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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
Subject: In the Matter of Rocky Mountain Power for Approval of an Electric Service Agreement between Rocky Mountain Power and Kennecott Utah Copper LLC.
Docket No. 09-035-59

Date: October 15, 2009

RECOMMENDATION: Approval with conditions on future contracts

The Division recommends that that Commission approve the Electric Service Agreement between Rocky Mountain Power and Kennecott Utah Copper LLC.

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 and 31 tariffs, or other indexes, and changes in the pricing terms of future ESAs to no more than 90 days. Changes in the Schedule 9 and 31 tariffs, 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 procedure before the Commission.

The Division recommends that the Commission require a cost of service study, or similar showing that RMP's costs are being reasonably covered by the ESA, be performed regarding

Kennecott's ESA for any future ESA, and that the results of such a study be filed with the Commission no later than concurrent with the filing of a new ESA.

BACKGROUND

On or about August 11, 2009, Rocky Mountain Power (RMP, or Company), a division of PacifiCorp, filed a proposed electric service agreement (ESA) for Commission approval between it and Kennecott Utah Copper, LLC (Kennecott). 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. 04-035-68. Subsequent to the filing, the Division met with representatives of the parties, submitted data requests, and had informal information exchanges with RMP and Kennecott.

The Commission issued an action request to the Division on August 11, 2009, with a due date extended to October 15, 2009. This memo, outlining the Division's investigation and conclusions, is in response to the aforementioned Commission request.

ANALYSIS

The proposed contract between PacifiCorp and Kennecott outlines the terms, pricing, and conditions under which PacifiCorp would continue to provide backup, maintenance, and supplementary power to the Kennecott facilities. The contract is broken up into sections, which this analysis will address as needed, by section number.

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

Section 4, in conjunction with Exhibit 1, deals with rates and adjustments. One of the standards that the Division attempts to apply to special contracts is whether or not that contract covers its cost of service. In this case, the answer to this question is not readily apparent. Due to the nature of the service provided to Kennecott, a cost of service study was not performed for the current rate case, or in, at least, the recent past.

The Division requested and received from the Company an analysis that showed that the proposed contract costs tracked closely to the current Schedule 9 rates. The Company performed the analysis under two scenarios. The first scenario compared the proposed contract pricing with the current Schedule 31 and Schedule 9 tariff prices. In this scenario Kennecott's monthly load profile was assumed to be the same as it had been in 2008. The results of this first scenario indicate that the proposed ESA rates that are indexed to Schedule 31 (i.e. customer charge, facilities charge, backup power charge, and excess power charge) result in revenues that are about 6.5 percent lower than if the full Schedule 31 rates were used. The proposed ESA rates that are indexed to Schedule 9 (i.e. supplemental power and energy), which account for about 85 percent of the revenues under this scenario, result in revenues that are about 2.8 percent lower than the full Schedule 9 rates. Overall, proposed ESA revenues under the first scenario are about 3.4 percent lower than they would be if actual current Schedule 9 and 31 rates were used.

The second scenario was conducted similar to the first scenario except that it was assumed that Kennecott's own power plant went down and did not produce any electricity for the year. This is a relatively extreme situation. The monthly load profile was assumed to be the same as the average of the actual loads for the months of January, February, November and December 2008, the months when the Kennecott power plant is normally not in operation. The proposed ESA has a power charge that is 19 percent higher than is provided for in the current Schedule 9. This higher power charge is in effect to provide an incentive to Kennecott to operate its power plant during the summer months when RMP's power needs are at their peak. The results of the second scenario indicate that the proposed ESA rates that are indexed to Schedule 31 result in revenues that are about \$2,800 lower than if the full Schedule 31 rates were used. However, the proposed ESA rates that are indexed to Schedule 9, which account for essentially 100 percent¹ of the revenues under this scenario, result in revenues that are about 1.0 percent higher than the full Schedule 9 rates. Overall, proposed ESA revenues under the second scenario are about 1.0 percent higher than they would be if actual current Schedule 9 and 31 rates were used.

The customer charge, backup power charge, and excess power charge are somewhat lower than those laid out in Schedule 31. The supplementary power charge and energy charge, which

¹ Actually 99.94 percent.

accounts for 85 to (potentially) nearly 100 percent of the total revenues, closely match those in Schedule 9. The Division concludes that in this one-year ESA, that the rates contained within the proposed contract sufficiently cover the Commission approved costs that PacifiCorp is currently incurring.

The proposed contract rates will not change during the contract year, even though there is currently a rate case in progress that may result in changes to Schedules 9 and 31, 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. This could result in the ESA being more “out of the money” than it is currently. Given that this contract is for one year and given the testimony in the rate case to date, the Division does not believe this is a significant issue in this docket. However, the previous contract provided for only annual updates that could result in Kennecott’s rates lagging the rates of Schedule 9 and Schedule 31 customers by up to 18 months. This was a concern to the Division in Docket No. 04-035-68, and will continue to be one in the future. The Division believes that it would be more in the public interest if Kennecott’s rates adjust to changes in Schedules 9 and 31 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 Schedules 9 and 31, 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 single-item rate cases affect this contract since it will terminate after one year.

DISCUSSION

The Division understands that rate stability is important for customers. The Division, however, also takes into consideration that Schedule 9 and Schedule 31 customers see their rates adjust when new Schedule 9 and Schedule 31 tariffs go into effect, usually after a general rate case.² The ESA with Kennecott creates benefits for RMP and its customers generally including the fact that Kennecott’s supplies its own power during the peak summer months, which effectively

² As a result of a general rate case, of course, nearly all other RMP customers’ rates change immediately when new tariffs go into effect.

means that RMP does not incur the costs to acquire what otherwise would be a significant amount of additional peak power. During the relatively low load months of November through February when Kennecott does not operate its own plant, RMP can supply power relatively easily to Kennecott.

Additionally, under Section 6 of the ESA, RMP can curtail or interrupt power to Kennecott under the prescribed situations. This benefits other RMP customers since Kennecott is a relatively large load which could be reduced or eliminated before most other customers should RMP experience systemic reduction of power. Thus, Kennecott 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.

Taking these considerations into account, the Division believes that it is reasonable and in the public interest that Kennecott's ESA include features beneficial to Kennecott such as a lag in rate adjustments compared to most other RMP ratepayers, and that Kennecott's rates be a little below those of Schedule 9 and Schedule 31 customers. With this latter issue though, the Division believes it would be in the public interest for a cost of service study to be performed, so that regulators have an understanding of how, if at all, costs for RMP to serve Kennecott differ from other, especially Schedule 9, customers, and recommends that the Commission direct RMP to perform a cost of service study, or some reasonable alternative to this end.

Changes to the proposed ESA as compared to the expiring ESA include updating the rates set forth in Exhibit 1 of the ESA, and 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 Kennecott understands and accepts that it will be subject to any charges related to these items "if so ordered by the Commission."³ 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

³ Sections 4.7-4.9.

“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 contract between Kennecott 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 Kennecott need to have more timely pricing revisions pursuant to changes in Schedules 9 and 31, or any future indexing mechanism. The Division believes that Kennecott’s rates should closely match the experience of RMP’s other Schedule 9 and Schedule 31 customers if a cost of service study shows that it imposes comparable costs, or in the alternative, that Kennecott’s ESA provide for the reasonable recovery of such costs. 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.

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