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DEPARTMENT OF COMMERCE
Office of Consumer Services

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Date: November 7, 2011

Subject: Office of Consumer Services' Recommendation on the Application of Rocky Mountain Power for Approval of an Electric Service Agreement between Rocky Mountain Power and Kennecott Utah Copper LLC.
Docket No. 11-035-181
[redacted]

1 Background

On October 13, 2011, Rocky Mountain Power (RMP) filed for Public Service Commission (Commission) approval of a one-year Electric Service Agreement (ESA) between RMP and Kennecott Utah Copper LLC (Kennecott). The new ESA would begin on January 1, 2012 and end on December 31, 2012. A hearing on the matter is scheduled for November 14, 2011.

2 Contract Overview

<u>Kennecott Load</u>
The new ESA combines Praxair's and Kennecott's total load requirements for supplemental and back-up power requirements. The maximum combined load is expected to be [redacted]. In the new ESA, RMP is expected to provide more

[redacted] than in the prior contract.[1] In summary, both Kennecott's [redacted] in the new 2012 ESA compared to the 2011 ESA.

Kennecott Pricing

The 2012 Kennecott ESA is similar to the previous contract in that: (1) contract demand and energy charges are set based on current Schedule 9 demand and energy rates; (2) the monthly energy "scalar" ratios in the proposed contract are the same as in the 2011 contract and are applied to incremental energy rate changes resulting from any 2012 rate proceeding.[2] The energy scalar is represented by RMP as reflecting Kennecott's unique load profile compared to Schedule 9 customers.[3]

In the new ESA, the monthly energy scalars are determined in the same manner as the previous contract. The energy scalars are based on the ratio of Kennecott energy to Schedule 9 energy and using the same July 2009 –June 2010 period. In testimony supporting its Application, the Company did not analyze impacts on retail customers and Kennecott of applying the monthly energy scalars to projected Kennecott energy loads in the 2012 contract period.[4] Nor did the Company update the monthly energy scalars using more current information.

[redacted]

Provision 4.8 in the ESA allows Kennecott to make a [redacted] to RMP to avoid paying interest on monthly surcharges resulting from [redacted]). However, the contract does not specify a reconciliation process by which an [redacted] is trued-up to actual once final [redacted] are determined by the Commission.

[1]Information provided by Kennecott at an October 31, 2011 meeting between the Office and representatives from Kennecott indicates that Kennecott expects to [redacted] compared to previous years. Kennecott's anticipated operation of its resources is based on [redacted].

[2]Section 4.10 (ESA, pg. 6) sets forth the monthly on-peak and off-peak ratios that are used to develop the energy scalar applied to any incremental energy rate change that occurs in the contract period. There is no corresponding demand scalar. Therefore, any changes to Schedule 9 demand charges during the contract period are applied in full to Kennecott.

[3]Kennecott's "unique" load is represented as reflecting a different [redacted] and [redacted] compared to Schedule 9.

[4][redacted] Therefore, the Company could have requested expedited delivery [redacted]

3 Analysis of Key Issues

Kennecott Load

The Office has not identified any concerns with the proposal to subsume the Praxair load within the Kennecott contract.

Kennecott Pricing - Energy Scalars

The key pricing issue involves the proposed use of monthly energy scalars to provide Kennecott with a potential energy discount in the 2012 contract period. The Office's analysis of the proposed monthly energy scalars includes the related areas of COS principles, COS data, and impacts on retail customers.

- COS Principles

  From a cost-of-service standpoint, a fundamental ratemaking principle is that customers should pay rates that are cost based. The rates in the Kennecott ESA are appropriately based on Schedule 9 demand and energy rates. Absent a rate change in 2012, Kennecott would pay the same demand charges and on/off-peak energy rates as any other industrial customer taking service under Schedule 9.

  However, the development of the energy scalars, and the potential Kennecott energy discount for incremental rate changes occurring in 2012, has not been adequately justified by the Company. While the energy scalars are tied to a specific formula, no attempt was made by RMP to explain how the discount created by the scalars is representative of or a proxy for cost differences in serving Kennecott. The Office is not opposed to discounts that are well-supported with evidence demonstrating how a proposed discount accomplishes specific goals. Such goals could involve developing a rate that better reflects cost of service, contractual provisions to reflect operational differences or specific policy objectives.

  The Office raised the same concern in connection with the proposed 2011 Kennecott ESA and they were not addressed by the parties in testimony or by the Commission in its order approving the contract. The Office submits that the establishment of just and reasonable rates for this proposed contract requires the Commission to appropriately address this issue and make necessary findings.

- COS Data

  The development and application of the monthly energy scalars results in a data mismatch between the period the scalars are developed and then applied to Kennecott's energy load in the ESA. Specifically, the scalars are determined based on Kennecott and Schedule 9 energy data for 2009-2010 and those "stale" ratios will be applied to Kennecott's 2012 energy loads that [redacted].[5] To the extent that scalars or any formula for discounting purposes is considered, the development of these monthly scalars should have properly reflected projected energy loads for Kennecott and Schedule 9 in the 2012 "rate-effective" period of the contract.[6]

- Results and Impacts

  In OCS DR 2.1, the Office requested the Company to provide the results of a hypothetical "two percent increase in general rates" scenario, where the 2009-2010 monthly energy scalars contained in the ESA are applied to projected Kennecott monthly energy loads in 2012. The Office requested this scenario analysis in an attempt to determine the potential size of the benefit for Kennecott and impacts on retail customers resulting from the energy scalar. The Company also provided the results of updating the monthly scalars to July 2010 – June 2011 and applying those scalars to projected Kennecott monthly energy loads in 2012.

  The results of the Company's analysis are provided as [redacted] to the Office's memo. The results show that, under a hypothetical two percent rate increase scenario, Kennecott would receive a [redacted] The Office believes this analysis demonstrates that the rate impact of the scalars is likely to be [redacted] during the duration of this one-year contract. However, the size of this energy discount could [redacted] The results could also vary if [redacted].

[redacted] Reconciliation

Kennecott's option to make an annual [redacted] rather than incur monthly surcharges raises concerns about reconciling interim with final payments and the transparency of the true-up process. The Office asserts the Commission must implement a disciplined public process by which the [redacted] is determined and reconciled to actual once a Commission final order is issued in the applicable [redacted]. This process should include compliance filings and hearings before the Commission on the [redacted] amount and reconciliation to actual so parties can be confident that the amount assigned to Kennecott is appropriate and other retail customers do not pay higher rates as a result of this ESA provision.

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[5] To re-iterate, Praxair load is subsumed within Kennecott's load which [redacted]

[6] The Company asserts that it does not have a 2012 load forecast available for Schedule 9, which is necessary to create monthly energy scalars for 2012.

4 Conclusion

Based on the information provided by the Company in support of its Application, the Office cannot say whether the proposed Kennecott ESA is in the public interest. Contract terms relating to the energy scalar are not supported with evidence demonstrating they are consistent with sound COS principles and the analysis was not based on current data.

However, application of the energy scalars (specified in Section 4.10 of the contract) to Kennecott's projected 2012 loads appears to have [redacted] on Utah retail customers in 2012.

The Office also understands from our discussions with Kennecott and RMP that substantial changes will likely occur in the next contract. This will require the Commission providing the Division, Office and other interested parties sufficient time to review what could be a more complicated ESA with possibly greater impacts on retail customers.

5 Recommendations

Because the proposed Kennecott ESA [redacted] residential and small business customers, the Office will not oppose approval of the Kennecott ESA. However, the Office continues to raise concerns about the discount methodology because, if continued, it could have much greater impacts in the future [redacted].

If the Commission elects to approve the proposed Kennecott ESA, the Office recommends that:

1) The energy scalars used in the ESA not be viewed as precedent setting for any other special contract or future Kennecott ESA;
2) The next Kennecott ESA should be filed with the Commission at least 75 days before a hearing is held to consider RMP's Application;
3) Prior to Kennecott making a [redacted] proceeding there should be a defined process in place, including a compliance filing and hearing, to determine the amount of the payment and the means to true up payments based on interim rates. Any proposed payment should be brought before the Commission for approval.