



Resources Division

Mr. Robert G. Gray

Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

SUBJ: Notice of Inquiry, Gas Infrastructure Matters in Arizona

Dear Mr. Gray,

By this letter, the City of Mesa Utilities Department (City) provides its response to the Arizona Corporation Commission (Commission) Notice of Inquiry. Rather than answer each question specifically, the City respectfully submits a general overview with its perspective.

The City is a Full Requirements (FR) shipper on the El Paso Natural Gas Company (El Paso) system. The City provides natural gas sales and transportation services to over 40,000 customers in Maricopa and Pinal Counties. Typical of most Arizona natural gas utilities, the City's annual system load factor is about 30%. This low annual load factor requires the City to secure firm resources with upstream pipelines and natural gas supplies to cover peak day requirements in excess of 35,000 MMBtu's per day in the heating season down to 5,000 MMBtu's per day in the cooling season.

In the near future the City and other East of California (EOC) shippers taking service from El Paso will be required by order of the Federal Energy Regulatory Commission (FERC) to convert their FR service to Contract Demand (CD) service. With this conversion EOC customers will be losing all of the benefits FR service provided to a low load factor natural gas utility. However, the conversion may also provide incentives for the development of new interstate pipelines and storage facilities may mitigate the loss of some benefits under FR service.

Factors that need to be addressed include: 1. access to marketplace; 2. environmental permit process; 3. competitive rates compared to the status quo; 4. regulation at the state and/or federal levels; and 5. fair and equitable treatment for all stakeholders.

The major metropolitan areas of Arizona have experienced phenomenal growth over the past decade and some forecasts expect this growth to slow somewhat but maintain growth levels higher than national averages. Additional electric and natural gas resources will be needed to meet these growth requirements. Local Distribution Companies such as the City need access to firm interstate pipeline transportation services supplies. The City's electric utility also needs access to economic supplies of natural gas to fuel its natural gas fired generators.

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Currently there is only one major interstate pipeline serving the majority of natural gas consumers in Arizona. This situation will most certainly change, mainly because of the forced conversion of FR customers to CD service on El Paso. Opportunities for the construction of new interstate pipelines and storage facilities will provide the market new avenues for solving complex energy decisions to keep energy costs down and maintain reliability.

Ultimately the market will decide whether new infrastructure is required to meet growing demands. The City will always explore alternatives to the current situation to mitigate energy costs and increase competition on the wholesale energy market in Arizona. The Commission and other market participants have an opportunity to devise a sound strategy and implement policy that will ensure benefits to all Arizona gas consumers. The numerous stakeholders include LDC's, electric utilities with regulated generation assets, unregulated affiliates of Arizona owned electric utilities with generation assets, unregulated merchant companies and a host of large industrial companies. All of these entities need to secure reliable upstream assets to successfully meet their business goals.

One of the determining factors for a successful project is location in respect to the market. A new interstate pipeline that crosses northern Arizona will not provide benefits to the majority of Arizona. The same holds true for storage facilities. Storage needs to be close to the market in order to be economic. Additionally, the additional costs of interstate transportation will factor into the economics if the storage is not directly connected to the customer. As in real estate, gas infrastructure is all about location. The need to locate facilities in proximity to the market can complicate the environmental permitting and regulatory approval process and impact the timely development of a valuable facility.

If the Commission decides to conduct workshops the City would like to participate in the discussion. The challenge is to develop strategies and policies that are fair to all and for all consumers in Arizona to enjoy the benefits of competition.

Sincerely,



Randy Bee  
Management Assistant II