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UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Norman C. Bay, Chairman;
Cheryl A. LaFleur, Tony Clark,
and Colette D. Honorable.

Arizona Public Service Company

Docket Nos. ER13-630-000
ER15-522-002
ER10-2437-001
EL14-98-000

ORDER ON MARKET-BASED RATES AND TERMINATING SECTION 206

(Issued November 10, 2015)

1. On October 3, 2014, the Commission issued an order addressing an updated market power analysis and a notice of change in status filed by Arizona Public Service Company (APS).¹ In that order, the Commission determined that APS satisfies the Commission's standards for market-based rate authority in the Southwest region, with the exception of the Tucson Electric Power Company (TEP) and APS balancing authority areas and the Phoenix Valley Load Pocket.² The Commission directed APS to submit an updated horizontal market power analysis for the TEP balancing authority area and instituted a proceeding under section 206 of the Federal Power Act (FPA)³ in Docket

¹ *Arizona Public Service Co.*, 149 FERC ¶ 61,013 (2014) (October 3 Order).

² The Phoenix Valley (which does not include Northern Arizona) includes an APS and Salt River Project (SRP) integrated network and the Rogers substation, which is interconnected with two Western Area Power Administration transmission lines located in a portion of the Western Area Lower Colorado control area. The Phoenix Valley is served primarily from four major extra high voltage substations: Westwing, Rudd, Pinnacle Peak, and Kyrene. These four stations form the cornerstones of an extensive internal network of 230 kilovolt (kV) transmission lines that constitute the high voltage energy delivery system within the Phoenix Valley. *Pinnacle West Capital Corp.*, 120 FERC ¶ 61,153, at P 1 n.2 (2007) (citing Pinnacle's February 18, 2005 Filing in Docket No. ER00-2268-010, Attachment C, "APS Reliability Must-Run Analysis 2003-2005," January 31, 2003, APS Transmission Planning, APS Resource Planning at 16).

³ 16 U.S.C. § 824e (2012).

No. EL14-98-000 to investigate horizontal market power issues in the APS balancing authority area and the Phoenix Valley Load Pocket.

2. In this order, the Commission finds that APS satisfies the Commission's horizontal market power standard for the grant of market-based rate authority for the TEP balancing authority area. Further, as discussed below, the Commission accepts APS's mitigation proposal for the APS balancing authority area and the portions of the Phoenix Valley Load Pocket that are within the APS balancing authority area.⁴ Accordingly, this order terminates the section 206 proceeding instituted in Docket No. EL14-98-000. Further, and as discussed below, this order accepts, subject to conditions, APS's proposed revisions to its market-based rate tariff, effective February 2, 2015, as requested.

I. Background

3. APS currently has authorization to make sales at market-based rates except in the Phoenix Valley Load Pocket in the summer season.⁵ The Phoenix Valley Load Pocket includes an APS and SRP integrated network and the Rogers substation, which is interconnected with two Western Area Power Administration transmission lines located in a portion of the Western Area Power Administration – Lower Colorado (WALC) balancing authority area.⁶ Thus, portions of the Phoenix Valley Load Pocket are within the APS, SRP and WALC balancing authority areas.

4. On December 27, 2012, as amended on March 19, 2013, December 11, 2013, and December 18, 2013, APS filed an updated market power analysis for the Southwest

⁴ APS states that it is proposing cost-based mitigation in “the APS [balancing authority area] and those portions of the [Phoenix Valley Load Pocket] that are within the APS [balancing authority area]. December 2, 2014 Filing at 1-2. Section 1.7 of APS's proposed tariff defines the Phoenix Valley Load Pocket as “a subset of the APS [b]alancing [a]uthority [a]rea which includes all delivery points owned by APS within the portion of the Phoenix 230kV loop that resides in the APS [b]alancing [a]uthority [a]rea, including APS's 230kV substations forming the boundaries of the loop, which include: Westwing 230kV, Pinnacle Peak 230kV and Raceway 230kV.” Therefore, we note that, while the proposed tariff language defines the Phoenix Valley Load Pocket as a subset of the APS balancing authority area within the APS balancing authority area, for purposes of this order, we distinguish between portions of the Phoenix Valley Load Pocket that are inside and outside of the APS balancing authority area, as APS has done in its filings.

⁵ See *Pinnacle West Capital Corp.*, 122 FERC ¶ 61,035 (2008).

⁶ See October 3 Order, 149 FERC ¶ 61,013 at P 2 n.2.

region in compliance with the regional reporting schedule adopted in Order No. 697.⁷ Additionally, on January 29, 2014, APS filed a notice of change in status. In its filings, APS requested that the Commission lift the current limitation on APS's market-based rate authority, which prohibits APS from making market-based rate sales in the Phoenix Valley Load Pocket during the summer season.

5. In the October 3 Order, the Commission found that APS had not rebutted the presumption that it has market power in the Phoenix Valley Load Pocket in the summer season and therefore had not supported its request to lift the limitation on its market-based rate authority in the Phoenix Valley Load Pocket during the summer season. Further, the Commission found that APS's failure of the wholesale market share screen in the APS balancing authority area and APS's concession that it fails the screens in the Phoenix Valley Load Pocket establish a rebuttable presumption of horizontal market power. Thus, the Commission instituted a proceeding pursuant to section 206 of the FPA concerning the justness and reasonableness of APS's market-based rates in the APS balancing authority area and the Phoenix Valley Load Pocket. The Commission directed APS to: (1) show cause as to why the Commission should not revoke APS's market-based rate authority in the APS balancing authority area for all seasons and in the winter, spring, and fall seasons in the Phoenix Valley Load Pocket; (2) file a mitigation proposal tailored to its particular circumstances that would eliminate its ability to exercise market power; or (3) inform the Commission that it will adopt the default mitigation set forth in the Commission's regulations or propose other cost-based rates and submit cost support for such rates.⁸ Additionally, the Commission discussed its concerns with the Delivered Price Test (DPT) analyses APS submitted for the APS balancing authority area and the Phoenix Valley Load Pocket and stated that APS could submit corrected DPT analyses for those areas. The Commission also noted in the October 3 Order that APS did not submit screens in support of its claim in its January 29, 2014 change in status that it continues to pass the Commission's horizontal market power screens in the TEP balancing authority area. Therefore, the Commission directed APS to submit an updated horizontal market power analysis in support of its claim.

⁷ See *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, at PP 848-850, *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, *clarified*, 124 FERC ¶ 61,055, *order on reh'g*, Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 (2008), *order on reh'g*, Order No. 697-C, FERC Stats. & Regs. ¶ 31,291 (2009), *order on reh'g*, Order No. 697-D, FERC Stats. & Regs. ¶ 31,305 (2010), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012).

⁸ 18 C.F.R. § 35.38 (2015).

6. On December 2, 2014, APS filed its response to the October 3 Order. APS's filing includes an updated horizontal market power analysis in support of its continued authorization to sell energy, capacity, and ancillary services at market-based rates in the TEP balancing authority area, a DPT for the Phoenix Valley Load Pocket, and a tailored cost-based mitigation proposal for the APS balancing authority area, including the portions of the Phoenix Valley Load Pocket within the APS balancing authority area. APS states that in light of APS's decision to propose a tailored mitigation plan for sales in the APS balancing authority area, APS is not seeking at this time to continue or expand its market-based rate authorization with respect to those portions of the Phoenix Valley Load Pocket within the APS balancing authority area. APS maintains that the Commission should not revoke APS's market-based rate in the winter, spring, and fall seasons in the portions of the Phoenix Valley Load Pocket that are outside of the APS balancing authority area and requests that the Commission grant APS authorization to make sales at market-based rates in the summer season in the portions of the Phoenix Valley Load Pocket that are outside of the APS balancing authority area.

7. APS filed proposed tariff revisions reflecting its mitigation proposal on December 1, 2014, as amended on December 11, 2014 and February 13, 2015. In its February 13, 2015 filing, APS proposes to revise the Limitations and Exemptions section of its tariff (section 7.1) to state that APS is not authorized to sell electricity at market-based rates in the Phoenix Valley Load Pocket or the APS balancing authority area and proposes to revise section 1.7 of the tariff with respect to the definition of the Phoenix Valley Load Pocket, redefining it as the portions of the Phoenix Valley Load Pocket that are within the APS balancing authority area. APS also proposes to revise section 2.3.2 of its tariff to state that third-party ancillary services sales will not include sales delivered within the Phoenix Valley Load Pocket (as redefined in the tariff) or the APS balancing authority area. Finally, APS proposes to revise section 2.2 of its tariff to provide that sales of electric energy and/or capacity at market-based rates by APS are permissible in all balancing authority areas where APS has been granted market-based rate authority and also at the metered boundary between APS's mitigated balancing authority area and a balancing authority area where the APS has been granted market-based rate authority.

II. Notice of Filings

8. Notice of APS's December 1, 2014, December 2, 2014, December 11, 2014, and February 13, 2015 filings was published in the *Federal Register*,⁹ with interventions and protests due on or before March 6, 2015. None was filed.

⁹ 79 Fed. Reg. 73,062; 79 Fed. Reg. 73,289; 79 Fed. Reg. 75,134 (2014); 80 Fed. Reg. 9708 (2015).

III. Discussion

A. Market-Based Rate Authorization

9. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, horizontal and vertical market power.¹⁰ As discussed below, we conclude that APS satisfies the Commission's standards for market-based rate authority in the TEP balancing authority area and the portions of the Phoenix Valley Load Pocket that are outside of the APS balancing authority area. With respect to the APS balancing authority area and the portions of the Phoenix Valley Load Pocket that are within the APS balancing authority area, we accept APS's mitigation proposal, as discussed below.

1. Horizontal Market Power

10. The Commission has adopted two indicative screens for assessing horizontal market power: the pivotal supplier screen and the wholesale market share screen.¹¹ The Commission has stated that passage of both screens establishes a rebuttable presumption that the applicant does not possess horizontal market power, while failure of either screen creates a rebuttable presumption that the applicant has horizontal market power.¹² An applicant that fails one or more of the indicative screens is provided with several procedural options including the right to challenge the market power presumption by submitting a DPT analysis, or, alternatively, sellers can accept the presumption of market power and adopt some form of cost-based mitigation.¹³ APS's response to the October 3 Order includes indicative screens for the TEP balancing authority area, a DPT for the Phoenix Valley Load Pocket, and a mitigation proposal for the APS balancing authority area, which includes the portions of the Phoenix Valley Load Pocket within the APS balancing authority area.

a. Indicative Screens

11. APS prepared the pivotal supplier and wholesale market share screens for the TEP balancing authority area consistent with the requirements of Order No. 697.

¹⁰ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at PP 62, 399, 408, 440.

¹¹ *Id.* P 62.

¹² *Id.* PP 33, 62-63.

¹³ *Id.* P 63. The results of the DPT can be used for pivotal supplier, market share, and market concentration analyses.

12. We have reviewed APS's pivotal supplier screens and wholesale market share screens and determined that APS passes both screens in the TEP balancing authority area with market shares ranging from 10 to 18.5 percent. Accordingly, we find that APS satisfies the Commission's requirements for market-based rate authority regarding horizontal market power in the TEP balancing authority area.

13. APS submitted a DPT for the Phoenix Valley Load Pocket. As an initial matter, we note that APS's DPT analysis contains modeling errors that affect its calculation of competing supply, so we would not be able to rely on that analysis to rebut the presumption of APS's horizontal market power in the Phoenix Valley Load Pocket.¹⁴ More importantly, the DPT is for the entire Phoenix Valley Load Pocket, including the APS portions of the Phoenix Valley Load Pocket; it does not just consider the portions that are outside of the APS balancing authority area. For this reason, it is not an actual depiction of APS's market power in the non-APS portions of the Phoenix Valley Load Pocket, that is, the portion of the Phoenix Valley Load Pocket located in the SRP and WALC balancing authority areas.

14. However, we note that APS passes the indicative screens in the SRP and WALC balancing authority areas, with market shares ranging from 1.7 to 2.4 percent for the SRP balancing authority area and market shares of zero percent for the WALC balancing authority area.¹⁵ Further, APS does not own any generation in the non-APS portions of the Phoenix Valley Load Pocket. Accordingly, we find that APS has rebutted the presumption of horizontal market power and satisfies the Commission's horizontal market power standard for the grant of market-based rate authority in the SRP and WALC balancing authority areas, including the portions of the Phoenix Valley Load Pocket that are in the SRP and WALC balancing authority areas.

¹⁴ For example, Commission regulations require a DPT analysis to account for any and all applicable transmission costs that a supplier would incur to deliver the energy into the study area and add these costs to the estimate of the available unit's variable generation cost. Commission regulations state that these costs should include the maximum transmission rate in a transmission provider's tariff as well as the estimated cost of supplying energy losses. *See* 18 C.F.R. § 33.3(d)(5) (2015). APS did not include all applicable transmission costs in its economic capacity or available economic capacity calculations. APS's DPT analysis used a universal \$1.00 transmission rate for all generators, regardless of location.

¹⁵ October 3 Order, 149 FERC ¶ 61,013 at P 13.

b. Mitigation and Revised Tariff

15. As noted above, APS proposes to implement existing Commission-approved cost-based mitigation for sales within the APS balancing authority area and the portions of the Phoenix Valley Load Pocket within the APS balancing authority area. APS states that, under its current Commission-approved mitigation, APS's rates are capped at the sum of: (1) the system incremental cost, forecasted at the time the transaction is executed, plus ten percent of the forecasted system incremental cost; (2) a stated demand charge based on MW/month, MW/week, MW/day, or MW/hour, as appropriate; and (3) the cost of transmission service and any ancillary services purchased by APS and resold to the customer.¹⁶ APS states that allowing it to continue making sales of energy, capacity, and ancillary services pursuant to its existing tailored mitigation plan, with which APS and many of its wholesale power customers are already familiar, will help facilitate the transition from market-based rates to cost-based rates within the APS balancing authority area, including the APS portions of the Phoenix Valley Load Pocket.

16. APS filed proposed market-based rate tariff revisions reflecting the restriction on its sales in the APS balancing authority area, including the APS portions of the Phoenix Valley Load Pocket. Given that the proposed mitigation applies to the entire APS balancing authority area, which would necessarily include the portions in the Phoenix Valley Load Pocket, the definition in section 1.7 of the "Phoenix Valley Load Pocket" is no longer a necessary part of APS's tariff. Thus, we will accept, subject to conditions, APS's proposed revisions to its market-based rate tariff, effective February 2, 2015, subject to the tariff revisions discussed below. We direct APS to submit, within 30 days of the date of this order, a compliance filing correcting a typographical error in section 2.2 of its tariff¹⁷ and revising the limitations and exemptions section of its tariff to include a citation to this order.¹⁸ Further, while we accept APS's proposal to relinquish market-based rate authority in the APS balancing authority area including the portions of

¹⁶ December 2, 2014 Filing at 14 (noting *Arizona Public Service Co.*, Docket No. ER09-1402-000 (Aug. 11, 2009) (delegated letter order accepting revisions to APS's currently effective cost-based rate tariff)).

¹⁷ It appears that section 2.2 of APS's tariff contains a typographical error. The sentence states that "[s]ales of electric energy and/or capacity at market-based rates by APS are permissible capacity under this tariff in all balancing authority areas where APS has been granted market-based rate authority." We assume that the second use of the word "capacity" was not intended to be placed here and therefore we direct APS to submit a compliance filing correcting this section of its tariff.

¹⁸ See Order No. 697, FERC Stats. & Regs. ¶ 31,252 at Appendix C; Order No. 697-A, FERC Stats. & Regs. ¶ 31,268 at P 384.

the Phoenix Valley Load Pocket that are in the APS balancing authority area, we direct APS to remove the definition of the Phoenix Valley Load Pocket in section 1.7 as it is no longer necessary.¹⁹ Further, we direct APS to remove references to the Phoenix Valley Load pocket in sections 2.3.2 and 7.1 of its tariff.

2. Vertical Market Power

17. In cases where a public utility or any of its affiliates owns, operates, or controls transmission facilities, the Commission requires that there be a Commission-approved Open Access Transmission Tariff (OATT) on file or that the seller has received waiver of the OATT requirement before granting a seller market-based rate authorization.²⁰

18. APS states that the transmission facilities owned by APS are subject to the terms and conditions of APS's Commission-approved OATT and all requests for new transmission service over facilities owned by APS are governed by the APS OATT.

19. The Commission also considers a seller's ability to erect other barriers to entry as part of the vertical market power analysis.²¹ The Commission requires a seller to provide a description of its ownership or control of, or affiliation with an entity that owns or controls, intrastate natural gas transportation, storage or distribution facilities; sites for generation capacity development; and physical coal supply sources and ownership of, or control over, who may access transportation of coal supplies (collectively, inputs to electric power production).²² The Commission also requires sellers to make an affirmative statement that they have not erected barriers to entry into the relevant market and will not erect barriers to entry into the relevant market.²³ In Order No. 697, the Commission adopted a rebuttable presumption that the ownership or control of, or affiliation with any entity that owns or controls, inputs to electric power production does not allow a seller to raise entry barriers but will allow intervenors to demonstrate otherwise.²⁴

¹⁹ See December 2, 2014 Filing at 2 (stating that APS does not seek to continue its market-based rate authority within the APS balancing authority area or those portions of the Phoenix Valley Load Pocket that are within the APS balancing authority area).

²⁰ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 408.

²¹ *Id.* P 440.

²² Order No. 697-A, FERC Stats. & Regs. ¶ 31,268 at P 176.

²³ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 447.

²⁴ *Id.* P 446.

20. APS states that it does not own or control, and is not affiliated with entities that own or control, intrastate natural gas transportation, storage or distribution facilities, nor do APS or any of its affiliates own or control any sources of coal supplies or transportation of coal supplies. APS states that APS and/or certain of its affiliates own or control sites that may be potentially available for generation capacity development.²⁵

21. APS affirmatively states that neither it, nor any of its affiliates, has erected barriers to entry into the market in which they are located. APS also affirmatively states that neither it, nor any of its affiliates, will erect barriers to entry into the market in which it is located.

22. Based on APS's representations, we find that APS satisfies the Commission's requirements for market-based rate authority regarding vertical market power.

B. Reporting Requirements

23. An entity with market-based rate authorization must file an Electric Quarterly Report (EQR) with the Commission, consistent with Order Nos. 2001²⁶ and 768,²⁷ to fulfill its responsibility under FPA section 205(c)²⁸ to have rates on file in a convenient form and place.²⁹ APS must file EQRs electronically with the Commission consistent

²⁵ APS states that it will report such sites in accordance with the requirements of Order No. 697. APS's most recent land acquisition report was accepted by the Commission in *Wolverine Power Supply Cooperative, Inc.*, Docket No. LA14-3-000 (Dec. 11, 2014) (delegated letter order).

²⁶ *Revised Public Utility Filing Requirements*, Order No. 2001, FERC Stats. & Regs. ¶ 31,127, *reh'g denied*, Order No. 2001-A, 100 FERC ¶ 61,074, *reh'g denied*, Order No. 2001-B, 100 FERC ¶ 61,342, *order directing filing*, Order No. 2001-C, 101 FERC ¶ 61,314 (2002), *order directing filing*, Order No. 2001-D, 102 FERC ¶ 61,334, *order refining filing requirements*, Order No. 2001-E, 105 FERC ¶ 61,352 (2003), *order on clarification*, Order No. 2001-F, 106 FERC ¶ 61,060 (2004), *order revising filing requirements*, Order No. 2001-G, 120 FERC ¶ 61,270, *order on reh'g and clarification*, Order No. 2001-H, 121 FERC ¶ 61,289 (2007), *order revising filing requirements*, Order No. 2001-I, FERC Stats. & Regs. ¶ 31,282 (2008).

²⁷ *Electricity Market Transparency Provisions of Section 220 of the Fed. Power Act*, Order No. 768, FERC Stats. & Regs. ¶ 31,336 (2012), *order on reh'g*, Order No. 768-A, 143 FERC ¶ 61,054 (2013).

²⁸ 16 U.S.C. § 824d(c) (2012).

with the procedures set forth in Order No. 770.³⁰ Failure to timely and accurately file an EQR is a violation of the Commission's regulations for which APS may be subject to refund, civil penalties, and/or revocation of market-based rate authority.³¹

24. APS must timely report to the Commission any change in status that would reflect a departure from the characteristics the Commission relied upon in granting market-based rate authority.³²

C. Docket No. EL14-98-000

25. Finally, we will terminate Docket No. EL14-98-000. Based on the above discussion and our acceptance of APS's mitigation proposal, there is no further need for the proceeding in Docket No. EL14-98-000.

The Commission orders:

(A) APS's updated market power analysis and notice of change in status for the Phoenix Valley Load Pocket, the APS balancing authority, and the TEP balancing authority are hereby accepted, as discussed in the body of this order.

(B) APS's proposed revisions to its market-based rate tariff are hereby accepted subject to conditions, effective February 2, 2015, as discussed in the body of this order.

²⁹ See *Revisions to Electric Quarterly Report Filing Process*, Order No. 770, FERC Stats. & Regs. ¶ 31,338, at P 3 (2012) (citing Order No. 2001, FERC Stats. & Regs. ¶ 31,127 at P 31).

³⁰ Order No. 770, FERC Stats. & Regs. ¶ 31,338.

³¹ The exact filing dates for these reports are prescribed in 18 C.F.R. § 35.10b (2015). Forfeiture of market-based rate authority may require a new application for market-based rate authority if the applicant wishes to resume making sales at market-based rates.

³² *Reporting Requirement for Changes in Status for Public Utilities with Market-Based Rate Authority*, Order No. 652, FERC Stats. & Regs. ¶ 31,175, *order on reh'g*, 111 FERC ¶ 61,413 (2005); 18 C.F.R. § 35.42(a) (2015).

(C) APS is directed to submit a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

(D) The section 206 proceeding in Docket No. EL14-98-000 is hereby terminated, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.