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**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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IN THE MATTER OF THE APPLICATION OF US MAGNESIUM LLC FOR DETERMINATION OF LONG-TERM ECONOMIC DEVELOPMENT RATES AND CONDITIONS OF INTERRUPTIBLE SERVICE	DOCKET NO. 03-035-19
	<b>RESPONSE OF US MAGNESIUM LLC TO MEMORANDUM FROM DIVISION OF PUBLIC UTILITIES</b>

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US Magnesium LLC (“US Magnesium”) files this response to the Memorandum filed by the Division of Public Utilities (“Division”) in this docket dated October 10, 2003 (“Division Memo”). The Division Memo suggests that the Division cannot proceed with a substantive analysis of the Petition without additional specificity. The Division, however, has misinterpreted the need for and intent of the Petition. The Division Memo does not provide a sufficient justification to deny US Magnesium its right to have the Commission resolve disputed rates and terms of service in an orderly, timely and efficient manner.

The timing of US Magnesium’s Petition reflects an effort to avoid the types of problems encountered in Docket 01-035-38 upon termination of the Magcorp contract. The Petition asks the Commission to establish a schedule that will permit a reasoned, yet timely, analysis by all parties,

including the Division. Docket 01-035-38, which proceeded on an emergency, expedited basis, failed to produce a record sufficient to establish long-term prices and terms. That deficiency needs to be addressed in this docket at this time.

In order for US Magnesium to have a reasonable chance of survival, it needs much more certainty as to its long-term electric prices and conditions of interruption. Moreover, that certainty must be provided quickly. US Magnesium filed its Petition in this docket in order to permit a well-considered and timely determination of several serious issues that confront it.

The Division Memo requests additional specificity in three areas. First, it requests clarification of the term “economic development” as used in the Petition. Second, it asks for the specific price and terms desired by US Magnesium. Third, it asks about the status of negotiations with PacifiCorp. US Magnesium welcomes the opportunity to provide additional clarity on its Petition.

### **Economic Development**

The Division Memo asks for a definition of the term “economic development” as used in US Magnesium’s Petition. Simply stated, in requesting an economic development contract, US Magnesium asks for rates and terms for interruptible service that will give it a reasonable chance to survive. US Magnesium asks for due consideration of the long history of electric service to US Magnesium and its predecessors, and of the economic impacts that will result from the Commission’s determination.

Consideration of economic development in utility rates is directly authorized by Utah Code § 54-3-1: “The scope of definition ‘just and reasonable’ may include, but shall not be limited to, the cost of providing service to each category of customer, economic impact of

charges on each category of customer, and on the well-being of the state of Utah ....” In requesting an economic development contract, US Magnesium is asking the Commission to consider the economic impacts of its decision on US Magnesium, Tooele County and the State of Utah generally.

It is US Magnesium’s belief that a fully cost-based rate for interruptible service, properly determined, will be sufficient to enable it to continue its operations. Unfortunately, however, cost-based rates cannot be adequately determined or supported at this point in time because additional data and analyses are required. To the extent the Commission ultimately determines that cost considerations alone do not support rates and conditions of service necessary for US Magnesium operations to continue, US Magnesium submits that considerations of economic development and economic impacts should properly be taken into consideration.

Electricity for US Magnesium’s magnesium extraction facilities located on the west shore of the Great Salt Lake is much more than a source of energy to support manufacturing processes. Rather, electricity is a direct input into the manufacturing process, and electricity represents one of US Magnesium’s largest expenses.

Electric supply for the US Magnesium facilities has received more Utah regulatory attention over the years than probably any other PacifiCorp contract. In addition to lengthy Commission hearings in 1968 that made construction and operation of the facilities feasible in the first place, the Commission has revisited the terms of service to these facilities on many occasions, including proceedings leading to the approval of eight separate contract amendments over a 30-year period, as well as the proceedings in Docket 01-035-38 over the past two years. Furthermore, service to these facilities has been studied extensively by regulators in a 1992

economic incentive contract task force, a 1999 special contract task force, and the pending interruptible contract task force. Through all of these regulatory investigations and task force studies, the Commission has consistently recognized that the public interest of the State of Utah supports the continued operations of these facilities, and it has directed the utility to provide interruptible service at a steep discount to firm service for decades.

Prior Commission task force reports and orders provide one source of useful information on economic development considerations in the ratemaking process. For example, the 1968 Commission Order directed Utah Power to provide interruptible service to US Magnesium's predecessor at approximately 60% of the firm tariff rate. Excerpts from the 1968 Commission Order, as well as copies of several additional documents that may be useful<sup>1</sup>, are attached hereto.

The 1968 Order recognized the "great economic benefits that will result from development of our Great Salt Lake," and found that interruptible power supplied at a rate that "will justify the Project's proceeding" was the "only reasonable way the Project can proceed in this State." (at 53). This Order reflects the Commission's clear understanding of, and commitment to, its obligation to promote the economic well-being of Utah. This commitment and understanding was confirmed in a number of subsequent Commission Orders that approved eight separate amendments over a 30-year period, and through a variety of economic and electric supply conditions. Moreover, Utah Power has repeatedly represented that contract revenues were sufficient to cover costs. After Scottish Power acquired PacifiCorp, the utility began to argue

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<sup>1</sup> Attached are copies of excerpts from the 1968 Commission Order approving discounted service to US Magnesium's predecessor, the 1998 Commission Order approving the Eighth Amendment to US Magnesium's predecessor, the 1992 Economic Incentive Contract Task Force Report, the 1999 Special Contract Task Force Report, an August 1, 2003 Memorandum from the Division, and a letter from Tooele County regarding economic impacts of US Magnesium's operations.

that the contract did not cover its costs, and it began attempting to terminate the interruptible service that its predecessors had provided for many years. US Magnesium can only conclude that Scottish Power has little concern over economic development in the State of Utah. Fortunately, however, this Commission has repeatedly evidenced its commitment to the public interest and the economic development of this State.

An Economic Incentive Contract Task Force created as a result of Docket 90-035-06 produced a report dated December 14, 1992, a copy of which is attached hereto. This report recognized several situations in which an economic incentive contract may be appropriate, including situations in which a customer may “shut down or reduce operations at tariff price” or may “substantially increase its production only at an incentive price.” (at A-2). Several years later, a Special Contract Task Force stemming from Docket 97-035-01, and chaired by the Division’s Ken Powell, produced another report, a copy of which is also attached. This report also acknowledged that a customer may qualify for an economic incentive contract if it has an “ability and incentive to reduce or eliminate purchases at tariff rate” or “will not locate in Utah in the absence of special non-tariff rates.” (at 2).

As explained in the Petition in this docket, US Magnesium cannot reasonably expect to continue its operations in Utah or continue to contribute towards the economy unless it continues to receive interruptible service at a steep discount to tariff rates, as it has for over three decades. Only a long-term contract with rates and conditions of service that continue to make operations economical will permit US Magnesium to attract critically needed capital. US Magnesium is and will remain unable to attract needed investment without a clear view of its future production

costs, primarily electricity.

Simply stated, US Magnesium cannot continue in operation unless it continues to receive interruptible service at rates steeply discounted from firm service rates, as it has since 1968. If US Magnesium is not able to continue in operation, its significant contributions to the economies of Tooele County and the State of Utah will end. Thirty years of history, Utah statutes, prior Commission Orders and reports from prior Commission task forces all support US Magnesium's continued request for a long-term economic development contract.

### **Specific Rate Request**

The Division Memo notes that US Magnesium's Petition does not specify requested prices or terms of service. This was intentional, and it is appropriate given the status of this matter and the nature of the Petition. US Magnesium has not yet been given sufficient access to data and models necessary for a thorough cost analysis, and it does not believe that it would be useful at this early stage of the proceeding to suggest specific requested rates or terms of service. Rather, US Magnesium is requesting the commencement of a process that will lead to a reasoned, yet timely, determination of appropriate rates and terms.

The cost of providing interruptible service to US Magnesium is clearly one of the critical factors that the Commission should consider in setting long-term rates and terms for US Magnesium. Additional data and analyses not yet available to US Magnesium are critical to a proper determination of cost of service. The filing of US Magnesium's Petition in this docket is a necessary first step towards obtaining the data and analyses necessary to a determination of cost of service, and an ultimate determination of rates and terms of service that are just and reasonable in light of all relevant considerations.

The Commission's May 24, 2002 Order in Docket 01-035-38 acknowledged the lack of adequate documentation and analyses to support long-term rates or conditions of service, and it created a task force to address these deficiencies. While the task force has attempted to address the data and analytical deficiencies, it has enjoyed only limited success in obtaining critical data or in penetrating "black box" models.<sup>2</sup> While US Magnesium remains hopeful that informal requests submitted to PacifiCorp by the task force will provide some of the needed information and understandings, a full and adequate exploration of these issues will be possible only in the context of this docket, designed specifically to address long-term pricing and terms of service for US Magnesium.

Finally, the Division's August 1, 2003 Memorandum to the Commission concerning the current US Magnesium contract acknowledges that "there is insufficient data to determine whether the agreement as a whole is in the public interest and sets forth just and reasonable rates." No significant additional data has been produced since that time that could support a different conclusion. US Magnesium and the Division will be in a position to obtain the necessary data in this docket.

### **PacifiCorp Negotiations**

The Division Memo also asks about the status of negotiations with PacifiCorp. As it has illustrated to this Commission on several occasions, US Magnesium has been attempting to engage in meaningful discussions with PacifiCorp for long-term interruptible service rates and terms for many years. The May 24, 2002 Commission Order in Docket 01-035-38 was necessary

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<sup>2</sup> Magcorp filed a Request for Limited Review or Reconsideration in Docket 01-035-38 asking that PacifiCorp be required to retain and provide specific data. The Commission's Order on Petitions for Reconsideration denied this request.

because such discussions have not been possible. The filing of US Magnesium's Petition in this docket is necessary for the same reason.

For at least 5 months now, US Magnesium has been requesting a 10-year contract with terms that will give it a reasonable chance to continue its operations. To date, PacifiCorp's response has been an unwillingness to consider a contract term longer than 5 years or pricing discounts based on anything but short term market valuation estimates. Past experience suggests that this will continue to be PacifiCorp's position in this matter and that resolution will occur only after a hearing before this Commission. The analytical and discovery processes in this docket are likely to be complicated, controversial, and time-consuming. US Magnesium filed its Petition in this docket in order to give itself and others sufficient time to resolve these matters before they reach a crisis stage, as they did last time.

#### **US Magnesium's Request**

At this point, US Magnesium is requesting only that the Commission hold a scheduling conference to set reasonable deadlines for discovery, testimony and hearings. Only through this docket can US Magnesium begin the necessary discovery process. Also, it is important that hearing dates be established in order to give potential investors a time frame within which rate decisions can be expected. US Magnesium's goal with this filing is to initiate the necessary process and to establish a reasonable time frame that will give the Commission and all parties adequate time to deal properly with these serious issues.

US Magnesium respectfully requests that the Commission promptly hold a scheduling conference in this docket and set reasonable dates for discovery, testimony and hearings.



DATED this \_\_\_\_day of November, 2003

HATCH, JAMES & DODGE

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**CERTIFICATE OF SERVICE**

I hereby certify that a true and correct copy of the foregoing was mailed, postage prepaid, this \_\_\_\_ day of \_\_\_\_\_, 2003, to the following:

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