1. If Rate Schedule AG-1 is approved by the Commission, as currently proposed, each of the companies on whose behalf I am testifying has a commercial interest in participating as a GSP. My testimony does not discuss the nature or details of proposed Rate Schedule AG-1, as the APS' witness has provided that detailed review, making it unncessary and unproductive for me to simply duplicate the same.

Q.7 Please provide an overview of your testimony.

A.7 In the testimony that follows, I will describe (i) how the GSP Parties intend to proceed in offering service to prospective customers under the Rate Schedule AG-1 program and (ii) the potential benefits to prospective customers and the general public under the Rate Schedule AG-1 program. In addition, given the fact that Section 17.1 of the Settlement Agreement expressly states that the Rate Schedule AG-1 program "does not address the subject of retail electric competition," I will explain later in this testimony how the Rate Schedule AG-1 program differs from retail electric competition as it exists in other jurisdictions.

Q.8 Please describe how the GSP Parties, as prospective GSPs, would proceed in offering service to prospective customers under the Rate Schedule AG-1

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program.

A.8 The are two parallel sets of activities that will occur in connection with offering service to prospective customers under Rate Schedule AG-1. First, the GSP Parties, as prospective GSPs, will work with other interested parties to finalize the operational details of Rate Schedule AG-1. Specifically, there are references in Rate Schedule AG-1 to "program guidelines" that will address the details of the customer enrollment process, APS's provision of Imbalance Energy, billing by the GSP to APS for energy deliveries, and energy scheduling protocols. The GSP Parties anticipate that preparation of the program guidelines will be accomplished through a collaborative effort of APS, prospective GSPs, and customer representatives, with input and oversight from Commission Staff.

Second, competitive commercial activities will occur. With respect to these activities, Rate Schedule AG-1 allows GSPs to provide wholesale power to APS on behalf of specific customers, who will pay APS for this alternative supply in lieu of other generation related charges to which they are otherwise subject under APS's approved tariffs. The approval of Rate Schedule AG-1 will initiate a highly competitive process during which prospective GSPs will work with interested, eligible customers to structure wholesale supply agreements that meet the customers' pricing and risk management requirements, and that meet contracting and pricing requirements established by Rate Schedule AG-1. The manner in which each prospective GSP approaches this competitive activity is, of course,

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proprietary to each company and will likely differ to some extent for each prospective GSP. Generally speaking, however, prospective GSPs will work with customers to (i) assist with identifying their metered accounts that can be aggregated for service under Rate Schedule AG-1, (ii) analyze the historic energy usage of those accounts, and (iii) review with them the different types of supply structures and value propositions that the prospective GSP can offer. The goal of these commercial activities will be to reach commercial terms acceptable to both parties for a contract that the GSP will execute with APS for wholesale delivery of energy to APS on the AG-1 eligible customer's behalf.

Q.9 Do the GSP Parties anticipate that there will be active interest in the Rate Schedule AG-1 program by qualifying customers?

A.9 It is not possible at this time to predict with certainty the level of interest that eligible customers will have in taking service under Rate Schedule AG-1. Each customer's decision will be predicated upon market conditions that exist at the time they become eligible for service, and whether the prospective GSP is able to offer a value proposition to the eligible customer. Nevertheless, based on customer interest in other Western states that have somewhat similar programs, the GSP Parties anticipate that there will be substantial interest on the part of eligible customers for service under Rate Schedule AG-1.

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Q.10 Upon what information or experience is that anticipation based?

A.10 There are several reasons why the GSP Parties have an expectation of substantial customer interest in service under Rate Schedule AG-1:

- First, APS has indicated in responses to data requests submitted by the GSP Parties during the discovery phase of the rate case proceeding that (i) "the Company generally anticipates that Schedule AG-1 would be available to retail customers that are currently receiving power from the APS grid," (ii) "APS anticipates the aggregation provision would allow a significant number of customers to be eligible" and (iii) as of October 31, 2011, APS had estimated potential participation under Rate Schedule AG-1 to include "14 customer entities comprising 496 metered accounts and roughly 1,650,000 MWh per year."
- Second, evidence from other states where the ability for customers to choose alternative, competitively procured electricity has been introduced suggests that there will be signficant customer interest and enrollment. For instance, here in the West, California, ground zero for the energy crisis, lifted its suspension of retail choice in 2010 and offered commercial and industrial customers four separate phases in which customers not currently procuring their electricity in a competitive manner could submit notices to procure their electricity

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needs separate from the utility standard offer. Each phase had a customer participation cap with requests to participate accepted on a first come, first served basis. Each of the first three phases garnered so much customer interest that they were fully subscribed within minutes, and in some cases, within a few seconds. The fourth phase was conducted on January 13, 2012 and the results of that phase are not yet known.

- Third, Rate Schedule AG-1 service is limited to very large commercial and industrial customers, many of whom have nationwide operations and already have experience shopping for competitively priced electricity in other states. Those same customers, who have accounts in the APS service territory that would be eligible for service under Rate Schedule AG-1, are expected to have a proclivity toward evaluating electricity supply alternatives to determine whether or not their Arizona operations will benefit from enrollment in service under Rate Schedule AG-1. Moreover, these same customers are experienced in stimulating competition among prospective suppliers in order to get "the best deal" possible.
- Fourth, the Settlement Agreement itself has been signed by several entities that represent likely eligible customers or who are themselves likely to be eligible customers, including Arizona Competitive Power

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Alliance ("AzCPA"), Arizonans for Electric Choice and Competition ("AECC"), Freeport-McMoran Copper and Gold, Inc. ("Freeport-McMoran"), The Kroger Co. ("Kroger"), Wal-Mart Stores, Inc and Sam's West, Inc. ("Wal-Mart"). It is our understanding that several of those parties, including AzCPA, AECC, Freeport McMoRan, Kroger and Wal-Mart, are submitting statements and/or testimony in support of the Settlement Agreement and of Rate Schedule AG-1.

Q.11 Please discuss from the perspective of the GSP Parties, as prospective GSPs, what you believe are the potential benefits to (i) prospective customers and (ii) the general public under the Rate Schedule AG-1 program.

A.11 A significant potential benefit to customers who will be eligible for service under Rate Schedule AG-1 includes the ability to better manage their energy-related expenses by fixing the pricing of the generation portion of their energy needs by means of the contract executed between APS and the GSP on their behalf. That is, customers who take service under Rate Schedule AG-1 will not be subject to the variablity that could otherwise occur with APS' tariffs, such as the E-32-L, E-32 TOU-L, E-34, and E-35 rate schedules and various approved APS adjusters applicable to those rate schedules. In addition, competition among GSPs to provide service to eligible Rate Schedule AG-1 customers will create downward pressure on prices and spur the development of innovative energy products and

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services. Finally, any savings that customers achieve while taking service under Rate Schedule AG-1 can be used to support other aspects of their business, increasing their competitiveness and contribution to the Arizona economy.

Q.12 Is there a risk that APS' residential customers could be asked in APS' next rate case to compensate APS for any unrecovered fixed generation costs that APS might experience as a consequence of the Rate Schedule AG-1 program?

A.12 No. Section 17.2 of the Settlement Agreement is expressly worded to preclude that possibility.

Q.13 Given that the Settlement Agreement expressly states that Rate Schedule AG-1 "does not address the subject of retail electric competition," please describe the differences between the Rate Schedule AG-1 program and retail electric competition.

A.13 There are at least two significant differences between retail electric competition as contemplated under Arizona law and the electric service that is provided for under Rate Schedule AG-1. First and foremost, the GSP will transfer title to the electricity the GSP bought, at the direction of an eligible Rate Schedule AG-1 customer, to APS at a delivery point outside of APS' network delivery. Upon taking title to the electricity, APS remains the transmission and distribution provider for the Rate Schedule AG-1 customer. In essence, service under Rate

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Schedule AG-1 is not unlike the type of contractual hedging that APS performs to manage its system-wide portfolio of energy costs, except that the contract executed between the GSP and APS pursuant to Rate Schedule AG-1 will be "earmarked" on behalf of a specific customer, who will be billed for energy at the price the Rate Schedule AG-1 customer in question negotiated with the GSP, thereby bypassing the unbundled generation component of their otherwise applicable APS rate schedule.

A second significant difference between service under Rate Schedule AG-1 and retail electric competition is that in Arizona, the retail supplier is required to have first obtained a Certificate of Convenience and Necessity ("CC&N") for that purpose from the Commission, because the retail supplier under retail electric competition is considered to be the load serving entity of the end use customer. A GSP providing energy to APS pursuant to Rate Schedule AG-1 is not required to secure a CC&N because the electricity that the GSP is providing is delivered to APS at a wholesale delivery point; and, as noted above, title to the electricity passes to APS at that time. In that regard, the GSP is NOT utilizing nor paying for access to APS' transmission and distribution network, and APS remains the load serving entity for the retail customer providing all services, including the generation delivery and billing under a Commission approved rate schedule. In this instance, that rate schedule would be Rate Schedule AG-1.

This structure described above, while significantly different from the

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typical retail model as implemented across the United States, does contain many program similarities that are in place in a few other states in the West, most notably in Washington and Montana.

Q.14 Please summarize the program similarities between the proposed AG-1 rate schedule and the customer choice programs implemented in Washington and Montana.

A.14 Both Washington and Montana are similar to Arizona in that the utilities in those states do not belong to an organized regional transmission organization. Proposed Rate Schedule AG-1 is similar to Puget Sound Energy's Electric Schedule 449 in Washington State and Northwestern Energy's rate schedule CESGTC-1 in Montana.

Schedule 449 was implemented in 2003 for the largest industrial customers of Puget Sound Energy. These customers are free to negotiate wholesale power deliveries to Puget Sound Energy. Wholesale energy providers, acting on behalf of the customer(s) are not required by the Washington Utilities and Transportation Commission to register, obtain a license or certificate or obtain Commission approval to participate in the program. Puget Sound Energy remains both the balancing authority and the load serving entity.

In the state on Montana, Northwestern Energy offers their largest industrial customers the opportunity to bypass Northwestern Energy's energy procurement

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portfolio and arrange wholesale energy deliveries with wholesale energy providers under rate schedule CESGTC-1. Similar to Puget Sound Energy's program, Northwestern Energy remains both the balancing authority and the load serving entity. The Montana Public Service Commission does not register, license nor certificate the wholesale energy providers that arrange for electricity deliveries on a wholesale basis.

Q.15 Do you have any further comments with respect to Rate Schedule AG-1, as now proposed?

A.15 Yes. The GSP Parties believe that APS's introduction of Rate Schedule AG-1 was a constructive feature of APS's Application. The subsequent modifications and additions to the original rate schedule, which occurred as a result of the settlement negotiations involving parties having an interest in the successful deployment of this type of service, have served to ensure that Rate Schedule AG-1, as now proposed, is in the public interest and should be approved by the Commission.

Q.16 Does that complete your Direct Testimony in support of Rate Schedule AG-1, as attached to the Settlement Agreement as Attachment "J"?

A.16 Yes, it does.

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