

ARIZONA PUBLIC SERVICE COMPANY

DOCKET NO. E-01345A-11-0224

BEFORE THE

ARIZONA CORPORATION COMMISSION

TESTIMONY OF

FRANK W. RADIGAN

ON BEHALF OF THE

RESIDENTIAL UTILITY CONSUMER OFFICE

IN SUPPORT OF SETTLEMENT AGREEMENT

JANUARY 18, 2012

1 **INTRODUCTION**

2 **Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS**
3 **FOR THE RECORD.**

4 A. My name is Frank Radigan. I am a principal in the Hudson River Energy Group, a
5 consulting firm providing services regarding utility industries and specializing in the
6 fields of rates, planning and utility economics. My office address is 237 Schoolhouse
7 Road, Albany, New York 12203.

8
9 **Q. ARE YOU THE SAME FRANK RADIGAN WHO PREVIOUSLY SUBMITTED**
10 **TESTIMONY IN THIS PROCEEDING?**

11 A. Yes.

12
13 **Q. WHAT IS THE PURPOSE OF YOUR ADDITIONAL DIRECT TESTIMONY?**

14 A. I will discuss the technical aspects of the proposed Settlement Agreement ("Settlement")
15 filed on January 6, 2012 in Docket No. E-01345-A-11-0224 -- Arizona Public Service
16 Company's request for rate adjustment.

17
18 **Q. DOES RUCO SUPPORT THE SETTLEMENT?**

19 A. Yes, for the reasons that follow as well as the reasons set forth in the testimony of
20 Residential Utility Consumer Office's ("RUCO") Director Jodi Jerich being filed
21 contemporaneously with my testimony.

22

1 **Q. WHAT ARE THE MAIN TECHNICAL ELEMENTS THAT RUCO ENDORSES**
2 **IN THE SETTLEMENT?**

3 A. While I am sure that many people would point to the fact that there is no rate increase in
4 this case as a primary feature of the Settlement, I would note that the RUCO in its direct
5 case as well as several other parties showed that there was no need for a rate increase at
6 this time. In its direct case, RUCO showed that the instant rate case was more the matter
7 of the Arizona Public Service Company (“APS” or the “Company”) advocating for a
8 simple increase in profits and several adjustment mechanisms that passed risk on to
9 ratepayers and helped protect its net income. For example, in its direct case, APS sought
10 a very generous 11% return on equity. The Company also sought to include chemical
11 costs in the Power Supply Adjustment (“PSA”). The Company also advocated for an
12 Environmental and Reliability Account mechanism that would allow recovery of the
13 carrying costs of environmental improvement projects and for projects relating to
14 generating plant capacity acquisitions or additions. Finally, the Company sought the
15 elimination of the 90/10 ratepayer/stockholder sharing mechanism in the PSA.

16
17 I give this background only to show that many aspects of the Settlement had a high
18 probability of outcome in a fully adjudicated proceeding and note that it is not the rate
19 increase that should be focused upon, but rather the other elements of the Settlement that
20 provide value to ratepayers. To illustrate this point, in its direct case RUCO presented a
21 much more balanced case where it would only allow a 10% return on equity, no increase
22 in base rates and rejection of most of the new adjuster mechanisms or changes to the old.

1 Most of the elements of RUCO's direct case have been incorporated into the Settlement
2 such as the no base rate increase and the 10% return on equity.
3

4 **Q. COULD YOU PLEASE SUMMARIZE THE KEY ELEMENTS OF THE**
5 **SETTLEMENT?**

6 A. From RUCO's perspective, there are five key terms of the Settlement:

7 1. the overall zero dollar base rate increase with a four year rate case stay out,
8 in which APS agrees not to raise base rates as a result of any new general rate case
9 filing until at least mid-2016;

10 2. a narrowly-tailored Lost Fixed Cost Recovery ("LFCR") mechanism that
11 supports energy efficiency ("EE") and distributed generation ("DG") at any level or
12 pace set by this Commission;

13 3. an opt-out rate design for residential customers who choose not to
14 participate in the LFCR which will also support EE and DG at the requisite
15 Commission standards;

16 4. a process for simplifying customers' bill format; and

17 5. elimination of the Company's proposed changes to the Transmission Cost
18 Adjustor, the withdrawal of the request to recover chemical costs through the Power
19 Supply Adjustor, the withdrawal of the request for the introduction of an
20 Environmental and Reliability Account
21
22

23 Section 2.1 of the Settlement states that APS agrees not to file its next general rate case
24 prior to May 31, 2015, and no new base rates resulting from APS's next general rate case
25 will be effective before July 1, 2016. This is a key element of the settlement as it
26 represents a four-year moratorium on rate cases where ratepayers will see no increase in

1 base rates, and it puts the onus on management to control operating expenses, minimize
2 capital expenditures, and improve the productivity of its work force.

3
4 In addition, Section 4.1 of the Settlement states that when new rates become effective,
5 customers will have on average a 0.0% bill impact or less. This zero percent or slightly
6 negative bill impact will be achieved by allowing the negative credit that exists in the
7 Company's PSA to continue until February 1, 2013, at which time it will reset (Id). The
8 actual rate impacts due to the Settlement's provisions for low-income customers and the
9 reset of the PSA and discussion of bill impacts will be discussed in more detail later in
10 my testimony.

11
12 **Q. COULD YOU PLEASE DISCUSS THE LOST FIXED COST RECOVERY**
13 **MECHANISM?**

14 A. The Settlement implements a Lost Fixed Cost Recovery ("LFCR") mechanism in Section
15 9. This portion of the Settlement addresses the interest in directing EE and DG policy.
16 The LFCR shall recover a portion of distribution and transmission costs when sales levels
17 are reduced by EE and DG. It shall not recover lost fixed costs attributable to other
18 potential factors, such as weather or general economic conditions. To minimize its
19 impact, the amount of the LFCR mechanism excludes the portion of distribution and
20 transmission costs recovered through the Basic Service Charge ("BSC") and fifty (50)
21 percent of such costs recovered through non-generation/non-transmission demand
22 charges. The LFCR shall be adjusted annually to account for the unrecovered costs, as

1 demonstrated, and is subject to a 1% year over year cap. Any amount in excess of the
2 cap will be deferred.

3
4 Section 9.8 of the Settlement states that residential customers shall have the ability to opt
5 out of the LFCR by electing to pay a slightly higher BSC. The purpose of this opt-out
6 rate is to replicate, on average, the effects of the LFCR, and allow customers who are not
7 comfortable with the LFCR mechanism the option to opt-out. Section 9.9 of the
8 Settlement states that APS shall seek stakeholder input regarding and subsequently the
9 development of a customer outreach program to inform and educate customers about both
10 the LFCR and voluntary opt-out rates and shall implement this outreach program.

11
12 The LFCR is an alternative to the full decoupling mechanism that the Company requested
13 in its original case. In its direct case, RUCO stated that it was inappropriate to implement
14 a decoupling mechanism during this period of economic uncertainty and financial stress
15 for ratepayers. RUCO supports the LFCR as presented in the Settlement because
16 customers who do not want it have the option of another rate design. The ability to opt-
17 out of the LFCR is important as it provides the Company the financial protection for lost
18 sales from EE and DG but it also gives ratepayers the right to vote on these public policy
19 programs advocated by some groups. Similarly, the cap on the LFCR minimizes to a
20 reasonable degree the financial impact of the LFCR and which I note has been the
21 downfall of some decoupling mechanisms in the past.

22

1 **Q. COULD YOU PLEASE DISCUSS THE RESOLUTION OF BILL**
2 **PRESENTATION?**

3 A. Section 16.1 of the Settlement states that within 90 days following approval of the
4 Settlement, APS will initiate stakeholder meetings to address issues related to the APS
5 bill presentation with a goal of making the bill easier for customers to understand. The
6 Settlement also states that APS will thereafter file an application with the Commission
7 for any authorization needed to modify its bill presentation. Such application shall
8 explain how the APS bill presentation proposal reflects the input of stakeholders during
9 the stakeholder meeting process.

10
11 The current APS bill is unbundled with rates for specific services such as billing,
12 metering, system benefits, distribution delivery, transmission, and generation capacity
13 and energy. During the course of the proceeding, it was found that this makes for a fairly
14 long and complicated bill that can sometimes cause customer complaints. To address this
15 issue, in direct testimony the Company proposed to simplify the customers' bill by
16 providing the bundled charges and related information. RUCO supported any efforts
17 that will result in bill simplification, and it is my experience that customers are generally
18 wary of adjustor mechanisms and surcharges. The parties were unable to resolve all
19 issues relating to bill simplification during the proceeding and the initiation of
20 stakeholder meetings should provide the venue to resolve this important issue.

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1 **Q. WHAT ARE SOME OTHER IMPORTANT ELEMENTS OF THE**
2 **SETTLEMENT?**

3 A. Section 7.2 states that APS will withdraw its request to recover through the PSA the cost
4 of chemicals required for environmental compliance at APS's power plants, and APS
5 shall not raise this request before its next general rate case. As I discussed in my direct
6 testimony, the chemical cost is a cost of doing business, just like thousands of other
7 expense items that the Company has to deal with. There is nothing unique about
8 chemical costs and the elimination of this cost is appropriate.

9
10 Section 11.1 of the Settlement provides that APS shall withdraw its request for approval
11 of the proposed Environmental and Reliability Account ("ERA") mechanism, and APS
12 shall not raise this request before its next general rate case. As originally proposed, the
13 ERA mechanism would allow recovery of the carrying costs of projects related to
14 environmental improvement or acquisition/additions of generating capacity. To qualify
15 for recovery under the ERA mechanism a project would have to be generation related and
16 its costs would exceed \$500,000. In its direct case, RUCO opposed the mechanism
17 because the threshold of \$500,000 as proposed by the Company is so low that it would
18 result in almost any project at a generation plant being qualified for cost recovery. In
19 effect, the proposed ERA mechanism was akin to a formula rate plan that would only
20 benefit shareholders. The Settlement properly excluded the mechanism.

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1 Section 13.1 of the Settlement provides that the level of transmission costs presently in
2 APS's base rates will remain in base rates until further order of the Commission. The
3 Company had originally sought to have all transmission costs recovered through the
4 Transmission Cost Adjustor ("TCA"). In its direct case, RUCO recommended against
5 the full recovery in the TCA because RUCO believes that adjustor mechanisms are
6 unwarranted unless, among other things, the costs recovered through the adjustor are
7 highly volatile and beyond the Company's ability to control. RUCO does believe that the
8 Company had shown transmission costs to be highly volatile or beyond its control. The
9 Settlement properly excludes the mechanism.

10
11
12 Section 7.3 states that the 90/10 sharing provision in APS's PSA will be eliminated. In
13 its stead, to incent prudent fuel procurement and use, APS shall be subject to periodic
14 fuel audits. The first fuel audit shall be for 2014. I have been involved in incentive
15 power supply mechanisms for my whole thirty years career and in my experience have
16 learned that Utility's operate and maintain their low costs power plants (coal, hydro and
17 nuclear) at very high availability and capacity factors when they have a monetary stake in
18 their operation. As I stated in my direct testimony the PSA is a much better control for
19 the efforts on the Company's part on a day-to-day basis rather than some after the fact
20 prudence case. That said, this is just one element of the Settlement that must be weighed
21 against all others. On balance, I would not let my opposition to this one provision, while
22 important, hold up support of the Settlement.

1 **Q. COULD YOU PLEASE DSCUSS THE BILL IMPACTS RESULTING FROM THE**
2 **SETTLEMENT?**

3 A. Yes, as I mentioned previously, Section 4.1 of the Settlement states that when new rates
4 become effective, customers will have on average a 0.0% bill impact or less. For
5 residential customers this provision will result in a slight rate increase in base rates for
6 the non low-income residential customers, and a slight decrease in base rates for low-
7 income residential customers. The reason for this is that Section 14.2 of the Settlement
8 requires that low-income customers will have the PSA and Demand Side Management
9 Adjustor Mechanism applied to their bills. This provision has the effect of increasing
10 non low-income base rates and reducing low-income base rate, and can be best seen on
11 the Company's proof of revenue that supports the rates contained in the Settlement. I
12 have included the proof of revenue as an attachment to my testimony. I include this so
13 that the Commission has a full understanding of the rate impacts that result from the
14 Settlement.

15
16 Along these same lines, I would also like to point out that there are two other elements of
17 the Settlement that could cause rates to increase above the zero percent level. First, the
18 PSA is due to be reset in February 2013 (See Section 4.1). The Company has provided
19 rate impacts based on its forecast of changes to the PSA in a letter dated January 9, 2012
20 and is part of the record in this proceeding. The Company estimates that the PSA reset
21 will have the impact of increasing the average bill for a residential customer in February
22 2013 by 3.5%.

1 The second factor that could increase bills beyond December 31, 2012 (See Section 1.5)
2 reflects the fact that in Docket No. E-01345A-10-0474, APS has sought Commission
3 permission to pursue acquisition of Southern California Edison's ("SCE") current
4 ownership interest in Four Corners Units 4 and 5 and to retire Four Corners Units 1-3 (the
5 "proposed Four Corners transaction"). Pursuant to Section 10.2, the Settlement does in
6 fact state that upon execution of the Four Corners Transaction APS may within ten (10)
7 business days after any Closing Date but no later than December 31, 2013, file an
8 application with the Commission seeking to reflect in rates the rate base and expense
9 effects associated with the acquisition of SCE's share of Units 4 and 5, the rate base and
10 expense effects associated with the retirement of Units 1-3, and any cost deferral
11 authorized in Docket No. E-01345A-10-0474. In its January 9, 2012 letter to the
12 Commission, APS estimates that the Four Corners Transaction will increase the average
13 residential bill by an additional 3.2% beyond the 3.5% that it forecasts to occur due to the
14 PSA reset.

15
16 In summary, as shown in the January 9, 2012 letter to the Commission, APS forecasts
17 that because of the Settlement the average residential bill will increase from \$130.95 to
18 \$138.45 for an overall change of 5.7%. While I recognize the forecasting of fuel costs is
19 fraught with uncertainty and there is no certainty that the Four Corners Transaction will
20 take place, I do believe that the record in this case should be complete as to what the true
21 rate impacts could be. This is important in that the Commission has final approval of the

1 terms of the Settlement and can take steps to minimize what it perceives as undue rate
2 impacts resulting from the Settlement.

3

4 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

5 A. Yes, it does.

6

7

ARIZONA PUBLIC SERVICE COMPANY
SUMMARY OF BASE REVENUES BY CUSTOMER CLASSIFICATION
PRESENT AND PROPOSED RATES
TEST YEAR ENDING DECEMBER 31, 2010 ADJUSTED

Line No.	(A) Customer Classification and Current Rate Designation	(B) Average Number of Customers	(C) Adjusted MWh Sales	(D) Average Annual kWh Usage per Customer [[C] x 1000] / (B)	(E) Base Revenues under Present Rates ¹ (\$000)	(F) Proposed Rate Designation	(G) Proposed Revenue			(J) Change -Base Rates		Line No.
							(G) Base Revenues (\$000)	(H) Transmission Revenue ⁷ (\$000)	(I) Total Revenue (\$000)	(J) Amount (\$000)	(K) % (J) / (E)	
1	<u>Residential</u>											1
2	E-12	485,397	4,026,662	8,296	493,366	E-12	492,152	-	492,152	(1,214)	-0.25%	2
3	ET-1	293,620	4,344,033	14,795	480,986	ET-1	481,090	-	481,090	104	0.02%	3
4	ET-2	123,038	1,919,486	15,601	266,039	ET-2	266,172	-	266,172	133	0.05%	4
5	ECT-2	39,448	1,400,862	35,512	107,426	ECT-2	107,539	-	107,539	113	0.11%	5
6	ECT-1R	48,378	1,404,939	29,041	122,096	ECT-1R	122,201	-	122,201	105	0.09%	6
7	ET-SP	108	2,301	21,306	221	ET-SP	220	-	220	(1)	-0.45%	7
8	Total Residential	989,989	13,098,283	13,231	1,470,134	Total Residential	1,469,374	-	1,469,374	(760)	-0.05%	8
9												9
10	<u>General Service</u>											10
11	E-20	328	36,664	111,780	3,886	E-20	3,912	-	3,912	26	0.67%	11
13	E-30	4,644	6,349	1,367	1,406	E-30	1,407	-	1,407	1	0.07%	13
14	E-40	1	-	-	1	See note 9						14
15	E-32 XS	82,396	1,418,941	17,221	199,177	E-32 XS	203,014	-	203,014	3,837	1.93%	15
16	E-32 S	29,411	2,551,983	86,770	290,021	E-32 S	292,939	-	292,939	2,918	1.01%	16
17	E-32 M	4,425	3,279,542	741,139	317,315	E-32 M	317,809	-	317,809	494	0.16%	17
18	E-32 L	1,035	3,647,139	3,523,806	303,798	E-32 L	301,465	-	301,465	(2,333)	-0.77%	18
19	E-32 TOU XS	78	4,609	59,090	633	E-32 TOU XS	644	-	644	11	1.74%	19
20	E-32 TOU S	219	41,567	189,804	4,454	E-32 TOU S	4,484	-	4,484	30	0.67%	20
21	E-32 TOU M	73	69,937	958,041	6,385	E-32 TOU M	6,374	-	6,374	(11)	-0.17%	21
22	E-32 TOU L	47	295,614	6,289,660	22,917	E-32 TOU L	22,625	-	22,625	(292)	-1.27%	22
23	E-34	36	1,086,047	30,167,972	80,597	E-34	79,328	-	79,328	(1,269)	-1.57%	23
24	E-35	29	1,673,369	57,702,379	112,009	E-35	109,345	-	109,345	(2,664)	-2.38%	24
25	Total General Service	122,722	14,111,761	114,990	1,342,599	Total General Service	1,343,346	-	1,343,346	748	0.06%	25
26												26
27	<u>Irrigation and Water Pumping</u>	1,450	313,308	216,074	26,669	Irrigation and Water Pumping	26,681	-	26,681	12	0.04%	27
28												28
29	<u>Outdoor Lighting</u>											29
30	E-58	624	33,212	53,224	10,107	E-58	10,107	-	10,107	-	0.00%	30
31	E-59	293	93,502	319,119	9,701	E-59	9,701	-	9,701	-	0.00%	31
32	Contract 12	41	11,496	280,390	1,013	Contract 12	1,013	-	1,013	-	0.00%	32
33	E-67	181	3,432	18,961	178	E-67	178	-	178	-	0.00%	33
34	Total Outdoor Lighting	1,139	141,642	124,356	20,999	Total Outdoor Lighting	20,999	-	20,999	-	0.00%	34
35												35
36	<u>Dusk to Dawn Lighting</u>	See Note 5	24,613	See Note 5	8,457	Dusk to Dawn Lighting	8,457	-	8,457	-	0.00%	36
37												37
38	Total Sales to Ultimate Retail Customers	1,115,300	27,689,607	24,827	2,868,858		2,868,857	-	2,868,857	-	0.00%	38

NOTES TO SCHEDULE:

- 1) Base Revenues under Present Rates reflect adjusted test year revenues based on rates established in Decision No. 71448.
- 2) Share the Light Rate Schedules are included in Rate Schedule E-58.
- 3) Rider rate schedules are included in the "Parent" rate schedules listed on schedule H-2 as applicable.
Riders include: E-3, E-4, CPP-RES, CMPW-01, E-53, E-54, RSSP, PPR, CPP-GS, Solar-2, Solar-3, GPS-1, GPS-2, GPS-3, EPR-2, EPR-6, E-56, and SC-S.
- 4) Rate Schedule E-35 is not included as proposed price changes are market-related.
- 5) Dusk to Dawn Lighting customers are included in residential and general service counts as this service is included on each customer's primary billing.
- 7) Transmission revenues based on OATT charges effective during test year.
- 8) Rate Schedules GS Schools M, GS-Schools L have no revenue or customers.
- 9) Rate E-40 proposed revenue is reflected in E-32 M
- 10) Excludes 144,149 MWh of revenue credits, total sales with revenue credits = 27,833,756 MWh

Supporting Schedules:

N/A