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ARIZONA CORPORATION COMMISSION

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October 2, 2006

Re: Cost of Recent Palo Verde Unit 1 Unplanned Outage; Establishment of a Rate Stabilization Fund; Calculation of Rate Impact of the Parties' Rate Recommendations on Customer Bills; APS General Rate Case; Dockets No. E-01345A-05-0816, E-01345A-05-0826, E-01345A-05-0827

Dear Colleagues and Parties to the Docket:

I write today to request that the Parties address several questions during the hearing in this matter regarding the most recent unplanned outage at Palo Verde Nuclear Generating Station ("PVNGS"), the establishment of a Rate Stabilization Fund by Arizona Public Service ("Company"), and the calculation of the impact of the parties' rate recommendations on residential customer bills.

Palo Verde

On Tuesday, September 19, 2006, Unit 1 at PVNGS experienced an unplanned outage due to problems with the unit's pressurizer heaters. To date, Unit 1 has been down for more than a week, and is anticipated to remain off-line until the first week of October. Additionally, PVNGS Unit 2 is scheduled to be down for approximately 50 days beginning the evening of September 29, 2006 for routine refueling.

First, I would like the Company to estimate the weekly cost for the Unit 1 outage. Does the Company intend to seek recovery of these costs through the adjustor mechanism established in Decision No. 67744, or though a surcharge filing? If so, I would request that these costs be set aside and not passed through the PSA until Staff's prudence review of all 2006 PVNGS outages is complete.

Second, understanding that the high temperatures of summer are behind us, how do these outages affect the Company's power supply, both for metro Phoenix, and for Company's entire service territory? Will the outages require the Company to purchase power on the wholesale market or employ generators not normally utilized by the Company during this time of year?

Rate Stabilization Fund

Third, in Decision No. 68685, the Commission strongly urged APS to cut unnecessary expenses and establish a Rate Stabilization Fund to help shield the Company's customers from future rate increases.[1] To date, the Company has not established the Rate Stabilization Fund. During the Open Meeting on May 2, 2006, at which the Commission voted to approve interim rates for the Company, Mr. Bill Post, Chairman of the Board and CEO of Pinnacle West Capital Corporation, spoke about the establishment of a Rate Stabilization Fund in the general rate case:

[1] Decision No. 68685, Finding of Fact 64, Page 36.

> "It's just the establishment of the fund part of it that I think could be dealt with in the base rate case..."[2]

While I am disappointed that the Company has so far failed to implement the Rate Stabilization Fund, I look forward to a full evidentiary hearing in which the Parties discuss how such a fund can be effectuated as part of this rate case. As previously discussed, I believe the fund could be established through cuts to discretionary expenses such as the elimination of executive bonuses, non-essential advertising and sports sponsorships. I would also request that the Parties look at property tax savings and savings from Operations and Maintenance ("O&M") as potential funding mechanisms for the Rate Stabilization Fund. Additionally, I would like the Parties, as part of their analysis, to examine the Rate Stabilization Fund that has been implemented by the Salt River Project ("SRP").[3] If necessary, I would like to call a witness from SRP to discuss the specifics of its fund.

Calculation of Rate Impact on Customers' Bills from the Parties' Rate Recommendations

Finally, I would request that the Parties provide an analysis of the actual impact to residential customer bills from the parties' rate recommendations. This analysis should be based on a residential customer using 800 kWh per month, under the Company's E-12 rate. I would like the analysis to detail the following: the residential customer bill prior to Decision No. 67744, after Decision No. 67744 (including the 4-mill adjustor that was implemented on February 1, 2006), after Decision No. 68685 and what the residential customer bill would be under the Company's, RUCO's and Staff's proposed rates. Please put this information in table form, and provide it to the Commission prior to the beginning of the hearing in this matter.

Sincerely,

Kris Mayes
Commissioner

Cc: Chairman Jeff Hatch-Miller
Commissioner William A. Mundell
Commissioner Mike Gleason
Commissioner Barry Wong
Brian McNeil
Ernest Johnson
Heather Murphy
Docket

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[2] Transcript of May 2, 2006 Open Meeting, page 83.

[3] It is my understanding from discussions with SRP officials that SRP established a Rate Stabilization Fund in the late 1990s when they were refinancing debt. They established this fund by taking earnings from one year and shifting these earnings to future years while continuing to meet their debt. SRP used money from their wholesale electricity sales, lower O&M costs and property tax savings to fund their Rate Stabilization Fund.