

Proposal for Establishing Qualitative Principles for the APA Process  
for Allocating Hoover Post 2017 Power  
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## BACKGROUND

Enactment of the Hoover Power Allocation Act of 2011<sup>1</sup> (the “new Hoover Act” or the “Act”) in December, 2011 marked the beginning for the Arizona Power Authority (“APA”) of the process of reallocating Arizona’s share of Hoover power.

Important elements of that process are predetermined by statute (ARS 30-101 et seq. and ARS 45-1701 et seq.), by regulation (AAC Section R12-14-101 et seq.), and by APA’s previous actions and applicable prior allocation decision making. However, some elements, particularly relating to timing but other aspects as well, depend on the actions of others, in particular Western Area Power Administration as it pursues its duties under the new Hoover Act. Other elements, some very important, are discretionary to the Arizona Power Authority in the exercise of its duty to act in the best interests of the State of Arizona.

This proposal is intended to provide Commissioners of the APA with a basis for determining “qualitative principles” in the discharge of APA’s obligations resulting from the new Hoover Act.

In the context of this proposal “qualitative principles” mean the policies to be used as the fundamental basis for allocating, in the abstract, APA’s share of Hoover power under the new Hoover Act - not as to specific power users, and not in terms of specific amounts of energy, but rather as to types of entities.

As suggested in the Commission’s May, 2012 meeting, it has become apparent that the Commission should give serious consideration to developing qualitative principles which will serve as policy to govern its actions in allocating post-2017 power. These principles should be determined in relatively short order and sooner than perhaps the Commission has heretofore thought necessary. The reasons for this are several:

- a) The new Hoover Act provides that the 66% of Schedule D power created by the Act to be allocated through Western’s marketing process (“D1”) can be offered only to entities not receiving Hoover A and B power. In the absence of a governing determination, there is some question as to whether this limitation applies to pre-2017 and post-2017 allottees of Hoover A and B, or to one or the other, rather than both. Western’s deadline for application for new Hoover D1 power, according to recent information available from Western<sup>2</sup>, is probably sometime in the Fall of 2012. The combination of the A and B

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<sup>1</sup> 43 USC Sec. 619a.

<sup>2</sup> WAPA – Desert Southwest Region, Remarketing Milestone Goals, BCP 2017 (copy of undated PowerPoint slide)

limitation with its attendant uncertainty and Western's deadline, puts APA's A and B customers, current or prospective, in a quandary that is irreconcilable without advance knowledge of APA's qualitative principles regarding APA Hoover A and B power allocations. Do post-2017 APA customers apply for Western's D1, only to be determined to be ineligible under the Act because they are current APA A or B customers, or because they later become post-2017 APA A or B customers? The same uncertainties apply to both prospective applicants for and ultimate allottees of the 11% of post-2017 Hoover D to be allocated by APA (Hoover D2).

b) During the time consumed by both the Western and APA marketing processes, power users eligible for Hoover preference power will undoubtedly need to make resource and transmission decisions for both current and long-term planning purposes. Some of those decisions will involve sizable capital investment. It follows that the longer APA's qualitative policy regarding Hoover A and B is unknown, the more dubious and uncertain those resource and transmission decisions will be. By timing its policy-making appropriately APA can avoid imposing these uncertainties.

c) APA must at some point make qualitative decisions with regard to Hoover A and B anyway – which types of entities get Hoover A and B, and which type get D2 – and APA's staff is either partly or completely hamstrung in its development of application criteria and details necessary to determine the quantitative aspects of APA's allocation decisions (how much Hoover A and B, and D2 to whom) in the absence of basic policy decisions as to eligibility from the Commission.

## QUALITATIVE POLICY DECISIONS REQUIRED OF THE APA

### DECISION 1. Decide which types of entities will be considered for post 2017 Hoover A and B.

This is a principle which can be determined in the abstract. Initially, the APA doesn't need to, and shouldn't, decide on which specific entities and amounts of power to be allocated, since that must be determined by load and other considerations – which are properly the subject of a later quantitative step which, when undertaken, will be conducted as the formal allocation process set forth by law and in APA's regulations.

### DECISION 2. Decide at what point in the Western and APA processes to allocate, in the abstract or determinatively, D2.

Assuming there are more applications for Western D1 than there is D1, many unsuccessful D1 applicants eligible for APA power might wish to apply for APA D2. However, their identities and the extent of their power requirements that are unmet by the Western D1 process can't be known until after such process is complete.

DECISION 3. Decide qualitative eligibility for APA D2 by successful or partially successful Western D1 applicants.

The APA should determine qualitatively whether successful Western D1 applicants, or partly successful applicants – meaning D1 applicants which got some but not all of requested energy - will be considered in the D2 allocation process.

DECISION 4. Decide what APA Hoover D2 is.

The new Hoover Act provides for a specific amount of Hoover A and B (95% of present A and B capacity and energy<sup>3</sup>) and a specific amount of Hoover D1 (66% of the remaining 5%) and D2 (for Arizona 11% of the 5%). Arizona's Hoover D2 is subject to the jurisdiction of the APA. APA's governing statutes with regard to allocations are based on the type of power – Title 30 governs APA's disposition of Hoover A and Title 45 governs Hoover B. Of less legal significance, perhaps, but meaningful and maybe even governing from a practical standpoint, Hoover A and B have different energy and capacity characteristics and are treated differently in their physical dispatch under certain circumstances. For legal and practical reasons, therefore, the APA must determine which part of its D2 will be allocated as under Title 30 and which under Title 45.

DECISION 5. Decide the timing of APA qualitative policy making.

The actual allocation process described in APA's governing statutes and regulations occurs when qualitative principles are applied in a subsequent quantitative step to determine which specific power users are allocated which type and what amount of Hoover power. That process is strict and determinate. However, for reasons outlined above, the timing of APA's determination of its qualitative principles has consequences for both Western D1 applications and resource planning decisions by current and prospective customers.

DECISION 6. Decide the term of post-2017 APA contracts

Western will offer a contract to APA for its part of Hoover post-2017 power for 50 years, as required under the Act. The APA must decide, qualitatively and before the formal allocation process whether to match APA allocations to the 50 year term set forth in the Act, or to make them for a lesser length.

DECISION 7. Decide whether the concept of recapture is of any use

Recapture is the forced surrender of unused APA preference power to APA for reallocation. Depending on how recapture is structured, it directly affects the term of

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<sup>3</sup> The details are slightly more complicated. Post 2017 Hoover capacity and energy allocations increase from 1,951 Mw to 2,074 Mw based on recognition of capacity improvements to Hoover generation. A new pool of power (Schedule D) was created by the Act for new entities (those not receiving Hoover A and B) by reducing the 2,074 Mw of capacity and energy otherwise available by 5%.

prospective use, and therefore can have significant long-term planning effects for customers.

DECISION 8. Decide whether APA should impose limitations on the percentage of customers that are non tax-exempt entities.

APA's previous allocation of Hoover power in 1985 limited the number of non tax-exempt entities to 25% to comply with then in effect U.S. tax code requirements governing the issuance of tax-free bonds. Should that limitation (adjusted for any changes to the U.S. tax code since) be retained?

## QUALITATIVE PRINCIPLES PROPOSED FOR THE APA

[The PRINCIPLES numbered below correspond to the DECISIONS numbered in the section above]

PRINCIPLE 1. Which Types of Entities Will be Considered for APA Hoover A & B?

There is, effectively, no new Hoover<sup>4</sup>. This means that, with regard to Hoover A and B, APA must apportion a pie that is after 2017 95% the size it was before. It must use criteria which already exist (see the second paragraph of the first page of this proposal) to do so.

In making its decisions APA must act as in the best the interests of the State of Arizona, subject to governing law and regulation and its best judgment, informed by, among other factors, past practice, as to how to allocate power to existing and prospective customers.

For guidance as to how the allocation question is answered with regard to Hoover power elsewhere, the new Hoover Act itself makes specific allocations of essentially the same capacity and energy of California's share of Hoover power to existing California contractors. Nevada state law effectuates the same result for Nevada's Colorado River Commission customers. The Act leaves allocations of Arizona Hoover power to APA. It does, however, provide guidance to APA insofar as the Act denies Hoover A and B customers eligibility for the new category of energy and capacity (Hoover D ) and requires that it be allocated to "new allottees", which, depending on its ultimate interpretation excludes either current Hoover A and B customers, or post-2017 Hoover A and B customers, or both. Either way, one might fairly draw an implication from the Act that Hoover A and B is preferentially intended for existing customers including those in Arizona.

As to guidance from Arizona's past, the APA's 1987 allocation process, described in the "Red Book"<sup>5</sup>, created the existing class of APA Hoover A and B customers. The 1987 process had the advantage of a small amount of Hoover A new to Arizona, and additional

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<sup>4</sup> See Footnote 3

<sup>5</sup> APA Final Hoover Power Marketing Plan Post-1987 dated June 7, 1985

power from Hoover power generation upratings (now referred as Hoover B) which for Arizona's portion were financed by bonds which by 2017 will have been paid for in full by both Hoover A and B customers.

The 1987 process, which operated under slightly different Arizona statutes and regulations than now exist, essentially institutionalized for a 30 year period an Arizona preference power plan which had its origins well before 1987. That plan, in the fullness of time since, has had enormous positive consequences for the State of Arizona.

In 1987, the allocations of what there was of "new" Hoover A went to new entities and "old" Hoover A went to existing APA customers. Arizona's Hoover B went, mostly, to provide power for the CAWCD after the CAP came into operation.

The energy load now served by APA to its existing customers is not simply electrons and capacity. It is, more fully, what those electrons and energy capacity are used for - irrigation pumps, electrical motors, lighting, heating, cooling, and countless other uses of the almost uncountable customers of APA's 29 different customers - uses that have been built around and built into the power that APA provides, businesses and consumers which depend on them, and, in the case of not just the CAWCD but other APA customers, urban and rural areas whose present and future land uses, past and future growth, business climate, and the like have developed around the availability of long term, reliable Hoover power.

In short, APA's prior decision making with regard to Hoover power, both in 1987 and before, has effectuated a water and power plan for Arizona that is broad in scope and deep in importance and interconnection with Arizona's economic fabric.

It is inconceivable that a subsequent allocation process by APA in discharging its obligations to the State of Arizona would destabilize the vast array of arrangements and investments that have grown out of and are a result of APA's prior decision making.

Further considerations for APA's decision making arise from language in the Act. First, the Act excludes Hoover A and B customers from eligibility for Hoover D, and vice versa, and second, the Act characterizes Hoover D entities as "new entities". If "new entities" are ineligible for Arizona A and B and if, under some interpretations of the Act, present APA Hoover A and B customers are ineligible for Hoover D post-2017, a decision by APA not to renew its existing A and B customers' allocations, in whole or in part, is a denial of any other Hoover power to such existing customers to the extent of the amount of power non-renewed.

For these reasons APA should adopt a qualitative principle to allocate post-2017 Hoover A and B as a matter of preference to existing customers, subject to demonstration by such customers during the allocation process prescribed in statute and regulations that such customers meet the requirements set forth to contract for such power, including an appropriate demonstration of load to support such allocation.

PRINCIPLE 2. At what point in the Western, APA processes should D2 be allocated?

Some or all unsuccessful, or even partially successful, D1 applicants might wish to apply for D2 power. Additionally, there is a chance, however slight, that some D1 may not be allocated by Western. If so, the amount of Arizona's D2 will change, and that amount cannot be known until after the Western D1 process. Therefore, as a practical matter, APA cannot allocate D2 power until it knows the results of Western's D1 process. APA should establish a policy now that it will wait on D2 allocations until the Western D1 process is complete.

PRINCIPLE 3. What is APA policy for considering D2 applications by successful Hoover A and B, and Western D1 applicants?

APA should consider any application for D2 power under its existing statutes and regulations, subject to a qualitative principle that Hoover A and B customers, and Western D1 customers (including wholly and partially successful applicants for Western D1) will not be considered for APA D2.

PRINCIPLE 4. What is Hoover D2 for APA's purposes?

The definition of the attributes of Arizona's Hoover D2 under the new Hoover Act is important, given APA's statutory and regulatory scheme and even the physical characteristics of the energy and capacity itself. For purposes of the APA's 2017 process, APA should adopt a qualitative policy that Hoover D2 will be allocated under Title 30 and Title 45 in the same proportion as Arizona Hoover A and B are to their sum.

PRINCIPLE 5. What should the timing of APA qualitative policy determinations be?

APA should determine qualitative principles to govern its future allocation policy before the Western D1 application deadline. It can leave its quantitative determinations under existing law and regulations until later.

PRINCIPLE 6. What should the term of post-2017 APA contracts be?

APA, in making its allocation decisions for the post 2017 period, is continuing a state water and power plan that its governance of Hoover power has effectuated since Arizona first received and put Hoover power to use. The resulting uses did not arise overnight; rather they involved enormously complicated long-term plans, commitments, and capital investment. Some of those uses are direct and easy to understand – for example preference power is used to pump water for farming. But probably the most important uses - those with the greatest long-term significance - are indirect. A good example of the indirect effects of Hoover power use in Arizona is the CAWCD. Without the Colorado River water pumped by CAWCD with, in no small part, Hoover power, Arizona might not have been able to retain its share of Colorado River water and the most populated

parts of Arizona and its largest municipalities would not have had the advantage of a Colorado River water supply to grow to the extent they have in the years since the last allocation of Hoover power by APA. The urban growth made possible by this occurred over a long period on the basis of an implicit assumption of the permanence of the power sources that bring Colorado River water to the CAWCD's service area. Therefore, given the importance of the reliability of access to Hoover power over the long term, APA should adopt a policy to issue contracts to customers upon completion of its post-2017 that are coterminous with Western's post-2017 contract with APA. It should also advocate to Western that its contract to APA be for the full term permitted by the new Hoover Act.

PRINCIPLE 7. Does the concept of recapture serve any purpose?

At present, unused, or unusable preference power in Arizona is redistributed on a short-term basis by the APA's power banking arrangements, by APA's resource exchange program, and by integrated scheduling. Otherwise, at the initiation of the customer, unused power can be surrendered to the APA for reallocation. The concept of recapture (in the mandatory sense, rather than as an optional practice), when viewed through the prism of present practice, has the potential to be highly inefficient. Post-2017 APA contract language should accommodate present practice.

PRINCIPLE 8. Should APA impose limitations on the percentage of customers that are non tax-exempt entities?

There is a high likelihood that future bond issuance for existing and new improvements attendant to Hoover power production and transmission will either be necessary or advantageous. APA should adopt the principle that its allocation decisions to non tax-exempt entities be limited so as to not prohibit the APA's ability to issue tax-free bonds.