**BEFORE THE ARIZONA CORPORATION COMMISSION**

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| IN THE MATTER OF THE APPLICATION OF SOLARCITY FOR A DETERMINATION THAT WHEN IT PROVIDES SOLAR SERVICE TO ARIZONA SCHOOLS, GOVERNMENTS, AND NON-PROFIT ENTITIES IT IS NOT ACTING A S A PUBLIC SERVICE CORPORATION PURSUANT TO ART. 15, SECTION 2 OF THE ARIZONA CONSTITUTION. | Docket No. E-20690A-09-0346 |

**RUCO'S EXCEPTIONS**

The Residential Utility Consumer Office ("RUCO") hereby submits its Exceptions in the matter of the application SolarCity ("SolarCity" or "Company") for a determination of whether it is acting as a public service corporation ("PSC") when it provides solar service to Arizona's schools, government or non-profit entities by means of a Solar Service Agreement ("SSA"). For the following reasons, RUCO disagrees with the recommendation of the Administrative Law Judge ("ALJ") in her Recommended Opinion and Order ("ROO") that SolarCity is acting as a PSC when it provides solar service to Arizona's schools, government or non-profit entities by means of a SSA.

## I. INTRODUCTION

This is one of those exceptional cases where the Commission will be setting a course which will undoubtedly impact the implementation of a major renewable energy source in Arizona. Should there be any question as to whether the Commission's decision here will have a negative effect on the future of Arizona's solar industry, attached is a copy of the May 28, 2010 Phoenix Business Journal article entitled "Solar at schools may be "dead in the water" as judge recommends regulation". The article explains how school officials claim that regulation "…likely would end their foray into solar as a power source." The concerns raised in this article are not unfounded. In fact, they are consistent with the evidence in the record in this case – evidence which should give this Commission serious pause, given that the Commission has stated over and over again that its goal is to promote the proliferation of the solar industry in Arizona, not impede it.

The real decision in this case is whether the Commission truly wants to encourage the proliferation of the solar industry in this state. This policy decision rests with the Commission. Adoption of the ROO signals to the solar industry that Arizona has taken a step backward in its efforts to secure carbon-free renewable energy for its residents.

The ROO's recommendation is restricted by its legal conclusion. By determining that the situation meets the textual definition of a PSC, the ROO sidesteps the public interest concerns. Yet, the Arizona courts, as will be more fully explained below, have made it clear that a PSC determination must include a public interest analysis. RUCO believes that the ROO extends an overly-broad definition of a PSC, which is the opposite approach the Commission should take under the subject set of circumstances. RUCO believes that a finding that the Company is not acting as a PSC from a public policy and public interest perspective further supports the legal analysis that the company is not acting as a PSC. RUCO believes that the public interest and the goals of the Commission would be furthered by such a finding here and that the law would support such a finding.

## II. PUBLIC POLICY OVERWHELMINGLY WEIGHS AGAINST REGULATING SOLARCITY AND OTHER THIRD PARTY PROVIDERS THAT UTILIZE SSA'S.

### A. Regulation Will Hinder Development of Solar Generation

The Commission has made it clear that it intends, as a matter of policy, to encourage the development of the solar industry in Arizona. If so, then the most compelling policy reason against regulation is the uncontroverted evidence in the record that regulation of any kind will impede the development of the solar industry in Arizona.

According to the Company, "Regulation is likely to drive out numerous, if not all, solar providers from the State of Arizona. SolarCity's profits and its investors' returns would suffer causing them to look to other less expensive States for solar investment." Not a single intervenor in this case contested this claim – even those who support regulation.[1] The difficulty, according to Solar City's Chief Executive Officer and President, Lyndon Rive is the constraint on tax equity. Tax equity is the most valued aspect in the solar industry today. Tax equity financing is the ability of the lenders to monetize the tax credits that are available for the next eight years. The returns on tax equity financing are very low and only banks and some insurance companies are willing to provide tax equity financing. As a result, tax equity financing is very scarce.

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[1] RUCO does not turn a blind eye to the irony of SRP's participation in this docket. It argues for regulation of installers when SRP itself is immune from the very regulation it claims is necessary to impose on SolarCity. Furthermore, SRP declined to offer a witness for cross-examination at hearing in order to fully examine its rationale. It is interesting to note that adoption of the ROO would have the effect of discouraging SSA's everywhere in Arizona except in SRP's territory. Conversely, APS does not oppose SolarCity's application.

The lenders that will provide tax equity financing are few and far between and, given the low returns, are not willing to take on any additional risk. Regulation to any degree represents uncertainty and added cost, and prospective lenders will look elsewhere to lend. Other states, where there is no regulation, will be more “attractive” to lenders and Arizona and solar customers will be the losers. The Company’s argument makes sense. It was questioned during the course of this case but there was no evidence in the record to refute the Company’s claim.

**B. SSA's Are A Financing Mechanism That Promotes Solar Installations Without Any Threat To Public Safety.**

Not only do SSA’s promote solar generation, they are in the public interest for other reasons. In many ways SSA’s are a preferable financing mechanism compared to either a lease or purchase arrangement. The SSA requires no upfront costs. The SSA establishes a repayment schedule predicated upon the amount of electricity produced and requires the installer to regularly maintain the installation. With a lease, the customer usually pays a monthly fixed charge regardless of performance, and the rooftop owner (lessee) is responsible to maintain the panels. With the purchase, the customer pays all of the upfront costs and bears all of the maintenance risks. Only under the SSA does the risk of poor performance fall entirely on the provider.

The risk of a poorly performing installation provides the incentive to install a good working product. Since the provider does not get paid if the equipment does not generate electricity the provider is encouraged to maintain the product in good working order. This encouragement also serves another important Commission policy objective – the use of more green energy. Since the installer is repaid based on the installation’s electrical output, the installer has a monetary incentive to install the system in order to promote the greatest amount of generation. This is a motivation the installer does not necessarily have when it installs a system that is not financed through a SSA.

The Commission's jurisdiction over the SSA's is not likely to further serve or protect the public's health and safety. There are numerous state and local laws and ordinances that already provide the consumer this protection. Solar installers must comply with state law. The Arizona Consumer Fraud Act prohibits deceptive practices (See ARS §44-1522 et seq.). In addition to a private right of action under this Act, the consumer has the benefit of having the Attorney General bring a claim on his or her behalf and also seek monetary relief. The Commission's complaint process precludes monetary relief.

There is little risk of physical or other harm to the consumer. State law already establishes standards for selling and installing "solar energy devices". ARS §44-1762 requires at least a one or two-year warranty for certain parts. An installer must meet standards established by the Registrar of Contractors and must be a licensed solar contractor under Title 32, chapter 10, article 4. The installation must comply with any consumer protection rating and safety standards adopted by the Arizona Department of Commerce.

These agencies are also in a better position to monitor and prevent any perceived harm to the public. These agencies are tasked with preventing certain types of harm and have the specific expertise to do the same. The Commission's oversight is not meant to be duplicative of these other state agencies. For example the Registrar of Contractors Office ("ROC") and local municipalities are in the best position to establish and enforce standards to preserve the structural integrity of rooftops when solar installations are placed on them. Id. To RUCO's knowledge, the Commission's Staff has no expertise or training to conduct such inspections.

If in fact the Commission's role here is duplicative, it begs the question of what the point of regulation would be in this case. The effect would be to impede the proliferation of the solar industry in Arizona. In other words, the effect would be to establish a policy which contravenes the Commission's stated goals and policies on renewable forms of generation. What is the quid pro quo? What is the benefit to be gained by regulation? RUCO is at a loss to understand why the Commission would approve such a result if the law allows otherwise. Based on the evidence in the record, added regulation – even "light" regulation – will result in either the decrease of the number of solar installers, or an increase in the cost of distributed solar. Either way, the Arizona consumer loses.

Nor does the Commission have the resources required to regulate the SSAs. Even "regulation light" will require the use of Commission resources. The Commission, like every other state agency, is under tremendous pressure given the State's current economic deficit. It is public knowledge that rate cases are taking longer to process; extension requests are becoming the norm, and not the exception. The number of large rate applications is increasing and overall resources are becoming more and more constrained. This is not the time for the Commission to burden its Staff with even more tasks when there is a strong case against regulation.

**C. Regulation Of SSA's Promotes Selective Regulation**

Another policy consideration alluded to above is the decision to regulate will have the effect of selective regulation. The Commission does not regulate solar installers like SolarCity when the customer selects a financing option other than an SSA. If the Commission were to find it has jurisdiction over solar installers when customers choose to finance the installations (but not when customers purchase or lease them), the Commission's decision would result in oversight of some installations but not others. Why should the manner of finance dictate whether a transaction is regulated or not? For public policy reasons, the Commission should not engage in selective enforcement.

### D. The Commission Correctly Exercises Oversight of Distributed Generation Through Its Net Metering Rules.

It is also sound public policy and in the public's interest for the customer to put excess green energy back on the grid. In one way, the Commission has asserted its jurisdiction over this type of transaction through its net metering Rule R14-2-1811. Through this Rule, utilities must file tariffs which set forth the conditions and price of those transactions. In this situation, the customer is furnishing the excess electricity that it owns to the utility for the public good.

With excess electricity, the relationship is between the customer and the ESP. The solar installer plays no role and has no interest in this transaction. Therefore, the regulated activity is the furnishing of electricity from the customer to the utility. The sale of excess electricity generated from a DG installation is a regulated transaction. Unlike negotiations with a solar installer, the consumer is not able to negotiate terms, conditions and price with the utility for this transaction. The regulatory burden for compliance rests with the regulated utility, not the consumer. And, the public enjoys the benefit of energy that was generated from the sun.

RUCO does not raise these public policy arguments lightly. These are strong public policy arguments and are the motivating factors behind RUCO's recommendation in this case. RUCO would be the first to support regulation of some type if it thought that there was the likelihood of monopoly abuse and/or strong public policy arguments in favor of regulation. But in this case, RUCO has yet to see even one benefit of regulation that trumps these public policy concerns. The ROO sidesteps these important policy considerations.

## III. THE LAW SUPPORTS A FINDING THAT THE COMPANY IS NOT ACTING AS A PSC

RUCO believes that the law supports a finding that the Company is not acting as a PSC. The ROO disagrees with RUCO and adopts the positions taken by Staff, SRP and TEP. However, RUCO offers the following legal points in response to some of the findings in the ROO which RUCO believes are, at the very least, misguided, if not legally correct.

The Arizona courts have made it clear that the legal determination of what constitutes a PSC is dependant on the facts and is more than just an overly-broad application of a textual definition. The Arizona Courts have said and required: (1) a presumption against regulation[2]; (2) a prohibition against an unfettered power to issue CC&Ns[3]; (3) a declaration that "furnishing" requires a transfer of possession[4]; and (4) that even when a corporation meets the textual definition of a PSC, jurisdiction shall be denied if the public interest requires it[5]. Looking at the cases in Arizona, considering the public policy, and from just a common sense standpoint, the facts in this case support a legal conclusion that SolarCity is not a PSC.

RUCO respectfully disagrees with the suggestion that the legal analysis is a one-step analysis once a text book finding has been made. ROO at 27. The ROO, relying on the Supreme Court's 1959 decision, *Trico Elec. Coop., Inc. v. Corp. Comm'n,* 86 Ariz. 27, 34-35, 339 P.2d 1046, 1052 (1959), concludes that where an entity is clearly furnishing electricity under the Arizona Constitution, and such activity is not merely incidental to the primary business activity and not clothed with the public interest, the analysis ends and the entity is a

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[2] *Arizona Corp. Commission v. Continental Sec. Guards* (App. 1967), 5 Ariz. App. 318, 426, P. 2d 418 vacated 103 Ariz. 410, 443 P.2d 406

[3] *Williams v. Pipe Trades Industry Program of Arizona*, 100 Ariz. 14, 20, 409 P.2d 720, 726 (1966).

[4] *Williams* at 20, 409 p.2d 720, 724

[5] *Serv-Yu*, at 237-238, 219 P.2d. at 325-326

Public Service Corporation. A *Serv-Yu* analysis is not necessary as it would be superfluous. Id.

In 2007, the Arizona Court of Appeals interpreted the *Trico* case differently. The Arizona Court of Appeals in *Southwest Transmission Cooperative, Inc., v. Arizona Corporation Commission, 213* AZ. at 427, 142 P.3d at 1240 (App. 2007) confirmed that consideration of the *Serv-Yu* factors is necessary and not superfluous even where the situation meets the textbook definition. Confirming that the analysis was a two-step analysis, the Court said:

> Merely meeting the textual definition, however, does not establish an entity as a "public service corporation." *Sw. Gas,* 169 Ariz. at 286, 818 P.2d at 721. To be a "public service corporation," an entity's "business and activities must be such as to make its rates, charges and methods of operation, a matter of public concern, clothed with a public interest to the extent contemplated by law which subjects it to governmental control-its business must be of such a nature that competition might lead to abuse detrimental to the public interest." *Trico Elec. Coop., Inc. v. Corp. Comm'n,* 86 Ariz. 27, 34-35, 339 P.2d 1046, 1052 (1959) (citing *Gen. Alarm, Inc. v. Underdown,* 76 Ariz. 235, 262 P.2d 671 (1953)).
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> The fact that an entity may incidentally provide a public commodity is not sufficient to subject it to regulation, it must be in the business of providing a public service. *Nicholson,* 108 Ariz. at 320, 497 P.2d at 818; *Gen. Alarm,* 76 Ariz. at 239, 262 P.2d at 673. In *Serv-Yu,* the Arizona Supreme Court articulated eight factors to be considered in identifying those corporations " 'clothed with a public interest' and subject to regulation because they are 'indispensable to large segments of our population.' " *Sw. Gas,* 169 Ariz. at 286, 818 P.2d at 721 Those eight factors are:
>
> (1) What the corporation actually does.
>
> (2) A dedication to public use.
>
> (3) Articles of incorporation, authorization, and purposes.
>
> (4) Dealing with the service of a commodity in which the public has been generally held to have an interest.

> (5) Monopolizing or intending to monopolize the territory with a public service commodity.
>
> (6) Acceptance of substantially all requests for service.
>
> (7) Service under contracts and reserving the right to discriminate is not always controlling.
>
> (8) Actual or potential competition with other corporations whose business is clothed with public interest.
>
> *Id.* at 286, 818 P.2d at 721; *Serv-Yu,* 70 Ariz. at 237-38, 219 P.2d at 325-26. The *Serv-Yu* factors act as guidelines for analysis, and we are not required to find all eight factors to conclude that a company is a public service corporation. *Sw. Gas,* 169 Ariz. at 287, 818 P.2d at 722.

*Southwest Transmission, 213* AZ. at 431-432, 142 P.3d at 1244-1245.

It could not be clearer from the *Southwest Transmission* case that merely satisfying the textbook definition is not enough to establish a PSC. There is another step – even the Supreme Court in *Trico* case discussed it – the public interest element – whether the entity in question is clothed with a public interest to the extent that governmental control is necessary to prevent competitive abuse. *Trico Elec. Coop., Inc. v. Corp. Comm'n,* 86 Ariz. 27, 34-35, 339 P.2d 1046, 1052 (1959) (citing *Gen. Alarm, Inc. v. Underdown,* 76 Ariz. 235, 262 P.2d 671 (1953)). The *Serv-Yu* factors provide guidance in determining this other very important legal step.

Given that the ROO considers a *Serv-Yu* analysis “superfluous” in this case, it is not surprising that the ROO concludes that a *Serv-Yu* analysis supports its conclusion that SolarCity is a PSC. ROO at 28. RUCO would simply refer to its Closing Brief at pages 7-14 for a point by point review of why RUCO believes the *Serv-Yu* analysis supports a finding that SolarCity is not acting as a PSC.

While RUCO and the ROO may disagree on the applicability of the *Serv-Yu* factors in this case, there is one point which both RUCO and the ROO agree. The ROO, at page 47 states:

> "SolarCity is not a monopoly and does not have market power and competes for business, at least with the schools and governmental entities, through an RFP process. Thus the need to regulate rates is not the same as with the traditional monopolistic utility service. However, after installing the equipment, SolarCity becomes the only solar provider at the site for at least the term of the contract." ROO at 47.

**The Company, as the ROO points out, is not a monopoly, does not have market power and it bids on an RFP process**. The question of this Company exerting market power or somehow manipulating the market for competitive gain, or an unfair competitive advantage is not even at issue. The ROOs concern appears to be focused on "reliable service at just and reasonable rates." ROO at 68. But this concern is hardly persuasive for the reasons stated above. The Company is paid based on the amount of energy it produces so it has a built in incentive to offer reliable service. To the extent the Company is unable to provide service the customer still meets its load requirements through its main service provider.

## IV. SOLARCITY IS NOT "FURNISHING ELECTRICITY"

The discussion to this point has focused mostly on the second step of the legal analysis. The facts in this case would also support a finding that SolarCity is not a PSC under the first step of the legal analysis – the textual definition step. The ROO concludes that SolarCity is acting as a PSC based on a finding that SolarCity is furnishing electricity. ROO at 25. From RUCO's perspective, the law supports a finding that SolarCity is not furnishing its customers with electricity and therefore not acting as a PSC. The ROO cites as support for its conclusion that the Company is furnishing electricity the Arizona Supreme Court's decisions *Williams v. Pipe Trades Industry Program of Arizona*, 100 Ariz. 14, 20, 409 P.2d 720, 726 (1966). and

*Southwest Transmission Cooperative, Inc. v. ACC*., 213 Ariz. 427, 430, 142 P. 3d 1240, 1243 (2007). Both cases are distinguishable from the current case, but of the two the *Williams* case is closer to the present set of circumstances. The ROO's support for its conclusion that SolarCity is furnishing electricity appears to be based on its conclusion that there is a transfer of possession of the electricity similar to what took place in the *Southwest* case. ROO at 22. However, such an analysis is highly fact specific. Based on the facts presented here, RUCO believes there is no transfer of possession in SolarCity's case.

The SSA is simply a financing mechanism which allows SolarCity's customer to take advantage of significant tax and depreciation incentives without prohibitive up-front costs. SolarCity provides its customers with the financing, design, installation, operation and maintenance of a solar panel system on the customer's property, the terms of which are described in the SSA. The electricity itself is never owned or even possessed by SolarCity. The electricity is not transferred or sold to the customer. The electricity is generated on the customer's rooftop. While it is true SolarCity owns the equipment that generates the electricity, that equipment is in the physical possession and control of the customer. The electricity is owned and possessed by the customer from its inception. Hence, like the case in *Williams*, but for different reasons, "there is no contemplated transfer of possession."

## V. CONCLUSION

In conclusion, RUCO believes that the SSA arrangement between SolarCity and its customers should not be regulated by the Commission. RUCO believes that the arrangement does not meet the textual definition of PSC. Nonetheless, the SSA arrangement does not meet the criteria set forth in *Serv-Yu.* Finally, it is not in the public interest to regulate the SSA arrangement. The Commission should reject the ROO in its entirety.

RESPECTFULLY SUBMITTED this 10th day of June, 2010.

Daniel W. Pozefsky
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# ATTACHMENT

Phoenix Business Journal - May 28, 2010
/phoenix/stories/2010/05/24/daily83.html

Phoenix Business Journal

Friday, May 28, 2010

# Solar at schools may be 'dead in the water' as judge recommends regulation

Phoenix Business Journal - by Patrick O'Grady

Plans to put solar systems on school and government roofs through solar-service or power-purchase agreements may be placed on hold after an administrative law judge said companies offering such agreements should be regulated as public utilities.

Judge Jane Rodda has recommended to the Arizona Corporation Commission that **SolarCity** and others that supply power to schools, nonprofits and governments be subject to ACC regulation.

SolarCity had filed the case seeking to have the work it does at schools ruled not a utility operation.

"When SolarCity utilizes an SSA arrangement, it is selling electricity to the school, governmental entity or nonprofit and is 'furnishing electricity' as included in the definition of a 'public service corporation'" in the Arizona Constitution, Rodda wrote.

The recommendation means the ACC could have a host of options in regulating the activity between companies that install solar systems and sell the power as third-party providers, and the buyers of that power.

ACC officials said it will be up to the commission to determine if the recommendations are adopted as laid out or to come up with their own plan. The commission has not set a hearing on the issue, and the recommendations cannot take affect without the commission's approval.

School officials said this likely would end their foray into solar as a power source.

"If the commission goes along with this ruling, we're dead in the water," said David Peterson, associate superintendent of the Scottsdale Unified School District, which was at the heart of SolarCity's case.

Foster City, Calif.-based SolarCity has used similar agreements in other states, but has not brought them to Arizona because of the constitutional requirement. the company petitioned the ACC to rule that providing the power to schools would not make it a public utility because it fell outside the boundaries of what the law considered.

SolarCity spokesman Jonathan Bass said the recommendation, if approved by the ACC, would end the company's ability to supply solar to schools. It offers a lease program, but those likely would be cost-prohibitive for schools.

"It would eliminate a component of what we could do, and cost the state jobs," he said.

Schools, nonprofits and governments in other states adopt solar agreements in which they buy energy from a third party that owns the system placed on their roofs, because it allows them to lower the cost by taking advantage of federal tax credits aimed at spurring solar development.

Other players, such as Tucson-based Solon Corp., have been partnering with schools on such agreements and looking at working in municipal areas. Arizona is the only state whose constitution defines what a public service corporation would be.

Jordan Rose, founder of Rose Law Group PC, said the recommendation could cost schools and governments millions to adopt solar. Rose Law represented SolarCity in its case.

"A PPA/SSA is simply a financing tool, used in every other state in the nation, to allow widespread proliferation of solar," Rose said via e-mail. "Regulation of these PPA providers would thwart the free market and treat these start up solar companies like monopolies."