IN THE SUPREME COURT FOR THE STATE OF ARIZONA

ROY MILLER, THOMAS F. HUSBAND, JENNIFER BRYSON, and CORPUS COMMUNICATIONS, INC.,	Case No. _____
Appellants/Cross-Appellees,	Court of Appeals Division One 1 CA-CV 09-0789
vs.	Maricopa County Superior Court Case No. CV2008-029293
ARIZONA CORPORATION COMMISSION, and KRISTIN MAYES, WILLIAM MUNDELL, JEFF HATCH-MILLER, GARY PIERCE, and MIKE GLEASON, in their official capacities as members of the Arizona Corporation Commission,	
Appellees/Cross-Appellants.	

APPELLANTS' PETITION FOR REVIEW

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Issues Presented

Issues Addressed Below

1. Where the entire cost of the Arizona Corporation Commission's Renewable Energy Standard and Tariff (REST) Rules is passed along in the form of surcharges to consumers, do consumers have standing to challenge the Rules as exceeding the Commission's limited powers?

2. Does the Commission possess constitutional authority pursuant to Ariz. Const. Art. 15, § 3 to impose sweeping and prescriptive mandates dictating the use of specified renewable energy sources by energy companies for the next decade?

3. In asserting that it possesses constitutional and statutory authority to impose the Rules, must the Commission demonstrate specific authority as to each discrete Rule, or may a court sustain the Rules as a whole?

Issue Raised But Not Addressed Below

4. In the absence of express legislative authorization of the Rules, and in the face of statutes evidencing a different policy approach, may the Commission dictate the State's renewable energy policy?

Material Facts

The Commission adopted the REST Rules on November 14, 2006 in Commission Decision 69127 and submitted them to the Attorney General for approval (I.R. 41 at 4). After initially finding that the Commission's authority for

the Rules was "vague," the Attorney General "requested specific authority from the Commission," which responded that it could not provide "an isolated source of statutory or constitutional authority." Nonetheless, "the Attorney General gave deference to the expertise of the Commission" and certified the Rules on June 15, 2007 (*id.*).

Though the new Rules supplant prior regulations, they differ from their predecessors in two crucial respects: (1) they are far more prescriptive in terms of specific renewable energy requirements than prior rules; and (2) they pass along to consumers the entire cost of compliance through a tariff (surcharge).[1] The Rules require utility companies that are subject to its jurisdiction to provide specific percentages of energy, calibrated and increasing by year, from a limited selection of renewable sources (R14-2-1804). The Rules specify rigid percentages of such energy to be transmitted from distributed sources (located on-site, such as solar rooftop panels) and non-distributed (off-site) sources) (R14-2-1805). Within the required portion of power that must be provided from distributed generation, the Rules prescribe precise percentages for commercial and residential generation (R14-2-1805(D)). Each year, companies must submit plans for Commission approval detailing how they will comply with the standards, including a line-item budget (R14-2-1813). The Commission mandates that companies pay up to half

[1] The Rules are set forth in the Appendix.

the funding for customers to install distributed energy devices (R14-2-1809); and it provides in detail how customers request funds, the minimum amount the customer must devote to the project, and how much money the customer may receive (*id.*). Utilities may be penalized for noncompliance (R14-2-1815).

The Rules establish a system of renewable energy credits, with the Commission determining terms of transfer, purchase, or sale (R-14-1803-04). Credits are given when utility companies make investments in solar electric manufacturing plants (R14-2-1807(A)). The Rules devise detailed and limited actions a utility may take to obtain extra credit multipliers (R14-2-1806 & 1807(C)).

The Commission limits the type of renewable energy technologies to those it specifies in the Rules (R14-2-1802); it further limits those (with one exception) to technologies installed after January 1, 1997 (R14-2-1802(C)); and it limits the amount of wholesale electricity sold by non-utility-owned generators that a utility may use to satisfy the distributed renewable energy requirement (R14-2-1805(E)). The Commission disqualifies energy conservation, energy management, energy efficiency, and other products that use non-renewable fuels (R14-2-1802(D)).

The Commission requires utilities to recover the reasonable and prudent costs of complying with the Rules by means of a tariff (R14-2-1808). The Rules make no exceptions nor provide any flexibility for cost considerations,

technological feasibility, adequacy or reliability of supply, or prices of competing energy sources. The Rules provide for waivers for "good cause," but they set forth no specifications for when such waivers should be provided (R14-2-1816).

During consideration of the REST Rules, the Commission staff "estimated the yearly costs" of distributed and non-distributed energy "above the Market Cost of Comparable Conventional Generation through 2025," plus the costs of compliance with the Rules, at $1.2 billion (I.R. 19, Exh. 11, App. B pp. 72-73). That figure does not include the "projected cost of the infrastructure needed to supply the renewable energy required to meet the RES," which the staff considered "unknown" (I.R. 19, Exh. 11, App. B pp. 68 & 70). The Commission's Economic, Small Business and Consumer Impact Statement states, "The cost to consumers will also vary over time and will directly follow the costs to the Affected Utilities" (I.R. 19, Exh. 11, App. C, p. 2).

The Rules became effective in August 2007, and the first APS surcharge was imposed on ratepayers in May 2008 (Ct. App. Op. at 3). This lawsuit was filed in June 2008 by residential and small-business consumers of Arizona Public Service (APS) who are subject to current and constantly escalating utility rate surcharges, alleging that the REST Rules exceed the Commission's limited authority under the Arizona Constitution and statutes. The trial court found that "the dissemination of the REST Rules falls within the Commission's ratemaking authority" under the

Arizona Constitution, a conclusion that "makes it unnecessary to review the parties' arguments of statutory authority for the promulgation of the REST Rules" (I.R. 41 at 8). The Court of Appeals affirmed, holding that consumers "lack standing to assert the managerial interference doctrine" (Ct. App. Op. at 15), and that the Rules are within the Commission's constitutional authority (*id.* at 16-27). This timely appeal followed.[2]

Reasons for Granting the Petition

I. THE CASE PRESENTS ISSUES OF STATEWIDE IMPORTANCE.

Nearly 20 years have passed since this Court has addressed "fundamental legal questions regarding the Commission's constitutional power," which the Court has characterized as an "urgent question with great importance to the people of this state." *Ariz. Corp. Comm'n v. State ex. rel. Woods*, 171 Ariz. 286, 288, 830 P.2d 807, 809 (1992).

In the interim, the Court of Appeals on at least two occasions has applied *Woods* to carefully scrutinize challenged Commission regulations. In both *US West Comms., Inc. v. Ariz. Corp. Comm'n*, 197 Ariz. 16, 3 P.3d 936 (App. 1999), and *Phelps Dodge Corp. v. Ariz. Elec. Power Coop., Inc.*, 207 Ariz. 95, 83 P.3d

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[2] As they did in the Court of Appeals, petitioners request costs and attorney fees pursuant to A.R.S. §§ 12-348 and the private attorney general doctrine (see Appellants' Combined Reply on Appeal and Answer on Cross-Appeal ("Reply Brief") at 44-47).

573 (App. 2004), the court found that some of the Commission rules challenged in those cases were reasonably necessary steps in ratemaking while others were not.

The REST Rules go far beyond any attempted prior exercise of Commission power that ever has been allowed. By mandating specified uses of prescribed renewable energy sources by all of the utility companies within its jurisdiction extending far into the future, the Commission has insinuated itself deeply into managerial decisions that are outside of the Commission's limited grant of constitutional and statutory authority. It has created renewable energy policy for the State, and has exercised police power to directly regulate the managerial functions of utility companies, both of which are the exclusive province of the Legislature. And it has ensured that every penny of the massive cost of the REST Rules will be shouldered by utility ratepayers, to the tune of at least $1.2 billion beyond market costs of conventional generation (I.R. 19, Exh. 11, App. B pp. 72-73). For all those reasons, this case presents important constitutional questions with substantial real-world ramifications for utility consumers throughout Arizona.

II. THE COURT BELOW INCORRECTLY DECIDED IMPORTANT LEGAL QUESTIONS.

On each of the issues presented, the Court of Appeals strayed from decisions of this Court and, on key issues, from its own rulings in *US West* and *Phelps Dodge*. This Court and the Court of Appeals have applied a consistent rule of law regarding the Commission's constitutional powers since *Corp. Comm'n v. Pac.*

Greyhound Lines, 54 Ariz. 159, 94 P.2d 443 (1939). By upholding Rules that exceed the boundaries of power consistently applied by the courts for 72 years, and by curtailing the standing of consumers to challenge them, the Court of Appeals untethered the Commission from its constitutional moorings.

A. Consumer standing. The creation of an independent Corporation Commission was one of several constitutional mechanisms designed to create a wall of separation between corporations and the levers of government power. See, e.g., John D. Leshy, *The Arizona Constitution: A Reference Guide* at 15 (1993) (describing provisions "limiting the power of private corporations, mostly aimed at protecting consumers"). Specifically, the constitutional convention delegates "had a general mistrust of government," and created the Commission "to shield the consumer against overreaching by public service corporations" that might dominate the Legislature. Deborah Scott Engelby, Comment, "The Corporation Commission: Preserving Its Independence," 20 *Ariz. St. L. J.* 241, 242-43 (1988); see also *Woods*, 171 Ariz. at 290-92, 830 P.2d 811-13.

Given that the Commission's *raison d'etre* is to protect consumers, it is odd and very troubling that the Court of Appeals plowed new jurisprudential ground by essentially eliminating consumer standing to challenge Commission rules that exceed its powers, especially where the cost of those rules is borne by consumers.

A.R.S. § 40-254 provides standing to review Commission actions to "any

party in interest." Plainly, consumers who shoulder the costs of the Rules are a party in interest.[3] However, noting that standing to sue is not the same as standing to raise a particular argument (Ct. App. Op. at 14), the Court of Appeals observed that "most, if not all, utilities affected by the REST Rules worked with the Commission during the extended evaluation and comment period preceding the rules' adoption" (*id.* at 13). Because the companies did not challenge the Rules as an impermissible invasion of their managerial prerogatives, the court held "that Plaintiffs lack standing to assert the managerial interference doctrine in these proceedings" (*id.* at 15). Specifically, the court held that "Plaintiffs' challenge to R14-2-1805 is based on the managerial interference doctrine, which they may not invoke" (*id.* at 23; see also *id.* at 25 (pertaining to the challenge to R14-2-1809)).

This was error for two important reasons. First, given the enormous disparity of resources between utility companies and consumers, and the far greater likelihood that utilities will be deeply involved in the regulatory process, the Commission has the duty "to protect the individual consumers' financial interests." Engelby at 245. "Obviously, the Commission must be independent of the companies it regulates." *Id.* at 260.

But what if it is not? As the Court of Appeals acknowledged, utility

[3] Indeed, the Arizona Consumers Council filed a consolidated action challenging the Commission's rules in *Phelps Dodge*, 207 Ariz. at 102, 83 P.3d at 580.

companies were actively involved in the creation of the REST Rules. It should concern the Court that the result of that process was to create a tariff mechanism through which all of the mandated costs are passed along to consumers (R-14-2-1808). It is not surprising that utilities would sacrifice management prerogatives for guaranteed revenue increases. In that context, the consumers who are bearing the cost of the Commission's failure to protect their interests should have standing to raise claims that the utilities have traded away.[4]

At a more fundamental level, though, the Court of Appeals erred in denying standing because the management interference doctrine is not a discrete cause of action. Rather, anything that lies outside the Commission's authority resides within the realm of management discretion, subject only to valid police power regulation by the Legislature. So that when the Court of Appeals holds that consumers have no standing to assert management interference, it is the same as holding that consumers have no standing to challenge the Commission's jurisdiction at all.

Thus the inquiry in these cases is whether challenged rules "so interfere with management functions that they constitute an attempt to control the corporation

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[4] This is somewhat akin to a derivative suit, in which a shareholder has standing to raise claims that the company declines to pursue. See also *Mtn. States Tel. & Tel. Co. v. Ariz. Corp. Comm'n*, 160 Ariz. 350, 356, 773 P.2d 455, 461 (1989) (holding company has standing to assert third-party free-speech rights in challenge to Commission orders).

rather than an attempt to control rates." *Woods*, 171 Ariz. at 297, 830 P.2d at 818. That determination defines the universe of possibilities. If the regulation falls within the realm of management discretion, the "paramount power to make all rules and regulations governing public service corporations not specifically and expressly given to the commission by some provision of the constitution, rests in the legislature." *Pac. Greyhound*, 54 Ariz. at 176-77, 94 P.2d at 450.

Petitioners have alleged that the Rules fall outside the Commission's constitutional authority. By definition, that means the displaced decision-making properly resides in the companies, unless it is regulated by the Legislature. If consumers do not have standing to challenge such rules, the core purpose of creating the Commission to protect consumers is thwarted. For these reasons and those set forth in our Reply Brief (at 34-39), it is imperative that the Court grant the petition to reverse this holding.[5]

B. Constitutional authority. The Court of Appeals (Op. at 20) found "a relationship between the REST rules and electric rates." Assuming the surcharges are "rates,"[6] of course "a relationship exists": the REST Rules inexorably lead to

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[5] Although the interest of judicial economy would be served by reviewing all of the issues presented herein, the Court could grant review solely on this threshold issue and remand the remainder of the issues to the Court of Appeals for consideration of the arguments that it incorrectly held the petitioners did not have standing to make.

[6] The test for whether a charge is a tax, which the Commission may not impose, or

higher rates. If that cause-and-effect relationship is all that is required to bring a regulation within the Commission's constitutional parameters, then it can decree anything so long as it leads to changed rates.

That is not the applicable test. The Commission has "no implied powers and its powers do not exceed those to be derived from a strict construction of the Constitution and implementing statutes." *Comm. Life. Ins. Co. v. Wright*, 64 Ariz. 129, 139, 166 P.2d 943, 949 (1946). The "Commission has no regulatory authority under article 15, section 3 except that connected to its ratemaking power." *Woods*, 171 Ariz. at 294, 830 P.2 at 815. Accordingly, the challenged Rules are valid only if they are "reasonably necessary steps in ratemaking." *Id.*

That rule embodies three analytical components: that the outcome of the process is ratemaking, that the Rules are steps in ratemaking, and that the steps are reasonably necessary.[7] The Court engaged in no such searching analysis. For the reasons set forth in our Court of Appeals Brief (at 9-22) and Reply Brief (at 2-19), the Rules exceed the Commission's constitutional authority.

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a rate (i.e., fee for service), is set forth in *May v. McNally*, 203 Ariz. 425, 430-31, 55 P.3d 768, 773-74 (2002). Here, where the tariffs applicable to certain ratepayers are used to subsidize the installation of solar systems for the primary benefit of only some utility customers (see R14-2-1809), they do not fit the definition of rates.

[7] "We interpret necessity in light of the framers' intent of the Commission's function," which is "to protect consumers from abuse and overreaching by public service corporations." *Woods*, 171 Ariz. at 295, 830 P.2d at 816.

C. Rule-by-rule analysis. Departing from its practice in *US West* and *Phelps Dodge*, the Court of Appeals did not apply the constitutional analysis to each of the contested rules. Petitioners identified 16 discrete Rules (Appellants' Brief at 18-19) that on their face go beyond reasonably necessary steps in ratemaking, interfere with management discretion, conflict with and/or are not authorized by statute, and impose costs on consumers. The Court of Appeals examined only two (Op. at 20-27), concluded that petitioners lacked standing to argue management interference (*id.* at 22-23), and upheld them despite the fact that they far exceeded in scope and intrusiveness any Commission regulations ever sanctioned by Arizona courts.

When a set of Rules is as sweeping as these, it is vital that the Court assess them one-by-one. Otherwise, the Commission easily could exceed its powers simply by inserting invalid regulations into otherwise valid ones. Although petitioners singled out two of the Rules as "poster-children" for impermissible regulation (Appellants' Brief at 19-20), others clearly exceed the Commission's constitutional authority as well. For instance, R14-2-1807(A), -1807(B), and -1804(F) establish a regime of manufacturing credits when utilities invest in or provide incentives to solar energy manufacturing plants in Arizona. That is on its face classic energy policy legislation, not a reasonably necessary step in ratemaking.

Even as to the specific Rules the Court of Appeals reviewed, it failed to enforce the line between "an attempt to control the corporation rather than an attempt to control rates." *Woods*, 171 Ariz. at 297, 830 P.2d at 818. The court's failure to do so emanates from its decision not to allow petitioners to make that argument, but in any event its analysis was faulty. Its review of R14-2-1805, which requires exactly 50 percent of distributed resource generation to come from commercial sources, is a classic management decision and appears to have no relevance to rates. When confronted with the fact that the Commission made no findings to justify the requirement, the court noted (Op. at 23) that a lack of findings is not a jurisdictional benefit, but then simply hypothesized rationales that might justify the Rule. As for R14-2-1809(B), which establishes requirements by which consumers may obtain reimbursement for renewable energy systems, the court concludes (*id.* at 26) that the requirements are not unduly intrusive because, after all, "[t]he rule leaves it to the utilities to process such applications." This extreme deference to Commission regulations and the resulting cost burden to consumers has never before been countenanced by Arizona courts.

The Court of Appeals failed to adequately scrutinize a vast enlargement of the Commission's authority, notwithstanding the black-letter law that the "scope of an agency's power . . . may not be expanded by agency fiat." *Cochise Cty. v. Ariz. Health Care Cost Containment Syst.*, 170 Ariz. 443, 445, 825 P.2d 968, 970 (App.

1991).

D. Statutory authority. The Legislature retains the "paramount power to make all rules and regulations governing public service corporations not specifically and expressly given to the commission by some provision of the constitution." *Pac. Greyhound*, 54 Ariz. at 176-77, 94 P.2d at 450. "In the exercise of the regulatory power, the legislature may interfere with the management of public utilities whenever public interest demands, but . . . no inference will be adjudged by implication beyond the clear letter of a statute." *So. Pac. Co. v. Ariz. Corp. Comm'n*, 98 Ariz. 339, 343, 404 P.2d 692, 695 (1965).

The Legislature has conferred upon the Commission certain limited powers beyond ratemaking, including remedial authority regarding service, facilities, or methods that are "unjust, unreasonable, unsafe, improper, inadequate or insufficient." A.R.S. § 40-321(A). However, such authority must be predicated upon specific findings that a company will fail to provide adequate service,[8] and not upon Commission orders based "upon a finding of facts by means of a crystal ball." *So. Pac.*, 98 Ariz. at 346, 404 P.2d at 697.

At the same time, the Legislature has adopted a statutory scheme to promote renewable energy through tax credits and other means that differs sharply with the

[8] To the contrary, as the Court of Appeals acknowledged (Op. at 15 n. 6), APS plans to develop renewable energy resources in excess of Commission requirements.

Commission's command-and-control approach. Renewable energy policy is the exclusive province of the Legislature. For the reasons set forth in petitioners' Court of Appeals Brief (at 22-33) and Reply Brief (at 19-26), the Rules are not expressly authorized by statute.

Conclusion

For all of the foregoing reasons, this case merits this Court's review.

RESPECTFULLY SUBMITTED May 9, 2011 by:

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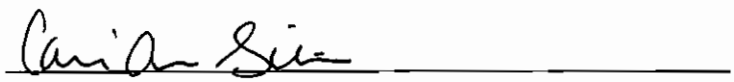

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