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Division of Public Utilities

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MEMORANDUM

To: Utah Public Service Commission

From: Division of Public Utilities

Philip J. Powlick, Director
Artie Powell, Manager, Energy Section
Charles Peterson, Technical Consultant
Jamie Dalton, Utility Analyst

Subject: In the Matter of the Application for Approval of an Electric Service Agreement between Rocky Mountain Power and US Magnesium LLC. Docket No. 09-035-20

Date: November 5, 2009

RECOMMENDATION, (ESA only): Approval with conditions on future contracts

The Division recommends that that Commission approve the Electric Service Agreement (ESA) between Rocky Mountain Power (Company or RMP) and US Magnesium LLC (US Mag).

The Division recommends that the Commission direct the parties to shorten the time between the approved changes in the pricing terms of the Schedule 9 tariff, or other indexes, and changes in the pricing terms of future ESAs to no more than 90 days. Changes in the Schedule 9 tariff, or other indexes, may occur through general rate cases, single item rate cases as provided for in Utah Code Annotated (UCA) 54-7-13.4, or other procedures before the Commission.

BACKGROUND

On or about August 20, 2009, Rocky Mountain Power, a division of PacifiCorp, filed a proposed electric service agreement for Commission approval between it and US Magnesium, LLC. This

ESA is a modification of the existing ESA that expires on December 31, 2009. The existing ESA was approved by the Commission in Docket No. 03-035-19. Subsequent to the filing, the Division met with representatives of the parties, submitted data requests, and had informal information exchanges with RMP and US Mag.

The Commission held a scheduling conference on August 13, 2009 and subsequently issued a Scheduling Order requiring the Division and the Office of Consumer Services to respond to the Company's application by November 5, 2009. This memo, outlining the Division's investigation and conclusions, is in response to the aforementioned Commission Order.

ANALYSIS

The proposed contract between PacifiCorp and US Mag outlines the terms, pricing, and conditions under which PacifiCorp would continue to provide electric service, including interruption and curtailment, and replacement power to the US Mag facilities. The contract is broken up into articles, which this analysis will address as needed, by article number.

Article 2 deals with the term of the agreement. The proposed term is five years beginning January 1, 2010 and ending December 31, 2014. The expiring ESA had a term of five years.

Article 3 sets forth the formulae for the annual contract price per MWh. The formulae show that there will be annual adjustments after 2010 to account for changes in Schedule 9 rates plus an amount to bring the prices more in line with US Mag's cost of service.

Article 4 sets out the terms for power curtailment. Article 5 covers replacement power.

The US Mag cost of service is currently several million dollars above the revenues received under the current contract.[1] Testimony by Company witness Paul Clements indicates that the intent of the proposed contract is to close this gap between revenues and cost of service over the five year term so that US Mag will be at, or near, its cost of service by the time the contract

[1] US Mag witness Roger Swenson disputes that US Mag's cost of service differential to revenues is as great as PacifiCorp asserts. However, that issue will not be decided in this docket. See, Prefiled Direct Testimony of Roger J. Swenson, p. 7.

ends.[2] The Division agrees that it is appropriate to bring the contract rates into line with cost of service and that a stepwise approach is warranted given the detrimental effect that a sudden large increase in rates is likely to cause US Mag.

The proposed contract rates will not change during a contract year, even though there is currently a rate case in progress that may result in changes to Schedule 9, likely in February 2010. The Company has indicated that it intends to file a single-item rate case for two large projects in February, with a potential additional rate increase in June. There will likely be other rate cases during the term of the contract. However, the contract provides for only annual updates that could result in US Mag's rates lagging the rates of Schedule 9 customers by up to 12 months. This is a concern to the Division. The Division believes that it would be more in the public interest if US Mag's rates adjust to changes in Schedule 9, or other indexes within a shorter period, preferably within 90 days or less of changes to the index. The Division recommends that the Commission require that in any future ESA contracts that rates adjust within 90 days after adjustments to Schedule 9, or other adjustment mechanisms, go into effect. This should include any schedule changes or surcharges that result from single-item rate cases under UCA 54-7-13.4. However, as mentioned above, the Division is not recommending that this contract be altered.

DISCUSSION

The Division understands that rate stability is important for customers. The Division, however, also takes into consideration that Schedule 9 customers see their rates adjust when new Schedule 9 tariffs go into effect, usually after a general rate case.[3] The ESA with US Mag creates benefits for RMP, and for its customers generally, by providing for curtailment of power to US Mag when certain conditions arise, including threats to the general reliability to PacifiCorp's system.[4] Thus, US Mag could be shut down, while remaining RMP customers could continue to receive electricity uninterrupted. This potential benefit has value, although this benefit cannot be readily quantified.

[2] Prefiled Direct Testimony of Paul H. Clements, pp. 5-6.
[3] As a result of a general rate case, of course, nearly all other RMP customers' rates change immediately when new tariffs go into effect.
[4] Section 4.2.

Taking these considerations into account, the Division believes that it is reasonable and in the public interest that US Mag's ESA include features beneficial to US Mag such as a lag in rate adjustments compared to most other RMP ratepayers.

Changes to the proposed ESA include updated rates as set forth in Exhibit 1 of the ESA, new provisions concerning the prospective implementation of an energy cost adjustment mechanism (ECAM), the implementation of a demand-side management surcharge, and prospective costs that may be ordered recovered by the Commission due to greenhouse gas emission regulation. Generally, these provisions state that US Mag understands and accepts that it will be subject to any charges related to these items "if so ordered by the Commission."[5] Additionally, the Division believes that future ESAs should contain provisions for changes that may result in one-item rate cases as provided in UCA 54-7-13.4 "Alternative Cost Recovery from Major Plant Addition." The Division recommends that the Commission direct the parties to include such a provision in future contracts.

CONCLUSIONS AND RECOMMENDATIONS

Based upon the above outlined analysis, the Division recommends Commission approval of the proposed ESA contract between US Mag and PacifiCorp. With the caveats presented herein, the contract terms and pricing appear to be just, reasonable, and in the public interest.

The Division believes that future contracts between the Company and US Mag need to have more timely pricing revisions pursuant to changes in Schedule 9, or any future indexing mechanism. Provisions will need to be made in future contracts for single-item rate cases that are prospectively going to occur, presumably beginning as early as the first half of 2010.

CC: Paul Clements, PacifiCorp
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[5] Sections 3.12-3.14.

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