

State of Arizona  
Office  
of the  
Auditor General

**PERFORMANCE AUDIT**

**RESIDENTIAL UTILITY  
CONSUMER OFFICE**

**AND**

**RESIDENTIAL UTILITY  
CONSUMER BOARD**

**Report to the Arizona Legislature  
By Douglas R. Norton  
Auditor General**

**June 1999  
Report No. 99-10**



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AUDITOR GENERAL

**STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL**

DEBRA K. DAVENPORT, CPA  
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June 17, 1999,

Members of the Arizona Legislature

The Honorable Jane Dee Hull, Governor

Mr. Greg Patterson, Director  
Residential Utility Consumer Office

Mr. James Spezzano, Chairman  
Residential Utility Consumer Board

Transmitted herewith are two reports of the Auditor General, Performance Audits of the Residential Utility Consumer Office (RUCO) and the Residential Utility Consumer Board (Board). These reports are in response to a May 27, 1997, resolution of the Joint Legislative Audit Committee. These performance audits were conducted as part of the Sunset review set forth in A.R.S. §§41-2951 through 41-2957.

The first report focuses on RUCO's ability to effectively advocate on behalf of residential utility consumers before the Arizona Corporation Commission. A review of closed rate cases in which RUCO intervened since January 1995 showed that RUCO is often successful at having its position adopted by the Arizona Corporation Commission and limiting rate increases for residential consumers. Additionally, RUCO monitors or analyzes non-rate cases to ensure residential customers' interests are protected. Although RUCO has been effective thus far, a dynamic regulatory environment is heightening the need for greater emphasis on strategic planning and formal processes. Therefore, RUCO should develop a comprehensive strategic plan and formalize its processes for determining in which rate and non-rate cases it should intervene and for evaluating the effectiveness of its intervention efforts.

June 17, 1999

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We also found that stronger fiscal monitoring is needed for RUCO to accurately determine its annual assessment. For the past few years, RUCO has incorrectly calculated its annual assessment, which has created a large and unnecessary fund balance.

The second report addresses the Residential Utility Consumer Board's inability to effectively fulfill the requirements of its statutory mandates. While statute requires the Board to advise RUCO on rate cases, the Board's efforts in recent years have had minimal impact. The Board has asserted the lack of impact was due in large part to a lack of support from RUCO. Board members maintain that RUCO has not responded to their requests for information on various issues. However, Board minutes do not contain such instances.

The Board has suggested it can best serve the public by advising it of cases under review by RUCO and advising RUCO of consumer concerns or questions. However, it has taken few steps to effectively fulfill this role. Additionally, inadequate processes and information have contributed to the Board's limited ability to assist in the preparation of RUCO's budget and to review court actions filed by RUCO. Therefore, the Board should work with RUCO to develop and implement various processes that will enable it to better fulfill its responsibilities.

As outlined in its response, RUCO agrees with and has agreed to implement all recommendations addressed to it. The RUCO Board agrees in concept with most of our recommendations. However, it believes statutory changes are needed to strengthen the Board's role before our findings can be addressed.

My staff and I will be pleased to discuss or clarify items in these reports.

These reports will be released to the public on June 18, 1999.

Sincerely,

A handwritten signature in dark ink, appearing to read "Douglas R. Norton", written in a cursive style.

Douglas R. Norton  
Auditor General

Enclosure

# SUMMARY

The Office of the Auditor General has conducted a performance audit and Sunset review of the Residential Utility Consumer Office (RUCO) and the Residential Utility Consumer Board (Board) pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee. This audit was conducted as a part of the Sunset review set forth in Arizona Revised Statutes (A.R.S.) §§41-2951 through 41-2957.

## **Residential Utility Consumer Office**

The Legislature established RUCO in 1983 (A.R.S. §40-462) to represent the interests of residential utility consumers in regulatory proceedings involving public service corporations before the Arizona Corporation Commission, Arizona's rate-setting body for electricity, gas, telecommunications, water, and sewer utilities. Statute authorizes RUCO to prepare and present briefs, arguments, and proposed rates or orders, and to intervene or appear on behalf of residential utility consumers.

### **RUCO Effective in Advocating on Behalf of Residential Consumers (See pages 7 through 14)**

RUCO's intervention into utility cases has provided benefits for residential consumers. A review of all 14 closed rate cases in which RUCO intervened between January 1995 and December 1998 showed that RUCO is often successful at having its position adopted for such matters as costs to be included in determining utility revenue requirements and requested rates of return. For example, for the 7 rate cases that proceeded fully through the hearing process, the Corporation Commission adopted RUCO's position in whole or in part for 105 (64 percent) of the 164 separate contested case issues involving plant and equipment values, revenues, expenses, or rate of return. RUCO's intervention also appears to affect final decisions on revenue increases. For example, in the 7 cases that were settled through negotiation rather than through a formal hearing, 5 had revenue increases that were close to what RUCO proposed. Additionally, in nearly all (13 of the 14) cases analyzed, the company received a smaller revenue increase than it had initially requested due to the efforts of Commission staff, RUCO, and/or hearing officers. For these 13 cases, the companies requested over \$100 million in revenue increases, but the Commission approved revenue increases of only \$44.5 million, thus reducing the companies' requested revenue collectively by almost 56 percent.

In addition to RUCO's efforts to limit rate increases for residential consumers, RUCO monitors or analyzes non-rate cases to ensure residential customers' interests are protected. Non-rate cases comprise approximately 67 percent of the cases in which RUCO intervenes and typically involve issues pertaining to rulemaking, pilot programs, financing, and company sales and mergers. RUCO's involvement can range from comprehensive analysis, such as RUCO's intervention in electric restructuring, to analysis of a single issue, such as gas company requests for temporary price increases because of higher prices being charged by suppliers. RUCO monitors these cases to ensure that residential customers will not pay more than their fair share of a price increase.

Although RUCO has been effective thus far, a dynamic regulatory environment is heightening the need for greater emphasis on strategic planning and formal processes. Recent changes and growth in the State's utility industries contribute to new challenges and a demanding workload for RUCO. Not only has the number of regulated utilities more than doubled in the past four years, growing to nearly 1,200 companies at the end of 1998, the number and diversity of applications have also increased. RUCO does not have a comprehensive strategic plan that could help identify key areas for advocacy. Components of this plan could include establishing a broader mission statement, identifying its stakeholders and the services it will deliver, and the direction in which it should take its case intervention efforts. Additionally, RUCO can benefit from more formal processes for determining where its resources can be best applied and for evaluating the effectiveness of its intervention efforts.

### **Stronger Fiscal Monitoring Needed to Accurately Determine Assessment (See pages 15 through 18)**

For the past few years, RUCO has incorrectly calculated its annual assessment, which has created a large and unnecessary fund balance. RUCO receives its funding from an annual assessment against utility companies, an amount paid ultimately by consumers. Under state law, RUCO is to reduce the size of this assessment if it carries over money from one year to the next. However, for fiscal years 1998 and 1999, RUCO assessed utility companies the full amount of its spending authority granted by the Legislature. For example, despite having a \$448,015 fund balance at the end of fiscal year 1998, RUCO sought an assessment of the full \$941,400 in spending authority granted for fiscal year 1999. If it had subtracted the fund balance, the assessment would have been only \$493,385.

RUCO needs to improve its fiscal monitoring procedures to better monitor its revolving fund and fiscal activities. Additionally, to comply with state law, RUCO needs to reduce future assessments to account for the carryover balance in its revolving fund.

## **Other Pertinent Information**

### **(See pages 19 through 21)**

During the audit, other pertinent information was collected regarding current efforts to restructure the electric utility industry in Arizona and RUCO's role in these efforts. Numerous parties, including representatives from utilities, RUCO, and large industries, as well as the Arizona Corporation Commission, have worked since 1994 to implement electric restructuring, which would allow consumers the opportunity to choose their supplier of electricity. While electric competition was to be phased in beginning January 1, 1999, a decision by the Arizona Supreme Court prohibited electric competition from beginning as planned. Consequently, in January 1999, the Commission suspended the electric competition rules for further study and possible revision, a process that may take from six months to a year. Meanwhile, RUCO continues to participate in the State's efforts to introduce electric competition to ensure residential consumer interests are represented and protected.

### **Residential Utility Consumer Board**

The Board was established in conjunction with the RUCO in 1983 and consists of five citizen members appointed by the Governor, who serve staggered five-year terms. The Board is required to meet monthly and is authorized to advise RUCO on all matters relating to rate making or rate design and involving public service corporations. The Board is statutorily empowered to instruct RUCO's director to withdraw any court action filed by RUCO, and to prepare, jointly with the director, RUCO's proposed annual budget request.

## **The Board Ineffectively Fulfills Its Role**

### **(See pages 29 through 34)**

In recent years, the Residential Utility Consumer Board has not effectively fulfilled the requirements of its statutory mandates. While statute requires the Board to advise RUCO on rate cases, the Board's efforts in recent years have had minimal impact. RUCO has evolved into a highly technical agency to perform its work in rate cases and does not rely on Board advice concerning the technical merits of rate cases. Instead, the Board has suggested it can best serve the public by advising it of cases under review by RUCO and advising RUCO of consumer concerns or questions. However, it has taken few steps to effectively fulfill this role. Questions among board members concerning its role and authority, board vacancies, and members' poor meeting attendance have contributed to board inaction.

Additionally, the Board has been limited in its ability to appropriately fulfill its oversight duties of RUCO, which include assisting with the preparation of RUCO's biennial budget

request and requiring RUCO to withdraw filed court actions that it deems are inappropriate. However, the Board is not involved in the preparation of RUCO's budget, but only in reviewing and approving a budget prepared by RUCO. Additionally, the Board has had limited opportunity to require RUCO to withdraw court actions it has filed. Inadequate policies and procedures for involving the Board in the budget preparation process and notifying the Board in a manner that facilitates its review of court actions RUCO's director has filed contribute to these circumstances.

To improve the Board's performance, it should work with RUCO to develop and implement various processes for fulfilling its consumer and RUCO advisory roles. For example, to encourage increased public awareness and participation, processes should be developed for scheduling and selecting appropriate sites for board meetings and speaking engagements, as well as informing the public of these board activities. Additionally, the Board should work with RUCO to establish processes to ensure timely dissemination of information specific to preparing the budget and when court actions are filed. Lastly, the Board should work with RUCO to identify and provide a dedicated, part-time staff person to the Board to facilitate its activities.

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## **Residential Utility Consumer Office**

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# INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit and Sunset review of the Residential Utility Consumer Office (RUCO) pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee. This audit was conducted as a part of the Sunset review set forth in Arizona Revised Statutes (A.R.S.) §§41-2951 through 41-2957. This is the third performance audit of RUCO. In 1986, the Auditor General completed the first performance audit of RUCO (Auditor General Report No. 86-6) and in 1989 the second (Auditor General Report No. 89-6).

## **Arizona's Utility Regulatory Process**

Although RUCO is part of the State's utility regulation process, it is not the agency that makes decisions about utility rates and service quality. The Arizona Corporation Commission (Commission) has jurisdiction over the quality of service and rates charged by public service (investor-owned) utilities. According to the Commission, it currently regulates 1,188 public utilities divided into the following areas: electricity (21 utilities), gas (11), water and/or sewer (369), and telecommunications (787).<sup>1</sup> By state law, public utilities are regulated monopolies given the opportunity to earn a fair and reasonable return on their investments. What is fair and reasonable in any particular case has been and always will be open to debate in rate hearings before the Commission. Arizona is one of seven states in which its utility regulatory body is created in state constitution. Because of its status as a constitutional body, the Commission functions in three capacities: adopting rules and regulations; administering and enforcing such rules; and sitting as a tribunal and making decisions in contested matters, such as determining a utility's rates.

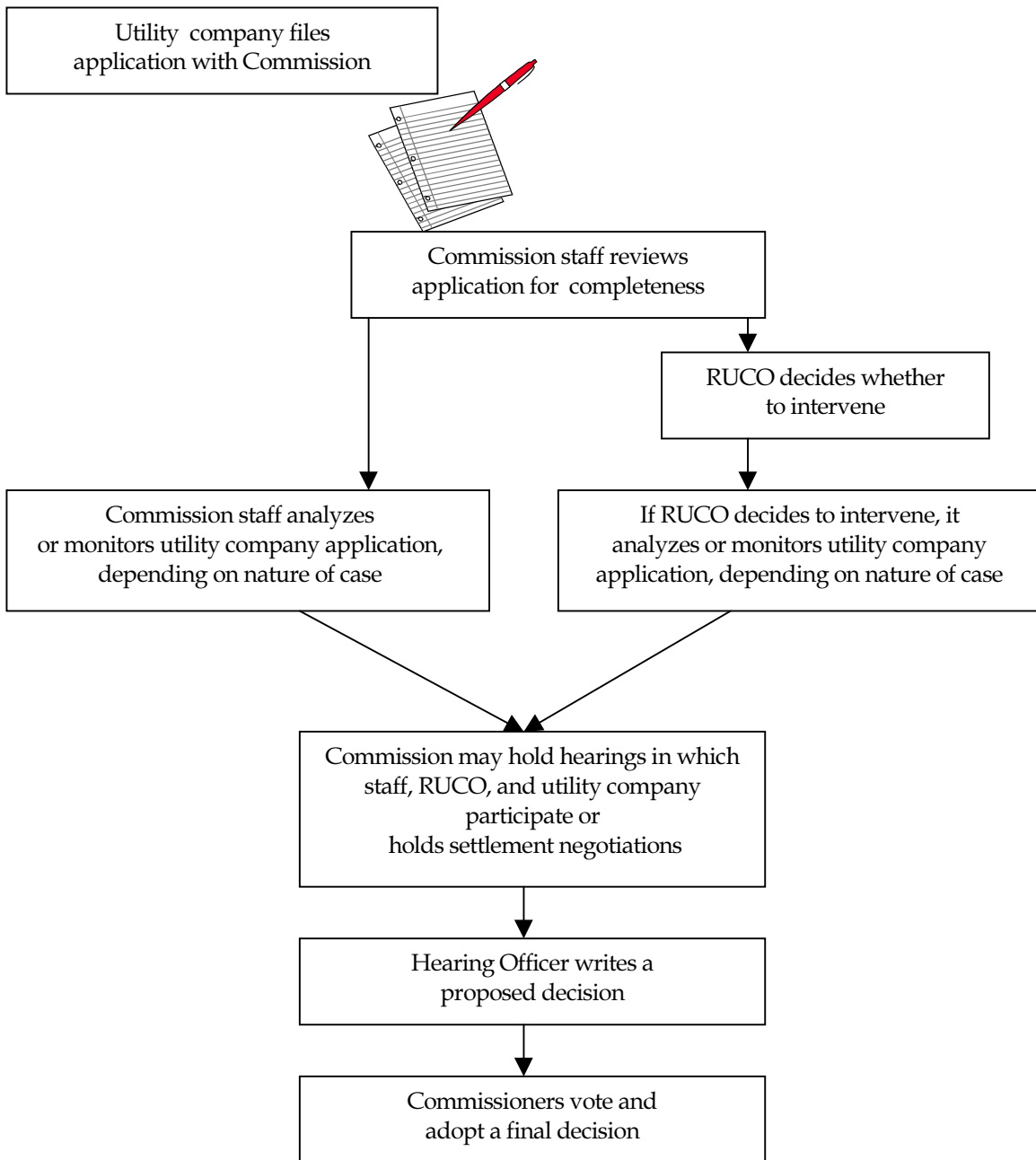
As illustrated in Figure 1 (see page 2), the utility regulatory process begins when a utility company files an application with the Commission. The Commission may conduct public hearings, examine evidence and testimony presented by various concerned parties, and make final decisions on utility companies' proposed rate adjustments, applications to start up or expand service, and financing changes. The Commission's Utilities Division makes specific recommendations to the commissioners to assist them in reaching decisions regarding public utility rates, utility finance, and quality of service.

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<sup>1</sup> Many of these telecommunication public utilities consist of individually owned and regulated pay phones.

**Figure 1**

**Arizona Corporation Commission  
Utility Regulatory Process  
As of March 1999**



Source: Auditor General staff analysis of Residential Utility Consumer Office (RUCO) Fiscal Year 1997-98 Annual Report.

## **RUCO's Role in the Regulatory Process**

The Legislature established RUCO in 1983 (A.R.S. §40-462) to represent the interests of residential utility consumers in regulatory proceedings involving public service corporations before the Arizona Corporation Commission. A.R.S. §40-464 defines the power and duties of the RUCO director, including the director's authority to:

*"Research, study and analyze residential utility consumer interests . . . Prepare and present briefs, arguments, proposed rates or orders and intervene or appear on behalf of residential utility consumers before hearing officers and the corporation commission as a party in interest and also participate as a party in interest pursuant to §§40-254 and 40-254.01 in proceedings relating to rate making or rate design and involving public service corporations."*

To perform its advocacy role, RUCO conducts a preliminary review of every utility rate increase application filed with the Commission, regardless of the utility's size. In addition, RUCO reviews other company applications (such as starting up or expanding service, financing, and mergers) to determine potential impact on residential consumers. As illustrated in Figure 1 (see page 2), if RUCO determines that the application merits further attention, it requests permission from the Commission to intervene as an advocate on behalf of residential consumer interests. Intervention status provides RUCO the right to do the following: 1) Obtain additional information from the utility, 2) submit written briefs, present evidence, and cross-examine other parties' witnesses, and 3) present recommendations via written testimony and by testifying at hearings. RUCO can also file a suit that appeals a Corporation Commission decision to either the State's Superior Court or Court of Appeals.

## **Staffing and Budget**

For fiscal year 1998-1999, RUCO was authorized 11 full-time equivalent (FTE) positions: a director, a deputy director, three attorneys, an engineer, three rate analysts, an administrative services officer, and a legal secretary.

RUCO operates using revenues it receives from an assessment against public service corporations serving residential customers. The Legislature first determines RUCO's spending authority, then RUCO determines the amount of the assessment. Once RUCO forwards the assessment amount to the Corporation Commission, the Commission levies the assessment against public service corporations with gross operating revenues in excess of \$250,000. Each utility's total assessment is limited to two-tenths of 1 percent of its gross operating



revenues of the preceding year and is paid by the utility's customers.<sup>1</sup> The Legislature appropriates RUCO's share of the monies received through this assessment, which are placed into the Residential Utility Consumer Office Revolving Fund. Revolving Fund monies do not revert to the General Fund. See Finding II (pages 15 through 18) for additional information. RUCO revenues and expenditures for fiscal years 1997 through 1999 are shown in Table 1 (see page 5).

## **Audit Scope and Methodology**

This performance audit and Sunset review was conducted to evaluate RUCO's operations, focusing on two objectives: to assess RUCO's effectiveness in representing residential utility consumer interests, and to determine the adequacy of RUCO's monitoring of its revolving fund. To address these objectives, many methods were used, including:

- Conducting a content analysis of the Corporation Commission's final orders for 47 RUCO interventions (representing all closed interventions for calendar years 1995 through 1998), to determine RUCO's impact;
- Collecting and analyzing Corporation Commission filing information to determine the frequency of RUCO interventions;
- Analyzing financial documents and assessment and budget practices to determine the adequacy of RUCO's monitoring of its revolving fund;
- Contacting 9 other states to learn best practices regarding how other states perform advocacy, measure impact, and determine the necessity for intervention<sup>2</sup>; and
- Interviewing various individuals involved in the utility regulatory process, including commissioners, hearing officers, and Commission staff; various consumer advocacy representatives; and all 11 members of RUCO's staff.

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<sup>1</sup> Utility companies pay a similar assessment to fund Corporation Commission operations. The assessment limit applies to the combined amount.

<sup>2</sup> Nine states having an organization similar to RUCO were identified and contacted: Colorado, Illinois, Iowa, Kansas, Kentucky, New York, Ohio, Oregon, and Utah.

**Table 1**  
**Residential Utility Consumer Office**  
**Statement of Revenues, Expenditures, and Changes in Fund Balance**  
**Years Ended or Ending June 30, 1997, 1998, and 1999**  
**(Unaudited)**

	<b>1997</b> <b>(Actual)</b>	<b>1998</b> <b>(Actual)</b>	<b>1999</b> <b>(Estimated)</b>
Revenues:			
Intrastate Utility Assessment <sup>1</sup>	<u>\$925,923</u>	<u>\$941,388</u>	<u>\$940,602</u>
Expenditures:			
Personal services	405,547	454,328	535,400
Employee related	75,925	80,218	103,000
Professional and outside services	440	6,378	
Travel, in-state	5,416	8,763	10,000
Travel, out-of-state	8,540	3,354	4,600
Other operating	128,204	140,677	109,800
Capital outlay	20,709	36,436	9,600
Professional witnesses <sup>2</sup>	<u>85,569</u>	<u>124,101</u>	<u>170,000</u>
Total expenditures	<u>730,350</u>	<u>854,255</u>	<u>942,400</u>
Excess of revenues over (under) expenditures	195,573	87,133	(1,798)
Fund balance, beginning of year	<u>483,610</u>	<u>679,183</u>	<u>766,316</u>
Fund balance, end of year	<u>\$679,183</u>	<u>\$766,316</u> <sup>3</sup>	<u>\$764,518</u>

<sup>1</sup> Assessment revenues are reported in the year they are available for expenditure.

<sup>2</sup> Fiscal year 1997 and 1998 amounts include expenditures totaling approximately \$73,700 and \$114,100, respectively, of nonlapsing monies authorized in prior fiscal years.

<sup>3</sup> Approximately \$318,300 of the 1998 fund balance consisted of unexpended monies from 1995 through 1998 authorized for professional witnesses. The remaining balance is subject to legislative authorization prior to being expended.

Source: The Arizona Financial Information System (AFIS) *Accounting Event Extract File, Revenues and Expenditures by Fund, Program, Organization, and Object* report, *Companion Transaction Entry/Transfer* documents, and *Trial Balance by Fund* report for the years ended June 30, 1997 and 1998, and as of November 30, 1998, for the year ending June 30, 1999; and RUCO's *Professional Witness Expenditures for FY 1995 – FY 1999* listing. Fiscal year 1999 estimated expenditures were obtained from the *State of Arizona Appropriations Report* for the year ending June 30, 1999.

This report presents findings and recommendations in two areas:

- RUCO has benefited residential consumers by advocating for limited utility rate increases, but to ensure it remains effective, RUCO should conduct strategic planning and formalize its case selection and review processes; and
- RUCO should reduce its extensive carryover balance in its revolving fund and otherwise improve its fiscal management.

This report also contains Other Pertinent Information regarding Arizona's progress with electric restructuring, including RUCO's role in this process.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Residential Utility Consumer Board members, the Director and staff of RUCO, and the Arizona Corporation Commissioners and their staff for their cooperation and assistance throughout the audit.

## FINDING I

### RUCO EFFECTIVE IN ADVOCATING ON BEHALF OF RESIDENTIAL CONSUMERS

RUCO intervention into utility cases has provided favorable benefits for residential consumers. Its actions have contributed to lower rate increases and fewer costs passed on to consumers. However, a rapidly changing regulatory environment, particularly with regard to electricity and telecommunications providers, poses a challenge to RUCO's continued ability to represent consumer interests. Therefore, to ensure it remains effective, RUCO should formalize its processes for deciding where to focus its efforts, how to evaluate the success of its work, and how to be involved in consumer education.

#### RUCO Interventions Benefit Consumers

Analysis of the rate cases in which RUCO has intervened showed that the agency's intervention has positive benefits for consumers. The Commission often accepts RUCO's findings and recommendations on specific matters that affect a utility's revenue requirement. Additionally, RUCO intervenes on consumers' behalf in non-rate cases, such as mergers or new pilot programs.

*RUCO's rate case intervention addresses utilities' revenue needs and rate requests*—Since the Corporation Commission establishes each utility company's rates, any change in rates must receive Commission approval. Thus, each company periodically files a rate adjustment application, which is presented and analyzed in two distinct phases:

#### ■ Revenue — Is an increase in the company's revenue requirement justified?

First, the Corporation Commission must decide whether to authorize an increase in the company's revenue requirement. The company's application presents its rationale for the proposed revenue increase, using various financial figures as support, such as building and equipment values; revenues and expenditures for the preceding 12 months; and rate of return (the amount of profit the company will be allowed to pay its investors). After the company's application is filed, both the Commission's Utilities Division staff and RUCO perform separate analyses and propose adjustments to the company's figures. Commission staff and RUCO then submit their analyses to a Commission hearing officer, where both parties and the company present and debate their positions at an open hearing. The hearing officer then forwards a recommendation for Commission approval.

■ **Rates—What change in rates is necessary to achieve this revenue increase?**

Next, if the Corporation Commission approves an increase in the company's revenue requirement, the Commission must also approve a new set of rates that will allow the company to generate the increased revenue. This rate increase may be applied to one or more of the customer classes (i.e., residential, commercial, or industrial). Therefore, similar to the revenue analysis, both Commission staff and RUCO present their proposed set of rates and the hearing officer forwards a recommendation to the Commission for approval.

*Analysis of interventions shows RUCO has an effect on rate cases*—To assess RUCO's success in having the Commission adopt its position, auditors reviewed all 14 closed rate cases in which RUCO intervened during the four-year period January 1995 through December 1998. While RUCO analyzed all 14 cases, a Commission hearing officer resolved the various contested positions and issued a recommendation for Commission approval in only 7 cases. The other 7 cases were settled by the parties to the case (company, RUCO, and Commission staff) and the hearing officer forwarded the settlement to the Commission for approval. This analysis showed that RUCO's work had an effect on contesting specific issues, limiting utilities' revenue increases, and affecting rate increases.

■ **RUCO successfully contests various issues**—Overall, RUCO is successful at having its position adopted for a variety of issues, including adjustments to company proposed building and equipment values, revenues and expenditures, and requested rate of return. When Commission staff, RUCO, or both contest a company's particular position, they can propose an alternative position for that issue. For example, in its 1998 application, Southwestern Telephone Company included in its labor expense salaries for three employee positions that were eliminated midway through the year. While RUCO and Commission staff both recommended decreasing the total labor expense by \$34,121 and \$29,996, respectively, the Commission preferred RUCO's method, modifying it slightly to \$34,031.

Among the 7 rate cases that proceeded through the hearing officer process, this analysis identified a total of 164 issues in which RUCO could have analyzed and presented a position. As illustrated in Figure 2 (see page 9), the Commission adopted RUCO's position in whole or in part for 105 (64 percent) of the 164 separate issues. For 21 (12.8 percent) of the 164 issues, the Commission did not adopt the position advocated by RUCO and for the remaining 38 (23.2 percent) issues, the Commission's order indicates that RUCO did not provide an alternative position to the Company's proposal.

■ **RUCO contributes to lowering the company's overall revenue increase**—In addition to effecting change for individual issues, RUCO contributes to lowering the company's proposed revenue increase. In nearly all (13 of the 14) cases analyzed, the company received a smaller revenue increase than it had initially requested due to the efforts of Commission staff, RUCO, and/or hearing officers. For these 13 cases, the companies' total proposed revenue increase was over \$100 million. However, the Commission ap-

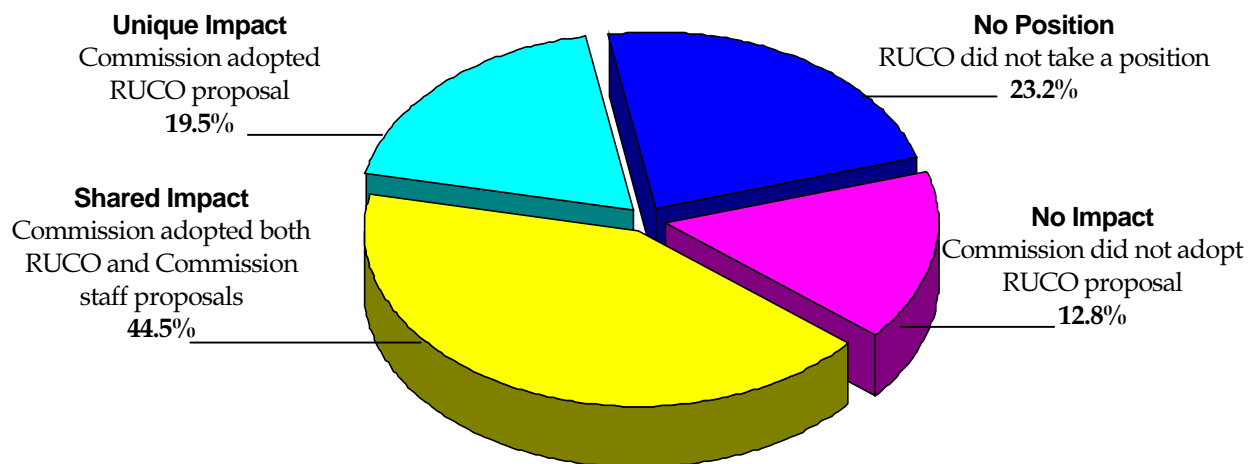
proved a total revenue increase of only \$44.5 million, thus reducing the companies' requested revenue collectively by almost 56 percent.

RUCO's contribution to lowering the company's proposed revenue is particularly evident among the 7 settlement cases auditors reviewed. While settlement negotiations represent a collaborative effort in which RUCO actively participates, RUCO's proposed revenue increase figures were close to what the parties agreed upon for 5 of the 7 settlements. For example, in response to Rio Rico Water Company's requested revenue increase of \$446,000, the Commission staff and RUCO recommended alternative increase amounts of \$225,000 and \$190,000, respectively. In March 1996, the parties settled on a \$195,000 revenue increase. Similarly, in response to Citizens Utility Company Gas Division's requested revenue increase of \$7 million, RUCO's analysis determined that the company's increase should be no more than \$2.7 million, with residential rates increasing by no more than 6.3 percent. In October 1995, the parties settled on a \$2.7 million revenue increase and a 6 percent increase among all consumers.

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**Figure 2**

**Residential Utility Consumer Office  
Impact on Litigated Case Issues  
Years Ended December 31, 1995 through 1998**



Source: Auditor General staff analysis of Arizona Corporation Commission decisions regarding litigated rate cases in which RUCO intervened for years ended December 31, 1995 through 1998.

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- **RUCO's impact in establishing favorable residential rates is more difficult to assess**— Available evidence, while limited, suggests that RUCO's recommendations, along with those of the Commission's staff, affect the Commission's rate decisions. The Commission's final orders do not contain sufficient information to determine RUCO's ability to limit residential rate increases that result from the approved revenue increase. First, the Commission's final orders do not consistently identify each party's proposed rates nor do they identify why the Commission adopted a particular set of rates. Additionally, since each party's proposed rates correspond to their proposed revenue increase, any deviation from the proposed revenue increase would suggest that a party's proposed rates would also not be adopted. However, where information was available in the final order, the Commission generally adopts elements of both the Commission staff's and RUCO's proposed rates.

*RUCO's intervention into non-rate cases seeks to protect a variety of consumer interests—*

In addition to RUCO's efforts to limit rate increases for residential consumers, RUCO monitors or analyzes non-rate cases to ensure residential customers' interests are protected. Non-rate cases comprise approximately 67 percent of the cases in which RUCO intervenes and typically involve issues pertaining to rulemaking, pilot programs, financing, and company sales and mergers. RUCO's involvement can range from comprehensive analysis, such as RUCO's intervention in electric restructuring, to less involvement through monitoring, where RUCO will monitor the case proceedings to identify any potential concerns to the residential customers. If problems are identified, RUCO will conduct further analysis, file briefs, or testify before the Commission about its concerns. The following are two examples of non-rate intervention activities:

- **Purchased Gas Adjustor**—RUCO intervenes in these cases when a company requests a temporary increase in the price of gas (Purchased Gas Adjustor). The increased gas prices result from weather changes or open market availability that affect what a utility pays for the gas. RUCO monitors the case to ensure that residential customers will not pay more than their fair share of the price increase. In addition, RUCO continues to monitor the case to ensure that rates will be reduced when gas prices have returned to their normal levels.
- **Rulemaking for electric restructuring**—Since 1995 RUCO has intervened in all rulemaking and associated cases before the Commission pertaining to electric restructuring in the State. As such, RUCO has performed various analyses and filed testimony to ensure that as electric competition is introduced, residential interests are protected. (See Other Pertinent Information, pages 19 through 21, for additional information about electric restructuring.)

## **RUCO Should Formalize Strategic Planning and Other Processes**

Changes sweeping the utility industry provide strong indications that RUCO should carefully plan for the future. Recent changes and growth in the State's utility industries contribute to a more challenging and demanding workload for agencies advocating on behalf of utility consumer interests. As such, RUCO should develop a formalized, comprehensive strategic plan that identifies key areas for advocacy. Additionally, RUCO should formalize its case selection and case outcome evaluation processes, as well as more fully develop its plans for providing consumer education.

*Arizona's changing and growing utility industry creates challenges*—In Arizona and nationally, the utility industry is undergoing considerable change, potentially challenging RUCO's ability to continue to effectively manage its workload and advocate on behalf of residential consumers. In Arizona, the number of regulated utility companies has more than doubled in the past four years, increasing from approximately 500 companies in 1995 to nearly 1,200 companies at the end of 1998 with the majority of this growth occurring in the telecommunications industry. Meanwhile, the State's electric industry is undergoing restructuring, which will eventually allow other states' electric companies to potentially conduct business in Arizona. In fact, two companies have already requested and received approval from the Commission to become certified electric service providers capable of competing and operating in the State. Additionally, as shown in Table 2 (see page 12), the number of utility applications filed with the Corporation Commission has grown by 60 percent during the last four years, increasing from 524 in 1995 to 838 in 1998.

In addition to the growing number of applications, utility companies are also filing a greater diversity of cases that involve issues such as arbitration, financing, mergers, start-ups, pilot programs, and rate and restructuring issues.

*Strategic planning can enhance RUCO's advocacy efforts*—To respond effectively to the dynamic change occurring in Arizona's utility regulatory environment, RUCO should place greater emphasis on its long-range and strategic planning. Currently, RUCO does not have a comprehensive strategic plan to guide its efforts. Such an approach may include RUCO's external and internal operating environment as well as describing RUCO's short and long-term plans. Additionally, RUCO has not developed a vision or mission statement that captures the needs of its stakeholders and reflects the dynamic utility regulatory environment in which it operates. Without a formal strategic plan, RUCO has no comprehensive method for defining, prioritizing, balancing, and evaluating its growing advocacy role.



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**Table 2**

**Residential Utility Consumer Office  
Number of Utility Applications and RUCO Interventions  
Filed with the Corporation Commission  
Years Ended December 31, 1995 through 1998**

Utility	1995		1996		1997		1998	
	Apps.	Intvs.	Apps.	Intvs.	Apps.	Intvs.	Apps.	Intvs.
Electric <sup>1</sup>	47	4	48	3	71	4	76	14
Gas	15	3	20	4	17	2	25	4
Sewer/Water	173	11	163	2	206	4	205	11
Telecommunications <sup>2</sup>	<u>289</u>	<u>11</u>	<u>426</u>	<u>18</u>	<u>522</u>	<u>2</u>	<u>532</u>	<u>1</u>
Totals	<u>524</u>	<u>29</u>	<u>657</u>	<u>27</u>	<u>816</u>	<u>12</u>	<u>838</u>	<u>30</u>

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<sup>1</sup> Electric industry restructuring that began in 1997 caused increased RUCO activity in 1998.

<sup>2</sup> Telecommunications industry deregulation in 1995 caused increased RUCO activity in 1995 and 1996.

Source: Auditor General staff analysis of Arizona Corporation Commission utility company application data and RUCO's case intervention database for years ended December 31, 1995 through 1998.

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Some states that are also undergoing significant regulatory change are using strategic planning to enhance their state's consumer advocacy efforts. These states are focusing on new activities to ensure that any change in utility company revenue structures will not have an impact on the safety, reliability, and overall quality of utility services; to more clearly define their mission and objectives; and to better serve their customers. For example, Maine's consumer advocate is working with its public utility commission to realign the advocacy responsibility. The commission will focus on utilities regulation while the advocacy agency will seek to protect competition, provide residential consumers with the tools to make informed choices, and protect consumers from market abuses.

*Formalizing internal processes can enhance RUCO's strategic capabilities*—To ensure effective use of its limited resources in the future, RUCO should formalize its procedures for deciding which cases to select for detailed study and possible intervention, evaluating the results of these efforts, and plans for consumer education. Specifically, RUCO should:

- **Formalize its case selection guidelines**—Although RUCO has a basic process in place for case selection, which incorporates key factors and relies on the experience and judgment of staff, it has not formalized this process. Currently, RUCO considers the size of the utility company, amount of rate increase sought, number of customer complaints involving the company, importance of case issues, and the availability of resources in determining when to intervene in a case. However, RUCO has not formalized this process, a process that also relies on the experience and judgment of current staff. Should RUCO

lose any staff that assist in this process, its ability to continue to appropriately select cases for intervention may be impacted. Therefore, RUCO should document its process and criteria used for selecting cases for intervention.

- **Formalize its process for assessing case outcomes**—RUCO should also formalize its process for critiquing its performance in cases in which it intervenes. Currently, RUCO informally assesses its performance to gain insight into how it may need to modify its activities to improve its impact in utility rate and non-rate cases. Additionally, as reflected in its annual reports, RUCO measures its success by taking the difference between the company's proposal and the Commission's final order. However, other than this measure, RUCO does not employ a formal process to document its performance on individual issues in a case, the effectiveness of other parties in the case, or other factors that may affect Commission decisions. Therefore, RUCO should consider developing a mechanism to evaluate its performance and to document pertinent information. This mechanism should include written procedures for evaluating each type of case in which it intervenes; reviewing components of the case including building and equipment values, revenue and expenditures, and rate-setting issues for rate cases; and specifying its potential concerns and critiquing case outcomes in relation to those concerns for non-rate cases.
- **Develop plans for its consumer education program**—Lastly, RUCO should more formally develop its plans to become involved in consumer education. Although RUCO is in the initial phases of launching a consumer education program and has received approval to expend \$50,000 annually in fiscal years 2000 and 2001 for consumer education purposes, it has yet to develop plans that specify what such a program will accomplish or what activities it will entail, such as distributing pamphlets or creating a newsletter. Additionally, while RUCO has discussed developing a Website on the Internet to provide information, RUCO has no formal plans for development or implementation.

## Recommendations

1. To ensure that RUCO continues to beneficially advocate on behalf of residential consumers, RUCO should develop a more comprehensive strategic plan that identifies key areas for advocacy in Arizona's dynamic utility regulatory environment. Components of this plan could include:
  - a. Establishing a broader mission statement;
  - b. Defining its stakeholders and customers;
  - c. Identifying what services it will deliver; and
  - d. Determining the focus of future advocacy efforts.
2. RUCO should formalize its case selection process by documenting the process it employs and the factors it considers when assessing cases for possible intervention;
3. RUCO should formalize its process for measuring and critiquing its impact on cases to continue to maximize RUCO interventions on behalf of residential consumers; and
4. RUCO should define its consumer education focus, including development of a Website.

## **FINDING II**

### **STRONGER FISCAL MONITORING NEEDED TO ACCURATELY DETERMINE ASSESSMENT**

For the past few years, RUCO has incorrectly calculated its annual assessment, which has created a large and unnecessary fund balance. By statute, RUCO should be reducing this balance by adjusting the size of the annual assessment paid by utility companies, and ultimately by consumers. Therefore, RUCO needs fiscal monitoring procedures to better monitor its revolving fund and accurately determine its annual assessment.

#### **Revenues Derived from Utility Assessment**

RUCO operates using revenues it receives from an annual assessment against public service corporations. The Legislature establishes RUCO's annual spending authority based upon RUCO's biennial budget requests. Under A.R.S. §§40-401.01 and 40-409, RUCO must subtract any monies remaining in its revolving fund from this spending authority to arrive at the assessment amount and forward this amount to the Corporation Commission. The Corporation Commission then levies the assessment against public service corporations with revenues in excess of \$250,000.

For fiscal years 1995, 1996, 1998, and 1999, the Legislature has allowed RUCO to carry over certain monies in its revolving fund into the next year instead of reducing its assessment by these unexpended monies. Statute requires that when calculating the assessment, RUCO must subtract only its unexpended *lapsing* monies, while being allowed to carry forward any monies specifically identified by the Legislature as *nonlapsing*. Beginning with RUCO's fiscal year 1995 appropriation, legislative session law has generally identified monies appropriated specifically for professional witnesses as nonlapsing monies to cover contracts that extend beyond the fiscal year. These services are generally for professional witness/expert service to assist with case analyses and testimony.

## Inadequate Fiscal Monitoring Contributes to Incorrect Assessments

Because of inadequate fiscal monitoring, RUCO has not correctly determined its assessment, which resulted in a balance of \$448,015 in lapsing monies at the end of fiscal year 1998. In recent years, RUCO has not followed the statutory requirement to reduce its assessment and has received more revenue than necessary to finance its operations. This inadequate fiscal monitoring also creates inaccuracies and confusion regarding RUCO's fiscal status.

### *Over-assessment due to unexpended monies not being subtracted as prescribed by statute—*

For at least fiscal years 1998 and 1999, RUCO has not complied with statutory requirements to reduce annual assessments by an amount equal to unexpended lapsing monies remaining in RUCO's revolving fund. For example, as illustrated in Table 3, the Legislature approved \$941,400 in spending authority for RUCO's fiscal year 1999 operations. Despite having \$448,015 in lapsed monies available in its revolving fund at the end of fiscal year 1998, RUCO instructed the Corporation Commission to assess and collect \$941,400 from utilities. However, consumers needed to pay only \$493,385 to raise RUCO's fiscal year 1999 spending authority. Similarly, RUCO instructed the Corporation Commission to assess the approved spending authority for fiscal year 1998, failing to subtract any unexpended lapsing monies that existed in the revolving fund. This practice results in a large fund balance. Taking action to reduce the balance would not only comply with the statute but also provide a substantial one-time reduction in the assessment, a cost that is ultimately passed on to the consumer.

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**Table 3**

**Residential Utility Consumer Office  
Determination of Statutorily Allowed Assessment  
Years Ended or Ending June 30, 1998 and 1999  
(Unaudited)**

	<b>1998</b>	<b>1999</b>
Legislatively approved spending authority	\$946,400	\$941,400
Less: Revolving Fund prior year-end unexpended lapsing monies	<u>443,472</u>	<u>448,015</u>
Statutorily allowed assessment	<u>\$502,928</u>	<u>\$493,385</u>

Source: The Arizona Financial Information System (AFIS) *Status of Appropriations and Expenditures* report for the fiscal years ended or ending June 30, 1998 and 1999.

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*RUCO's inadequate fiscal monitoring creates inaccuracies and confusion—*Inadequate fiscal monitoring has contributed to RUCO's inability to comply with statutory requirements for determining its assessment. RUCO officials have been largely unaware of how and when the Commission levies the assessment; whether the full assessment is collected;

when and what deposits are made to its revolving fund; and what the revolving fund balance is at any particular time. Such basic fiscal knowledge is essential for RUCO to ensure that it assesses consumers correctly, and that monies are deposited appropriately and are available to cover expenditures.

RUCO's difficulties in this regard became particularly evident during fiscal year 1999. In January 1999, RUCO believed that although it was midway through fiscal year 1999, it had received only \$2,300 of its \$941,400 assessment and that its fiscal year 1999 operations were being financed from its carryover fund balance. In fact, RUCO's fiscal year 1999 assessment had already been levied, significantly collected, and deposited in RUCO's revolving fund in June 1998. This discrepancy arose mainly because the Corporation Commission mislabeled the fiscal year 1999 assessment deposited into RUCO's revolving fund as fiscal year 1998 monies. However, RUCO's inability to monitor the activity in its revolving fund exacerbated the situation.

## **Steps Needed to Ensure Proper Fiscal Monitoring**

RUCO needs to improve its revolving fund management, thereby maximizing the use of assessment monies. Specifically, the following changes are needed:

*Compute assessment according to statute*—RUCO should follow statute and ensure that the assessment amount it forwards to the Corporation Commission accounts for any unexpended lapsing monies remaining in its revolving fund. Specifically, RUCO should subtract monies estimated to remain in its revolving fund at the end of the fiscal year from its legislatively approved spending authority to arrive at the assessment amount. This amount should then be forwarded to the Commission for assessment.

*Establish better financial management procedures*—Additionally, RUCO needs to formally establish guidelines that require adequate monitoring of RUCO's revolving fund and other financial activities. Specifically, RUCO should develop policies and procedures for monitoring its fiscal activities, providing the statutorily allowed assessment amount to the Commission, and monitoring its revolving fund balance. In addition, RUCO needs to establish and implement reconciliation practices to ensure monies are properly assessed, collected, and deposited. Furthermore, RUCO needs to enhance its monitoring of revolving fund transactions so that it can ascertain its financial status at any given time.

## **Recommendations**

1. RUCO should abide by A.R.S. §§40-401.01 and 40-409 when determining its annual assessment amount. Specifically, RUCO should reduce each year's assessment by an amount equal to any monies estimated to remain in its revolving fund at the end of the fiscal year.
2. To ensure proper fund management, RUCO should strengthen its financial practices by:
  - a. Developing policies and procedures to monitor fiscal activities;
  - b. Assigning responsibility within policies and procedures for performing various fiscal activities;
  - c. Reconciling assessments, collections, and deposits; and
  - d. Monitoring revolving fund transactions.

## OTHER PERTINENT INFORMATION

During the audit, other pertinent information was gathered regarding current efforts to restructure the electric utility industry in Arizona and RUCO's role in these efforts.

### The Electric Restructuring Process

Similar to what happened in the telephone industry, efforts are underway to create a competitive marketplace for the provision of electricity. Electric competition, with the goal of providing lower costs to all users, presents a dynamic change for the electric utility industry. While federal regulation opened the door for electric restructuring, it is up to each state as to when and how it wishes to pursue implementation.

*How electricity is now provided and how it will be provided under electric competition—*Electric restructuring is changing the electric utility industry by creating a competitive environment in order to provide electricity customers with lower rates, new optional services, and new technology. Electric competition changes electric monopolies into free-market companies that must compete with other suppliers for customers. Currently, utility companies produce the electricity, act as the sole supplier to consumers, and distribute the power through their transmission networks. As electric competition is introduced, consumers will still use their current utility for transmitting and distributing electricity, but will be able to choose the company that supplies their electricity. Under electric competition, power supply companies will produce electricity and sell it wholesale, retail companies will buy power from suppliers and market it to consumers, and transmission and distribution companies will deliver electricity to the home or business over existing lines.

Before electric competition can be provided to consumers, critical issues of “stranded costs” and “unbundling” by electric utilities must be addressed. These issues could result in additional expense to the electric consumer and offset any potential benefit the consumer would otherwise receive from restructuring.

- **Stranded costs**—Stranded costs represent investments in plants, equipment, and improvements that the electric utility made in the past, but may not necessarily be recoverable in a deregulated environment. Utilities made these investments expecting to recover these costs by passing them on to their customers. However, in a competitive market, owners of these plants may not be able to charge high enough rates to recover their costs and still compete for customers.
- **Unbundling**—“Unbundling” refers to separating the total process from generation to distribution for the purpose of separate pricing. Before electricity suppliers can offer competitive rates, generation charges need to be separated from transmission and distribution



charges and the billing process determined. Resulting electric bills may include a line item for each charge or the consumer may receive two bills, one from the company that supplies the electricity and one from the local electric company that delivers the electricity. However, with either billing process, consumers should have better information regarding their electric rates.

***National efforts to restructure electricity***—Federal regulations provided the groundwork for states to pursue electric restructuring. The Public Utility Regulatory Policies Act (PURPA) of 1978 provided an opportunity for a shift in the way utility companies generated electricity. In addition to the traditional method where the utility generated, transmitted, and distributed power, PURPA allowed companies to generate and wholesale electricity to other utilities without also having to transmit and distribute power. However, while PURPA created the opportunity to generate and wholesale electricity, the National Energy Policy Act of 1992 established the federal government's intention to stimulate competition by requiring existing utilities to allow wholesale suppliers to transmit electricity over the existing utilities' lines for a reasonable price.

While federal regulation opened the door for electric restructuring, each state must decide when and how to pursue implementation. Although the process by which any state pursues electric restructuring is similar, each state's utility regulatory environment determines its progress. While nearly all states have at least begun the process, approximately half are now considering legislation to provide for electric competition. The remaining states have either passed rules for implementing electric restructuring, or are involved in pilot programs and/or phasing in electric competition. The states that have made greater progress tend to be the states with higher consumer energy costs. California, Arizona, and Nevada are in the forefront in the West. In fact, in 1998 California was the first state to allow its customers to choose their electric supplier.

## **Status of Arizona's Efforts to Implement Electric Restructuring**

Various parties have worked for several years to implement electric restructuring in the State. Specifically, the Arizona Corporation Commission and other interested parties have worked since 1994 to implement electric restructuring. Additionally, RUCO is actively participating in these efforts to ensure residential consumer interests are represented and protected.

***Electric restructuring in Arizona***—In June 1994, the Arizona Corporation Commission (Commission) decided to study and consider electric restructuring in Arizona. Since then, representatives from utilities, RUCO, electric cooperatives, large industries, mines, unions, tribal councils, energy marketers, consumer groups, and state agencies have participated in a series of workshops and Commission hearings to discuss electric restructuring for all utility consumers. The Commission adopted electric competition rules in December 1996, which provided a framework for electric utility companies to operate in a competitive market. In response to

these rules, Arizona's existing electric companies filed "cost recovery plans" to address stranded costs and unbundling issues. In addition, electric companies in other states became eligible to file applications with the Commission to become certified electric service providers capable of competing and operating in the State.

Introduction of electric competition in Arizona is temporarily on hold. The Commission had adopted rules allowing utilities to open electric competition to consumers effective January 1, 1999. However, on January 4, 1999, the Commission suspended the electric competition rules for further study and possible revision.

***Present and future role of RUCO in electric restructuring***—To represent residential consumer interests, RUCO has taken an active role in the restructuring process by engaging in a variety of activities. These include:

- **Participating in forums**—RUCO is involved in a number of forums. For example, RUCO participates on the Salt River Project Consumer Advisory Board, which prepares and disseminates restructuring information to its residential consumers. Additionally, to help provide the residential consumer with the lowest rates and the highest quality of service, RUCO is a voting member of Desert Star, a membership cooperative made up of transmission providers and interested parties. It is expected that Desert Star will eventually operate the transmission system in Arizona, New Mexico, and parts of Nevada and Texas to ensure that each electricity supplier has access to transmission facilities.
- **Intervening in and analyzing Commission cases involving electric restructuring**—RUCO has intervened in cases involving electric restructuring before the Commission. Specifically, RUCO has intervened in all phases of the rulemaking proceeding, attempting to assure that all residential consumers are free to choose an electric supplier. RUCO has also intervened in cases involving new suppliers of electricity for authority to serve customers in Arizona. So far, the Commission has authorized four additional electric service suppliers to operate in the State. Additionally, RUCO has intervened in proceedings involving stranded costs to ensure that any unnecessary costs are not being passed on to the residential consumer.
- **Representing residential interests in workshops and on committees**—To ensure that residential consumers are represented, RUCO participates in Commission workshops and sits on committees. Generally, these workshops and committees have discussed issues such as metering and billing, quality of service, stranded costs, ensuring service for low income customers, and consumer education.
- **Performing consumer outreach and education activities**—Although RUCO has no statutory mandate to provide consumer education or outreach programs, RUCO is active in certain areas. For example, RUCO has taken part in media presentations and has been quoted in newspaper articles advocating its position to protect the residential consumer from higher costs, unfair treatment by the utilities, or in areas of service quality.

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# SUNSET FACTORS

In accordance with A.R.S. §41-2954, the Legislature should consider the following 12 factors in determining whether the Residential Utility Consumer Office (RUCO) should be continued or terminated.

## **1. The objective and purpose in establishing RUCO.**

The Legislature established RUCO in 1983 to represent the interests of residential utility consumers of regulated utilities in proceedings before the Arizona Corporation Commission. Prior to RUCO's existence, the Corporation Commission's Utilities Division staff was responsible for considering residential consumers' needs when making recommendations to the Commission. However, because Commission staff were also charged with making recommendations that considered a broad base of interests, including shareholder and company as well as commercial and industrial customers, they could not exclusively represent the interests of residential consumers.

According to the act establishing RUCO, the agency is intended to represent the interests of residential consumers, critically analyze proposals made by public service corporations to the Commission, and formulate and present recommendations to the Commission. As such, RUCO is authorized to prepare and present briefs, arguments, and proposed rates or orders, and to intervene or appear on behalf of residential utility consumers before hearing officers and the Commission.

## **2. The effectiveness with which RUCO has met its objective and purpose and the efficiency with which the agency has operated.**

RUCO has generally met its objectives and purpose by intervening in matters involving residential utility consumers before the Corporation Commission. In addition, RUCO has actively participated in various forums to represent residential consumers in electric restructuring matters. However, the audit found that RUCO could more effectively meet its objectives by:

- Undertaking additional activities, such as developing a comprehensive strategic plan and formalizing its case selection process to better position itself for the future (see Finding I, pages 7 through 14).
- Improving its fiscal monitoring to comply with statutes for determining its annual assessment. In recent years, RUCO's annual assessment has been higher than necessary, generating a large and growing fund balance (see Finding II, pages 15 through 18).

**3. The extent to which RUCO has operated within the public interest.**

RUCO has operated within the public interest by representing residential consumers in rate cases before the Corporation Commission. RUCO intervenes to ensure that requested rate increases are fair for the company and do not over-burden residential consumers. In addition, RUCO's interventions can result in non-monetary benefits. For example, RUCO's intervention activities related to the State's move toward electric restructuring have advocated for increased consumer education and greater residential participation in electric deregulation (see Other Pertinent Information, pages 19 through 21).

**4. The extent to which rules and regulations promulgated by RUCO are consistent with the legislative mandate.**

Although the director has the statutory authority to promulgate rules, RUCO has not done so. Our review did not reveal the need for RUCO to develop any rules. RUCO has, however, participated in the Corporation Commission's process to develop rules governing electric restructuring in Arizona (see Other Pertinent Information, pages 19 through 21).

**5. The extent to which RUCO has encouraged input from the public before promulgating its rules and regulations and the extent to which it has informed the public as to its actions and their expected impact on the public.**

Since RUCO has chosen not to promulgate rules, RUCO has not needed to encourage input from the public before promulgating rules and regulations. According to RUCO, the public has been informed of the agency's activities primarily through the media. Additionally, the agency is considering other activities that would keep residential customers informed of important utility issues that affect them, such as developing a newsletter or glossary of terms that explains electric restructuring. However, while RUCO has identified a need for increased consumer education, it has not developed plans such as establishing a Website or developing brochures to accomplish this (see Finding I, pages 7 through 14). In addition, Corporation Commission hearings and meetings are open to the public and can provide attendees with an opportunity to learn more about RUCO's role and participation in the utility rate-making process and to voice their concerns and problems regarding utility services.

**6. The extent to which RUCO has been able to investigate and resolve complaints that are within its jurisdiction.**

RUCO does not have the statutory authority to investigate or resolve consumer complaints. Occasionally, however, RUCO receives complaints from residential consumers. When this occurs, RUCO refers these consumers to the Corporation Commission's Consumer Services Division.

- 7. The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation.**

This factor is not applicable since RUCO is not a regulatory agency. RUCO's own staff attorneys, pursuant to A.R.S. §41-192, provide legal representation for the agency in proceedings before the Corporation Commission and the courts.

- 8. The extent to which RUCO has addressed deficiencies in its enabling statutes which prevent it from fulfilling its statutory mandates.**

RUCO does not believe there are any deficiencies in its enabling statutes which prevent it from fulfilling its mandates and therefore, has not sought changes in the last five years. According to RUCO, its ability to participate in utility matters before the Commission other than rate adjustment cases was challenged in the late 1980s. For example, statute provides RUCO the authority to intervene in proceedings before the Commission relating to rate making or rate design, yet rate making or rate design cases represent only approximately 5 percent of the utility cases filed with and decided by the Commission. Additionally, the 1989 Auditor General report (Report No. 89-6) recommended that the Legislature consider amending RUCO's statutes to expand and clarify RUCO's authority to participate in any case before the Commission that may have the potential to impact residential rates in the future. However, RUCO has continued to participate in a variety of other cases before the Commission, such as financing and mergers, without further challenge and sees no need to amend its statutory authority to specifically include non-rate cases.

- 9. The extent to which changes are necessary in the laws of RUCO to adequately comply with the factors listed in the Sunset Law.**

This review did not identify any necessary statutory changes.

- 10. The extent to which the termination of RUCO would significantly harm the public health, safety or welfare.**

While termination of RUCO would not significantly harm or have an impact on the welfare of residential utility consumers, RUCO's intervention into utility rate and non-rate cases has had some impact in limiting residential utility bills. In addition, RUCO's presence in the process ensures that residential consumers' interests are represented. Although other consumer groups or the Commission staff could provide representation for residential consumers, many of the consumer groups may not have the financial resources or technical expertise to present arguments in complex cases. Furthermore, Commission staff must balance the interests of the utilities and all classes of consumers and thus cannot be as attentive to residential consumer needs as can RUCO.

11. **The extent to which the level of regulation exercised by RUCO is appropriate and whether less or more stringent levels of regulation would be appropriate.**

This factor does not apply since RUCO is not a regulatory agency.

12. **The extent to which RUCO has used private contractors in the performance of its duties and how effective use of private contractors could be accomplished.**

RUCO periodically uses private contractors to assist in the performance of its duties. For example, RUCO contracts with experts or professional witnesses to provide utility rate case analysis and testimony in areas where in-house staff lack specific expertise or do not have sufficient time available. However, RUCO's use of professional witnesses has sharply decreased in recent years, largely due to the hiring of more qualified in-house staff. Consequently, RUCO's professional witness expenditures have dropped from \$333,400 in fiscal year 1994 to an annual average of \$129,000 for fiscal years 1995 through 1998. Our review of RUCO's professional witness use indicates an effective use of contractors, while increasing the agency's reliance on in-house expertise.

**Residential Utility  
Consumer Office  
Agency Response**



May 20, 1999

Douglas R. Norton, CPA  
Auditor General  
Office of the Auditor General  
2910 North 44<sup>th</sup> Street, Suite 410  
Phoenix, Arizona 85018

Dear Mr. Norton:

RUCO is pleased to receive such a favorable report from the Auditor General. His exhaustive analysis – spending over 2,000 hours examining every case in which the office has intervened over the last five years – quantifies what RUCO has believed all along. RUCO is an effective advocate for residential consumers.

RUCO also appreciates the Auditor General's recognition that changes and growth in the State's utility industries may contribute to a more challenging and demanding workload for the agency.

RUCO appreciates the Auditor General's suggestions concerning how our internal processes can meet those future challenges. Utility regulation is becoming increasingly complex and the suggestions "to ensure that RUCO continues to beneficially advocate on behalf of residential consumers" are excellent.

The Auditor General has recommended that, because of the changing regulatory environment, RUCO should establish a broader mission statement, expand the definition of its stakeholders and customers and determine the focus of future advocacy efforts. These changes will require modification of RUCO's statutory authority and we are committed to working with the Auditor General to prepare and present a Legislative agenda incorporating these recommendations.

Douglas R. Norton  
May 20, 1999  
Page 2

Additionally, the Auditor General has recognized that RUCO has achieved this high level of effectiveness while operating significantly below budget. RUCO appreciates the suggestions as to how we can work better with GOA and the Arizona Corporation Commission to ensure that our annual surplus flows back to consumers as efficiently as possible. RUCO will endeavor to eliminate the confusion caused returning a surplus to consumers through the labyrinthine assessment process.

Finally, RUCO would like to thank the Auditor General and his staff for their professionalism, recommendations, and responsiveness.

Sincerely,

Greg Patterson  
Director

## Recommendations

1. To ensure that RUCO continues to beneficially advocate on behalf of residential consumers, RUCO should develop a more comprehensive strategic plan that identifies key areas for advocacy in Arizona's dynamic utility regulatory environment. Components of this plan could include:
  - a. Establishing a broader mission statement; Agree: Implement
  - b. Defining its stakeholders and customers; Agree: Implement
  - c. Identifying what services it will deliver; and Agree: Implement
  - d. Determining the focus of future advocacy efforts. Agree: Implement
2. RUCO should formalize its case selection process by documenting the process it employs and the factors it considers when assessing cases for possible intervention;  
  
Agree: Implement
3. RUCO should formalize its process for measuring and critiquing its impact in cases to continue to maximize RUCO interventions on behalf of residential consumers; and  
  
Agree: Implement
4. RUCO should define its consumer education focus, including development of a Website.  
  
Agree: Implement
5. RUCO should abide by A.R.S. §§ 40-401.01 and 40-409 when determining its annual assessment amount. Specifically, RUCO should reduce each year's assessment by an amount equal to any monies estimated to remain in its revolving fund at the end of the fiscal year.  
  
Agree: Implement
6. To ensure proper fund management, RUCO should strengthen its financial practices by:
  - a. Developing policies and procedures to monitor fiscal activities;  
Agree: Implement

- b. Assigning responsibility within policies and procedures for performing various fiscal activities; Agree: Implement
- c. Reconciling assessments, collections, and deposits; and Agree: Implement
- d. Monitoring revolving fund transactions. Agree: Implement

## **Residential Utility Consumer Board**

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# **INTRODUCTION AND BACKGROUND**

The Office of the Auditor General has conducted a performance audit and Sunset review of the Residential Utility Consumer Board (Board) pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee. This audit was conducted as a part of the Sunset review set forth in Arizona Revised Statutes (A.R.S.) §§41-2951 through 41-2957. This is the third audit of the Board. In both 1986 and 1989, the Auditor General completed a limited review of the Board (Report Nos. 86-6 and 89-6, respectively).

The Board was established in conjunction with the Residential Utility Consumer Office (RUCO) in 1983. A.R.S. §40-463 requires that the Board shall advise RUCO on all matters relating to rate making or rate design and involving public service corporations. The Board is statutorily empowered to instruct RUCO's director to withdraw any court action filed by RUCO, and to prepare RUCO's proposed annual budget request jointly with its director. The Board may also advise the Governor and Legislature on matters relating to RUCO.

## **Organization and Staffing**

The Board consists of five citizen members appointed by the Governor, who serve staggered five-year terms. The Board is required to meet monthly and members are eligible to receive compensation for each day of actual service on the Board, pursuant to A.R.S. §38-611. Board expenditures for fiscal year 1997-1998 were approximately \$4,400. The staff of the Residential Utility Consumer Office (RUCO) provides various support services, including preparing the Board's meeting agenda and producing the meeting minutes.

## **Audit Scope and Methodology**

This performance audit and Sunset review was conducted to determine the need for the Board's statutory mandates and whether the Board is fulfilling these mandates. To evaluate the need for the Board and how well it fulfills its role, several methods were used, including:

- Attending 11 board meetings (from May 1998 through February 1999), and interviewing current, former, and recently resigned board members to assess the effectiveness of board actions;
- Analyzing board meeting minutes for April 1995 through February 1999 to determine board position vacancies, attendance, and meeting content;

- Contacting nine other states to learn best practices regarding the need for advisory boards<sup>1</sup>; and
- Interviewing various individuals involved in the utility regulatory process, including commissioners, hearing officers, and Commission staff; various consumer advocacy representatives; and all 11 members of RUCO's staff.

This report presents one finding along with a recommendation addressing the need for the Board and the functions it provides.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Residential Utility Consumer Board members, and the Director and staff of RUCO for their cooperation and assistance throughout the audit.

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<sup>1</sup> Nine states having an organization similar to RUCO and the Board were identified and contacted: Colorado, Illinois, Iowa, Kansas, Kentucky, New York, Ohio, Oregon, and Utah.



# FINDING I

## THE BOARD INEFFECTIVELY FULFILLS ITS ROLES

In recent years, the Residential Utility Consumer Board (Board) has not effectively fulfilled the requirements of its statutory mandates. While the Board has indicated its role should include informing residential consumers regarding cases under review by RUCO, educating consumers on relevant utility issues, and advising RUCO of consumer concerns and interests, it has taken few steps to fulfill these functions. Additionally, the Board has been limited in its ability to fulfill its statutory mandates to participate in the preparation of RUCO's budget and to require RUCO to withdraw filed court actions. Therefore, the Board should work with RUCO to develop and implement various processes that will enable the Board to more effectively work with consumers, advise RUCO, and carry out its responsibilities.

### **Board's Ability to Serve in an Advisory Capacity Limited by Inaction**

Although statute requires the Board to serve in an advisory capacity, the Board's efforts in recent years have had minimal impact. While statute requires the Board to advise RUCO on rate cases, the Board lacks the expertise to provide RUCO technical advice on these cases. Instead, the Board has suggested it can best serve the public by advising it of cases under review by RUCO and advising RUCO of consumer concerns or questions. However, it has taken few steps to effectively fulfill this role. Questions among board members concerning its role and authority, board vacancies, and board members' poor meeting attendance have contributed to board inaction.

***Limited need for technical advisory role***— According to statute, the Board was established to serve in an advisory capacity to RUCO. Specifically, A.R.S. §40-463 prescribes that the “Board shall advise the office on all matters relating to rate making or rate design and involving public service corporations.” However, over the years, RUCO has evolved into a highly technical agency, which enables it to perform its rate-making and rate design work. RUCO staff possess many years of technical expertise and experience and do not rely on board assistance to do their work. A review of monthly board meeting minutes, from April 1995 through February 1999, as well as auditors' observations of 11 board meetings, from May 1998 through March 1999, confirms that board members rarely advise RUCO on rate cases. Instead, board meetings largely consist of RUCO's director briefing board members on RUCO's activities and progress on cases during the preceding month.

The Residential Utility Consumer Board's present situation is not unique. Nationally, the changing regulatory environment has diminished the role of advisory boards among the few states that now have them. Consumer advocates like RUCO are performing more technical analyses, which has diminished the advisory boards' roles and functions.

***Board ineffective in representing public concerns***—The Board has not effectively represented public concerns regarding rate cases. While the Board believes that it can best serve the public by advising it of cases under review by RUCO and in turn, advising RUCO of consumer concerns and questions regarding those cases, it has not established any processes or procedures to fulfill this role. Currently, monthly board meetings represent the only forum for RUCO to inform the public about and solicit their comments and questions regarding public utility rate and non-rate cases under RUCO's review. In fact, previous Auditor General Sunset reports (Report Nos. 86-6 and 89-6) suggested that the Board's monthly meetings had been a valuable forum for the acquisition and dissemination of timely information to the media, public, and utility companies in attendance. However, a review of RUCO board meeting attendance data for January 1996 through December 1998 indicated very limited public attendance, with only three or fewer attendees at 65 percent (22 of 34) of monthly meetings, including one attendee from a major utility. The Board has acknowledged that its meetings are not held at locations or times that are conducive to public attendance and participation, but has not moved them to a more consumer-friendly time or location. Based on this limited public attendance, Board meetings have not served as a useful tool to inform the public of RUCO activities.

To reach residential consumers outside the greater Phoenix area, the Board has occasionally held its meetings in various parts of the State and indicated that it could better serve the public by individually meeting with or speaking to various consumer groups across the State. However, meetings held in other parts of the State have not been widely attended by the public, nor have board members individually met with consumer groups. For example, while the Board held 2 of its 1998 meetings outside of the Phoenix area, with one meeting in Tucson and another meeting in Prescott, only 2 or 3 people attended each of these meetings. Insufficient public notification of these meetings contributed to this sparse attendance. Additionally, although the Board has discussed meeting with the public in various areas of the State as far back as August 1996, it has not developed any plans or processes for individually meeting with consumers, a function that could potentially be very effective since board members live in and represent various areas of the State.

***Chronic vacancies, poor attendance, and questions about authority hinder effectiveness***—Board vacancies, members' poor meeting attendance, and questions about its authority have affected the Board's ability to serve in an advisory capacity. While the Board consists of five members, from April 1995 through February 1999 there has been at least one board vacancy, and sometimes two vacancies, for the majority of its meetings. Given the vacancies, any attendance problems experienced by appointed members affected its ability to obtain a quorum. As a result, the Board has lacked a quorum for 23 percent of its board meetings

from April 1995 to February 1999. This has meant that the Board could take few actions and often postponed agenda items for several months.

Additionally, the Board has openly questioned its role and authority, which has delayed the development and implementation of plans and processes to fulfill its advisory role. A review of board meeting minutes from April 1995 through February 1999 indicates that members have frequently questioned the Board's role and level of authority. Given the Board's repeated questions about its role, the Legislature may wish to restate the nature and scope of the Board's advisory role. In particular, the Legislature may wish to revise current statutes to strengthen the Board's focus on obtaining, and transmitting to RUCO, public concerns regarding utility issues and RUCO activities.

### **Board's Ability to Perform Its Oversight Duties Is Limited by Inadequate Processes and Information**

The Board has been limited in its ability to appropriately fulfill its oversight duties of RUCO, which include assisting with the preparation of RUCO's biennial budget request and requiring RUCO to withdraw filed court actions that it deems are inappropriate. The Board is not involved in preparing RUCO's budget, but only in reviewing and approving a budget prepared by RUCO. Additionally, although RUCO files few court actions, the procedures for notifying the Board in a timely manner of such court actions would make it difficult for the Board to act.

*Board has minimal role in budget matters*—RUCO does not use or rely on the Board's assistance in preparing its budget. Per statute, the *"Board and the director shall jointly prepare the proposed annual budget request for the office."* Although the Board provides formal approval of RUCO's annual budget request, it does not participate in its preparation. Essentially, the Board's involvement consists of reviewing and approving the budget prior to sending it to the Governor's Office. Although the Board has not signed all of the budget requests, board meeting minutes indicate that the Board approved both the fiscal years' 1998 and 1999 and fiscal years' 2000 and 2001 budgets.

The Board attributes its lack of involvement in preparing the budget to RUCO's failure to solicit board members' input earlier in the process. Generally, board members receive a copy of the budget request shortly before it is due to the Governor's Office. While Board members report that they previously raised concerns about their limited opportunity to provide input, the process has remained unchanged in recent years. Additionally, neither board members nor RUCO have initiated any changes to the budget preparation process.

*Few court actions filed*—RUCO seldom files court actions so there have been few occasions for the Board to consider exercising its oversight power of instructing RUCO to withdraw

filed court actions. A court action consists of RUCO appealing a Corporation Commission decision to either the State's Superior Court or Court of Appeals. Per statute, "*Any court action filed by the director shall be withdrawn if the board instructs the director to withdraw within five working days after filing.*" To date, there have been relatively few court actions filed by RUCO. Since its inception in 1983, RUCO reports it has filed a total of 16 court actions, with 12 filed on or before January 1990, and the remaining 4 filed within the past two years. The most recent court actions occurred in May 1997 and November 1998 and pertained to RUCO contesting the Commission's proposed electric restructuring due process rules.

Even if the Board desired to request the withdrawal of an action, the timeframes for doing so make it difficult for the Board to exercise such authority. For example, it is difficult for the Board to convene, obtain information and discuss the merits, and ultimately decide the appropriateness of the action within the five-day window. Furthermore, in one recent case, the court acted even before the five-day period expired. In November 1998, the Arizona Supreme Court rendered its decision two days after an action was filed. Although RUCO notified board members of this court action a few days prior to its filing, the Board did not have sufficient time to fulfill this statutory role had it chosen to do so.

## **Improvements Are Needed to Enhance the Board's Effectiveness**

Several improvements are needed to enhance the Board's ability to fulfill its roles. Specifically, the Board needs to establish procedures to increase public awareness, and work with RUCO to obtain information in a timely manner and obtain necessary staffing support.

*Establish processes to encourage increased public awareness, participation, and input*—The Board should develop and implement processes to more effectively perform consumer outreach and education, and advise RUCO on cases it has under review. Specifically, the Board should consider modifying how its meetings are conducted, where they are held, and establishing practices that will improve public attendance at the meetings in order to encourage greater participation by and information exchange with residential consumers. For example, meetings can be scheduled for a more practical, public-friendly location, which may increase attendance. Also, some board meetings could be held during the evening. The Board should also take steps to publicize its meetings to ensure residential consumers have an opportunity to attend and express their interests and concerns.

Additionally, the Board should work with RUCO to develop procedures for meeting individually with consumer groups. In at least two board meetings in 1998, the Board discussed the idea that it should become more involved in speaking to community organizations and requested RUCO to prepare an outline for the Board's use in these efforts and to schedule speaking engagements. However, no action was taken.

Finally, the Board should take steps to fulfill its advisory role to RUCO. These steps might include working with RUCO to obtain sufficient and timely information on rate cases under review, establishing a process whereby the Board can communicate its advice and consumer concerns or questions it receives to RUCO, and developing procedures for RUCO to report on case proceedings and actions to the Board.

***Improve processes to ensure timely dissemination of information for the Board's consideration***—The Board should work with RUCO to improve the processes by which the Board receives information specific to the preparation of the budget. Although the Board has expressed concern regarding current practices, RUCO has not actively sought the Board's assistance in preparing the budget and the Board has not acted to change the process. Therefore, the Board should work with RUCO to develop policies and procedures for involving the Board in the budget preparation.

The Board also needs to work with RUCO to receive timely information regarding court actions filed by RUCO. For example, to ensure that board members have sufficient time to convene, review a court action, and decide on the appropriateness of this action, the Board and RUCO might consider developing a process that requires RUCO to, where possible, notify the Board of an impending court action and provide appropriate materials on the action for the Board's review before it is filed.

***Coordinate the provision of staffing resources to assist the Board in its efforts***—To ensure that the Board has sufficient resources to perform its identified activities, the Board should work with RUCO to provide staffing resources. RUCO has periodically responded to board members' requests for legal advice and assistance with drafting correspondence. However, because board members are volunteers, and reside in several different areas of the State, the Board could benefit from having a part-time, dedicated staff person available to assist board members in their activities. These activities would involve setting the Board's meeting agenda, scheduling meetings and speaking engagements, informing the public of these meetings and engagements, working with the Board and RUCO to establish the processes needed by the Board to fulfill its various mandates, and assisting the Board with these processes.

The Board should first work with RUCO to determine if RUCO can dedicate any of its current staffing resources on a part-time basis to the Board. If RUCO cannot make these resources available, the Board should work with RUCO to identify monies currently available within its budget to retain the necessary staff. It appears RUCO should have sufficient budget capacity to hire a part-time position, as in recent years it has typically expended less than it has been appropriated. Lastly, if monies are not available within RUCO's budget, the Board should work with RUCO to include the necessary monies in its future budget requests.

Other state agencies currently provide staff to the boards with which they work. For example, the Arizona Department of Liquor Licenses and Control provides part-time, dedicated staffing for the Arizona State Liquor Board.

## **Recommendations**

1. The Legislature should consider revising A.R.S. §40-463 to clarify the Board's role and focus Board activities on obtaining, and transmitting to RUCO, public concerns regarding utility issues.
2. The Board should work with RUCO to develop and implement various processes to assist in fulfilling its consumer and RUCO advisory roles. Processes should be developed for:
  - a. Scheduling board meetings and speaking engagements, selecting appropriate sites for these meetings and speaking engagements, and informing the public of these board activities; and
  - b. Obtaining necessary information on cases under review by RUCO, advising RUCO on these cases and consumer interests and concerns, and receiving reports from RUCO on case actions and proceedings.
3. The Board should work with RUCO to establish processes for:
  - a. Providing for the Board's statutorily required participation in the preparation of RUCO's budget; and
  - b. Notifying the Board of court actions filed by RUCO's director and providing appropriate materials to the Board on the court action within sufficient time to allow the Board to convene, review, and decide on the appropriateness of the court action within the statutorily required timeframe.
4. The Board should work with RUCO to identify and provide a dedicated, part-time staff person to the Board to facilitate its activities. If RUCO cannot make these resources available, the Board should work with RUCO to use some of its available budget monies to provide the needed staffing resources.

# SUNSET FACTORS

In accordance with A.R.S. §41-2954, the Legislature should consider the following 12 factors in determining whether the Residential Utility Consumer Board (Board) should be continued or terminated.

**1. The objective and purpose in establishing the Board.**

The Residential Utility Consumer Board was established in 1983 to advise the Residential Utility Consumer Office (RUCO) on all matters relating to rate making or rate design and involving public service corporations. The Board is statutorily empowered to instruct RUCO's director to withdraw any court action filed by RUCO, and is mandated to prepare RUCO's proposed annual budget request jointly with its director. In addition, the Board may advise the Legislature and the Governor on all matters relating to RUCO.

**2. The effectiveness with which the Board has met its objective and purpose and the efficiency with which the Board has operated.**

The Board has had difficulty in meeting its objective and purpose. While statute requires the Board to advise RUCO on rate cases, RUCO does not rely on this assistance. Instead, the Board has suggested it can best serve the public by advising it of cases under review by RUCO and advising RUCO of consumer concerns or questions; however, it has taken few steps to effectively fulfill this role. In addition, RUCO has not involved the Board in developing its budget. Lastly, while RUCO infrequently files court actions, given the five-day period allowed for Board review, the Board would have difficulty exercising its power to instruct RUCO to withdraw such court actions. To improve its performance, the audit found that the Board should develop and implement various processes that will enable the Board to more effectively work with consumers, advise RUCO, and carry out its budget and court action review responsibilities. See Finding I (pages 29 through 34) for further detail.

**3. The extent to which the Board has operated within the public interest.**

Although the Board's activities are designed to serve the public interest, its limited statutory authority and the lack of policies and procedures that would enable it to more effectively fulfill its responsibilities have hampered the Board's ability to operate within the public interest.

4. **The extent to which rules and regulations promulgated by the Board are consistent with the legislative mandate.**

The Board does not have authority to promulgate rules and regulations.

5. **The extent to which the Board has encouraged input from the public before promulgating its rules and regulations and the extent to which it has informed the public as to its actions and their expected impact on the public.**

Since the Board does not have the authority to promulgate rules and regulations, input from the public has not been necessary for this purpose. However, the Board could inform the public about its actions by better publicizing its monthly meetings, and holding meetings in more “public friendly” locations and at more convenient times.

With one exception, the Board has complied with the State’s open meeting laws. Specifically, RUCO publishes the Board meeting notices before each meeting, makes an agenda available to the public, and provides minutes of the meetings in accordance with statute. However, the open meeting laws also require the Board to file a statement with the Secretary of State indicating where all meeting notices will be posted; but when contacted by auditors, the Secretary of State’s Office did not have this statement on file.

6. **The extent to which the Board has been able to investigate and resolve complaints that are within its jurisdiction.**

The Board has no authority to and does not investigate residential consumers’ complaints.

7. **The extent to which the Attorney General or any other applicable agency of state government has the authority to prosecute actions under the enabling legislation.**

The Board’s purpose is to act as an advisor to RUCO. Therefore, it has no regulatory authority, and consequently no enforcement powers.

8. **The extent to which the Board has addressed deficiencies in its enabling statutes which prevent it from fulfilling its statutory mandates.**

The statutes establishing the Board and its function have not been changed since the Board was created in 1983. Furthermore, no attempts have been made by the Board to change the Board’s mandates, as the Board has not identified any deficiencies.



9. **The extent to which changes are necessary in the laws of the Board to adequately comply with the factors listed in the Sunset Law.**

Because the Board has frequently questioned its role and authority, we recommend that the Legislature consider revising the Board's statutes to clarify this issue.

10. **The extent to which the termination of the Board would significantly harm the public health, safety or welfare.**

Elimination of the Board would not significantly harm the public health, safety, or welfare. The Board is an advisory board to RUCO and RUCO could continue to function without the Board.

11. **The extent to which the level of regulation exercised by the Board is appropriate and whether less or more stringent levels of regulation would be appropriate.**

This factor does not apply since the Board has no regulatory authority.

12. **The extent to which the Board has used private contractors in the performance of its duties and how effective use of private contractors could be accomplished.**

The Board has not used the services of private contractors nor did this review identify an effective use for private contractors.

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**Residential Utility  
Consumer Board  
Agency Response**

**BOARD OF DIRECTORS**  
Residential Utilities Consumer Office  
**James Spezzano, Chairman**  
Other Members of the Board

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<b>Dave Carson</b> Dewey	<b>Timothy Schmaltz</b> Phoenix	<b>Robert Usdane</b> Scottsdale	<b>Mercy Valencia</b> Tucson
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June 8, 1999

Douglas Norton  
AUDITOR GENERAL  
2910 No. 44<sup>th</sup> Street Suite 410  
Phoenix, AZ 85018

Dear Mr. Norton:

The Residential Utility Consumer Board has reviewed the revised preliminary draft, issued 5-11-99, of the performance audit conducted by your office. While the report sheds light on the many issues that have frustrated the Board for some time, we disagree with where the responsibility for solutions belongs. The Board's response to your audit report is contained in our attached **Final Draft Report**.

We have a general, serious concern with the audit's basic premise that the Board and RUCO office are two separate entities, which is contrary to the relationship established between ARS 40-463.I and 40-463.J, their relationship to ARS-462.A and the original intent of the statutes to protect residential utility consumer interests. The statutes clearly define RUCO's role as representing residential utility consumers. Albeit the Board's major responsibility is to "advise (RUCO) office on all matters," the Board is also mandated in the areas of budget, advisory input and court withdrawals. However, the Board's role has not been viewed as such by the RUCO administration. The audit does not reflect the increasing division that has occurred because of the legal opinion that the two separate statutes create two legally separate entities (agencies) that divide the roles of the Board and the RUCO office at the expense of the residential consumer. This separation effectively renders the audit recommendations unattainable by the Board.

The audit does not recognize the Board's continual attempts to deal with the RUCO office in a collaborative manner and the lack of responsiveness to explicit Board requests by the agency administration that has impeded the Board from fulfilling its obligations. Additionally, the audit report fails to mention that responsibility for carrying out the needs of the Board falls to the RUCO office since the Board has no budget or staff.

We would appreciate clarification of your May 11, 1999, letter referring to the April 8, 1999, Executive Session. The Board would like to know which *issues* and *instances* could not be verified and therefore not addressed by the board.

Sincerely,

James Spezzano  
Chairman

RESIDENTIAL UTILITY CONSUMER BOARD OF DIRECTORS

**Response to the Auditor General's performance audit report**  
(6-8-99 — final draft report)

The Board agrees with the AG's recommendation that processes be developed in collaboration with RUCO that would enable the Board to work effectively with residential consumers, advise RUCO and carry out its other responsibilities; however, there is a high degree of disagreement as to the basis for this recommendation. The basis for AG Finding 1 was based on minutes from Board meetings. The Board acknowledges that its meetings were not held under its own aegis. The Board was prohibited from carrying out its statutory mandate by the agency administration's lack of responsiveness to persistent requests that presentation of issues not be entirely technical in nature, but rather should focus more on the perspective of the residential consumer.

The Board has attempted to solve agenda issues collegially and informally, in the spirit of cooperation, without results from RUCO's leadership. The AG's report now requires the Board to publically declare its frustration and the lack of response from the agency. A current example of this lack of response is available through a review of the tape from the 4-23-99 public meeting, which documents the consistent demands from the Board for additional consumer perspective information on each issue for the next meeting, yet the agenda for the 5-15-99 meeting ignores the Board's request.

In the following the Board addresses each finding presented in the audit report.

**Finding 1: The Board Ineffectively Fulfills Its Roles**

*Limited need for technical advisory role:*

**RESPONSE**

The audit states that RUCO has evolved into a highly technical agency and does "not rely on board assistance to do their work." Here the audit assumes, that to be effective the Board should act as a technical advisory body. This statement is inherently contradictory since all agree that the Board is a consumer advisory board focusing on the broad impact on the consumer of utility costs and services, not the technical aspects of rate making and rate design.

*Board ineffective in representing public concerns:*

**RESPONSE**

The audit does not reflect attempts by the Board to address public concerns. A prime example may be found in the Arizona Community Action Association's (ACAA) 7-29-98 letter to Board member Usdane expressing concern regarding the proposed rule changes concerning deregulation as discussed at the ACAA 7-15-98 Stakeholders's meeting. The ACAA believes the public process was unfair to small consumers because (1) the hearing was not advertised, (2)

there was no residential consumer participation, (3) there was no consumer education and (4) the proposed changes lack small consumer benefits. The ACAA letter cites the RUCO director's testimony as a filing of technical information rather than a treatment of residential consumer interest issues. The Board attempted to bring this issue to RUCO and that effort was disregarded. The board has been put in the untenable position of seeking public participation without the budget or staff to relocate meetings for public input. The Board would prefer to have a more public forum than has been offered in the past. Two Board meetings were held regionally but lack of advertising and appropriate timing may have hindered public participation.

*Chronic vacancies, poor attendance and questions about authority hinder effectiveness:*

#### RESPONSE

The Board agrees that some members must assume responsibility for their lack of attendance, but has no control over the filling of vacancies with members committed to attending meetings. Historically, there seems to have been an inordinate amount of time passing before replacement of Board members has been accomplished, which increases the burden on the remaining members. Additionally, the consistent presentation of data on a technical basis and the lack of information regarding the impact of rates and services on residential consumers (as requested) has resulted in some indifference on the part of previous Board members. The Board has questioned its role and authority as stated, however the Board was questioning whether its mission was being fulfilled by the agency and how the Board could better interact with the agency to fulfill its mission. The Board agrees with the recommendation to have the legislature revise ARS 40-463 to strengthen the Board's ability to fulfill its statutory mandate.

#### **BOARD'S ABILITY TO PERFORM ITS OVERSIGHT DUTIES IS LIMITED BY INADEQUATE PROCESSES AND INFORMATION.**

#### RESPONSE

The Board agrees with the AG's statement regarding the Board's limited ability to fulfill its oversight duties. The RUCO staff has limited the Board's oversight duties by failing to provide needed information and not responding to direct Board requests to do so.

*Board has minimal role in budget matters:*

#### RESPONSE

ARS 40-463.L states the Board's responsibility to jointly prepare the budget but does not give clear authority for approval. The Board has played a minimal role because the RUCO administration has excluded the Board from the budget process. For example, the FY2000/2001 budget was not jointly prepared nor approved by the Board. In fact, the Board refused to sign the budget as it was presented, thus withholding approval pending further input. Nevertheless, the budget was forwarded to the legislature by the RUCO administration. In this instance, the Board was precluded from fulfilling its statutory obligation. Contrary to Board member narration of events, the audit states that the Board approved recent budgets; therefore the Board respectfully requests verification of when and in what manner the budget was approved.

*Few court actions filed:*

#### **RESPONSE**

There is no current process for informing the Board of pending legal action to allow the board to fulfill its role, however the Board has requested that RUCO implement a procedure whereby the Board could be fully informed as to the objectives and details of a proposed court action prior to the commencement of the action. This knowledge would enable the Board to exercise the 5-day withdrawal option when deemed necessary. The audit does not make note of the Board's attempt to ask for a specific case to be filed, where subsequently and without notification to the Board, RUCO withdrew the case. In this particular case, the issue was considered critical to the interests of residential consumers.

#### **IMPROVEMENTS NEEDED TO ENHANCE BOARD'S EFFECTIVENESS**

*Establish processes to encourage increased public awareness, participation and input:*

#### **RESPONSE**

The Board strongly supports the establishment of a process to increase public awareness, etc., but it is impossible for a voluntary board to achieve this without the agency's assistance. It is imperative that RUCO provide the Board with staff, budget and general assistance to assist the Board in performing its legislative mandate.

*Improve process to ensure timely dissemination of information for the Board's consideration:*

#### **RESPONSE**

The board is very supportive of improving processes for the timely dissemination of information, however the draft report places the onus on the Board to develop those improved processes. Without the cooperation of the RUCO administration, this is not achievable. At issue is the administrator's interpretation of the separation of the Board from the agency and the apparent assumption that processes to inform the Board are unnecessary. The Board is merely the recipient of information and as such is not in a position to change RUCO processes. The Board would support efforts to have RUCO change its information dissemination processes.

*Coordinate the provision of staffing resources to assist the Board in its efforts:*

#### **RESPONSE**

The Board wholeheartedly agrees with the draft report's substantiation of the need for support staff. At least a part-time dedicated staff person is critical to the Board if issues of agenda setting, taking and transcribing minutes, preparing reports and correspondence, scheduling meetings and speaking engagements, informing the public, etc., are to be successful.

#### **RECOMMENDATIONS**

#### **RESPONSE**

As stated in the Board's 6-3-99 cover letter, the Board is seriously concerned with the audit's

basic premise that the Board and the RUCO office are two distinct and separate entities (agencies), which is contrary to the relationship established between ARS 40-463I, 40-436.J and their relationship to ARS 40-462.A and the original intent of the statutes to protect residential consumer interests. The statutes clearly define RUCO's role as representing residential utility consumers. While the Board's major responsibility is to "advise (RUCO) office on all matters," the Board is also mandated in the areas of budget, advisory input and court withdrawals. However its role has not been viewed as such by the RUCO administration. The audit does not reflect the increasing division which has occurred because of the legal opinion that the two separate statutes create two separate organizations that divide the roles of the Board and the Agency at the expense of the residential consumer. The separation of the two agencies leaves the audit recommendations not achievable by the Board. Further, the audit does not reflect the efforts of the Board's continual attempts to deal with RUCO in a collaborative manner, and the lack of responsiveness to explicit Board requests by the agency administration that have impeded the Board from fulfilling its obligations. Additionally, the audit report does not reflect that the responsibility for carrying out the needs of the Board falls to the agency since the Board has no budget or staff.

1. *The Legislature should consider revising ARS 40-463 to clarify the Board's role and focus Board activities on obtaining, and transmitting to RUCO, public concerns regarding utility issues.*

**RESPONSE:**

The Board agrees with the finding of the Auditor General to request the Legislature consider strengthening ARS 40-463 to clarify the Board's role and to focus Board activities on obtaining and transmitting to RUCO public concerns regarding utility issues. The Board recommends that **Attachment A** be submitted to the Legislature to address statutory mandates.

2. *The Board should work with RUCO to develop and implement various processes to assist in fulfilling its consumer and RUCO advisory roles. Processes should be developed for:*
  - a) *Scheduling board meetings and speaking engagements, selecting appropriate sites for these meetings and speaking engagements, and informing the public of these board activities; and*
  - b) *Obtaining necessary information on cases under review by RUCO, advising RUCO on these cases and consumer interests and concerns, and receiving reports from RUCO on case actions and proceedings.*

**RESPONSE:**

The findings of the Auditor General is agreed to, however the recommendation can not be implemented as currently stated. The statutes create an interdependence between RUCO and the Board for the shared purpose of representing residential consumer interest, both mandated and advisory. While the onus of developing processes should be on the RUCO administration, the Board submits **Attachment B** as its recommendation for establishing one needed and important process to address the shared purpose of representing residential consumer interests.



3. *The Board should work with RUCO to establish processes for:*

a) *Providing for the Board's statutorily required participation in the preparation of RUCO's budget;*

RESPONSE:

ARS 40-463.L states the Board's responsibility is to jointly prepare the budget but does not clarify its authority for approval. The Board has played a minimal role because the RUCO administration has excluded the Board from the budget process. The finding of the Auditor General is agreed to in concept; however the recommendation cannot be implemented as presently stated. Legislative adoption of the statutory changes recommended in **Attachment A** would provide a constructive and workable remedy.

b) *Notifying the Board of court actions filed by RUCO's director and providing appropriate materials to the Board on the court action within sufficient time to allow the Board to convene, review, and decide on the appropriateness of the court action within the statutorily required time frame.*

RESPONSE:

There is no current process for informing the board of pending legal action to allow the board to fulfill its role, however the Board has requested that RUCO implement a procedure whereby the Board could be fully informed as to the objectives and details of a proposed court action prior to the commencement of the action. This knowledge would enable the Board to exercise the 5-day withdrawal option when deemed necessary. The statutory recommendations in **Attachment A** would accomplish this. The Board is prepared to fully function in its advisory role and meet the statutory mandates as suggested by the audit report upon implementation of the recommended procedural and statutory changes.

4) *The Board should work with RUCO to identify and provide a dedicated part-time staff person to facilitate its activities. If RUCO cannot make these resources available, the Board should work with RUCO to use some of its available budget monies to provide the needed staffing resources.*

RESPONSE:

The Board and RUCO should work together to identify and provide at least a dedicated part-time staff person to facilitate the Board's activities. If RUCO cannot make these resources available, the Board will work with the Legislature to request budget funds for the needed resources. The finding of the Auditor General is agreed to and the audit recommendation will be implemented to the extent possible.

ATTACHMENT A

Proposed Amendments to **ARS 40-463**

**Strike existing language and insert:**

**K. "BOARD APPROVAL SHALL BE REQUIRED PRIOR TO THE FILING OF ANY COURT ACTION AND ANY ONGOING COURT ACTION SHALL BE IMMEDIATELY WITHDRAWN UPON ORDER OF THE BOARD."**

**L. "THE DIRECTOR SHALL COORDINATE PREPARATION OF THE BUDGET WITH THE BOARD AND THE BUDGET SHALL NOT BE OFFICIALLY FILED UNTIL FIRST APPROVED BY THE BOARD."**

**Add the following new sections:**

**M. "AT THE BOARD'S DIRECTION AND WITH THE BOARD'S PARTICIPATION AND APPROVAL THE DIRECTOR SHALL PREPARE AND IMPLEMENT A PROCEDURE FOR INFORMING RESIDENTIAL UTILITY USERS IN ANY MATTER DEEMED BY THE BOARD VITAL TO THE INTERESTS OF THE USERS AFFECTED."**

**N. "THE DIRECTOR SHALL PROVIDE TO ANY BOARD MEMBER UPON THE MEMBER'S REQUEST AND IN A TIMELY MANNER ANY REPORT OR OTHER INFORMATION REASONABLY AVAILABLE PERTAINING TO THE AGENCY'S ACTIONS AND ACTIVITIES."**

**O. "UPON ORDER OF THE BOARD THE DIRECTOR SHALL PREPARE AND TRANSMIT TO THE CORPORATION COMMISSION OR OTHER AGENCY OR INDIVIDUAL ANY REPORT, RECOMMENDATION OR REQUEST PERTAINING TO RESIDENTIAL UTILITIES AND APPROVED BY THE BOARD."**

**P. "THE BOARD MAY PROMULGATE AND ADOPT RULES REGARDING THE NATURE AND FORMAT OF AGENCY DEVELOPED DATA PRESENTED TO THE BOARD FOR CONSIDERATION; THE DATE, TIME AND LOCATION OF BOARD MEETINGS AND THE NATURE AND SCOPE OF EDUCATIONAL MATERIAL TO BE MADE AVAILABLE OR DISTRIBUTED TO RESIDENTIAL UTILITY USERS."**

**Q. "UPON ORDER OF THE BOARD, FOUR-FIFTHS OF THE MEMBERS CONCURRING OR BY UNANIMOUS CONSENT OF THE MEMBERS IN ATTENDANCE AT THE MEETING AND CONSTITUTING A QUORUM, THE DIRECTOR SHALL INSTITUTE, REVISE OR WITHDRAW ANY RATE MAKING, RATE DESIGN OR OTHER RESIDENTIAL UTILITY RELATED INTERVENTION ACTION ANTICIPATED OR INITIATED BY THE AGENCY."**

## **ATTACHMENT B**

**The follows pertains to a Board recommended process for the provision of information to the Board by the agency for the Board's consideration and action.**

### **Information to be provided to the Board on NEW CASE filings**

1. The utility's name and case number.
2. The type of service(s) provided by the utility.
3. The geographic area (county, town/city, suburb, community, etc.) Served by the utility.
4. The approximate number of users served (in each category of service, if more than one) served by the utility.
5. Nature of the change requested by the utility and the utility's stated reason for requesting the change.
6. Whether or not RUCO has received or is aware of any user complaints regarding the operation of the utility and, if so, the nature and extent of the complaints.
7. RUCO staff's preliminary assessment and/or opinion as to the merits of the utility's request and the anticipated effect of the change on users.
8. RUCO staff's initial or anticipated intervention action(s) on behalf of the affected utility users.

### **Information to be provided to the Board on ONGOING CASE activity**

1. The utility's name and case number.
2. The type of service(s) provided by the utility.
3. The geographic area (county, town/city, suburb, community, etc.) Served by the utility.
4. The approximate number of users served (in each category of service, if more than one) served by the utility.
5. RUCO's evaluation, if any, of the utility's past performance in serving its users, including consideration of the following:
  - a. The quality and assured supply of its products, if applicable.
  - b. The age and reliability of its delivery/distribution system.

- c. Its reserve or emergency backup facilities, if any.
  - d. Its need and plan for system repairs, replacements & upgrades, if any.
  - e. Its capacity and plans for expansion of the system or service area, if any.
  - f. Its charges/fees to users for system expansion or service extensions.
  - g. Its non-metered (non-consumption of product) fees for meter installation, meter connects/disconnects, security deposits, late charges, etc.
  - h. Its general level of customer service, including the timely and efficient completion of service connections and disconnections, new construction and handling of emergency repairs and resolving billing and other complaints.
  - i. Based on the information gathered under paragraphs **5-f** through **5-h**, an estimate as to how the utility compares with other, similar utilities in terms of industry norms and reasonable utility users expectations.
- 6. Brief summary of RUCO's intervention activities to date.
- 7. Actual or estimated success of RUCO's intervention efforts to date.
- 8. Whether the information related to paragraphs **5-a** through **5-i** was gathered, analyzed and considered in RUCO's case intervention activities and, if so, how and to what degree it affected RUCO's recommendations.
- 9. RUCO's plans, if any, for continued intervention action in the case.