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Date: November 15, 2010

Subject: Office of Consumer Services' Comments 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. 10-035-116

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1 Background

On October 18, 2010, Rocky Mountain Power (Company) filed for Public Service Commission (Commission) approval of a one year Electric Service Agreement (ESA) between Rocky Mountain Power and Kennecott Utah Copper LLC (Kennecott). The ESA is essentially an extension of the current agreement which expires on December 31, 2010 with two new provisions. The new ESA would begin on January 1, 2011 and terminate on December 31, 2011.¹ On October 28, 2010 the Company filed supplemental documents addressing some of the terms of the contract.

2 Issues

In this memo the Office of Consumer Services will not address every aspect of the ESA; rather we will discuss certain issues that we view as important to other customers of

¹The ESA establishes the terms and conditions for back-up and supplemental electric service to Kennecott.

Rocky Mountain Power and offer our comments and recommendations regarding those issues.

2.1 Changes in Rates.

Overview

The ESA pricing begins with Kennecott properly paying [Confidential], depending on the type of service required. It also requires that adjustments resulting from a Commission approved energy cost adjustment mechanism (ECAM), or other net power cost-related recovery mechanism, general rate cases or major plant additions application will be implemented concurrently with the Commission ordered effective date for customers under those [Confidential]. This concurrent treatment of rate increases is also appropriate. However, Kennecott's rates will not be adjusted to precisely align with the approved rate changes to [Confidential]. Kennecott's rates may only be increased by a calculated amount contained in Section 4.10 of the ESA. The calculation of the adjustment to [Confidential] is based on the percentage of Kennecott's [Confidential]. Any [Confidential] will be multiplied by the applicable ratio in the table in Section 4.10 of the ESA. Changes to [Confidential] for Kennecott.

Supplemental supporting documentation provided on October 28, 2010 indicates that "Kennecott desires that this one-year Agreement include assurance that rate changes allocated to Kennecott in 2011 adequately take into account Kennecott's unique load characteristics. In particular, Kennecott desires that energy related charges be allocated in a manner that reflects Kennecott's unique seasonal usage pattern and its flatter-than-tariff-class load profile."

Applicability to Different Types of Rate Increases

The Company has provided analysis of precisely how the proposed adjustment mechanism would work in the case of the approval of the ECAM as proposed by the Company. The Company has not provided any analysis of the outcome of such a mechanism in the case of a general rate case or the current major plant addition cases or if a different ECAM design is approved. Thus, the analysis provided does not cover a large percentage of the expected types of rate increases planned to occur in 2011, the time period covered by the proposed contract.

The Company has currently requested that the balance being deferred from MPA I begin to be collected on January 1, 2011. The Company has also requested that a rider collecting the annual costs associated with MPA I and the annual costs associated with MPA II be implemented on January 1, 2011. In total, the Company's request represents a 6.37 percent increase to the revenue requirement, which is a greater increase than the last two rate cases combined. Such a significant increase needed to have been specifically addressed within this contract approval request so that other customers can assess whether the proposed treatment produces an equitable outcome. The Company

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confirmed in the response to OCS data request 1.2 that the adjustment mechanism in the ESA would apply to rate increases associated with MPA I ² and II that the Company has requested the increase to go into effect January 1, 2011.³

The Company has indicated its intent to file its next general rate case in January 2010, which would result in another rate increase before this proposed contract expires. Since it is known and expected to have this kind of rate increase within the time period of the proposed contract, the Company should also have provided explanation and analysis of the adjustment mechanism on the impact of rates for Kennecott as well as a justification for why such an adjustment is appropriate.

Analysis

The Company has provided Kennecott's load characteristics and uses the Confidential, as the basis for the adjustment mechanism. However, the Company's use of Confidential may overstate the actual differences.

Figure 1 below shows a comparison of the Confidential:

Figure 1 Confidential

² Including the deferred amount from MPA 1.

³ In response to OCS data request 1.3 the Company stated that "Confidential."

Figure 2 below shows a comparison of the Confidential.

Figure 2 Confidential

In reviewing the load profiles for Kennecott and Confidential customers, Confidential. Despite these Confidential, the Company does not provide any additional evidence to justify the proposed adjustment mechanism. It is important to note that with any per kWh charge, each customer pays the rate times the number of kWh consumed. Therefore, if the rate is distinguished by on and off-peak times, a customer with more off-peak energy consumption will, by definition, pay less because its charges are based on usage. Therefore, it is not clear why an additional adjustment mechanism would be necessary. While the proportion exercise is interesting as a premise, the proposed rate schedule is devoid of an economic rationale. The proposed schedule would fix for the upcoming year a Confidential, not an appropriate assignment of costs of service. Such price difference must be accompanied with a cost of service rationale.

Further, no evidence whatsoever has been presented to demonstrate that any price adjustments are reasonable for other types of resources or for increases resulting from

general rate cases or MPA cases. The burden of proof is with the Company to provide evidence that the contract rates and terms are reasonable. Without this demonstration of reasonableness, allowing Kennecott to incur less than the full impact of rate increases to **Confidential** cannot be found to be in the public interest.

2.2 Interim Solution.

Overview

The Company indicates that the rate adjustment mechanism in the ESA is intended to be a short term solution to address the uncertainty associated with a potential ECAM that could be implemented during the contract term.

Analysis

As noted above, the explanation and analysis provided by the Company deal exclusively with the potential ECAM and is insufficient to demonstrate that this solution is reasonable or necessary for other any type of rate increases.

If the Commission approves this ESA it should explicitly state that this is an interim, not a long-term solution. The Commission must clearly indicate that it will not be sufficient for the Company to use the circular logic that a special contract with the adjustment mechanism was approved once so therefore it remains a reasonable solution. If any adjustment mechanism is proposed in future contracts the Commission should require evidence as to the reasonableness of that mechanism as it pertains to each and every type of rate increase to which the Company proposes to apply it. Other parties, including the Office, will also analyze the impacts that resulted from any application of the allocations proposed in this contract.

Because of the anticipated level of analysis that will accompany next year's Kennecott contract, the Company should be directed to file early enough with the Commission to allow such analysis prior to the desired hearing dates. It is unreasonable to repeatedly ask the Commission and the parties for expedited treatment of any special contract which the Company knows is going to expire.

2.3 ECAM Lump Sum Payment Option.

Overview

If the Commission approves an ECAM the ESA provides the option for Kennecott to request that RMP calculate a lump-sum annual ECAM adjustment amount for Kennecott which would allow Kennecott to avoid **Confidential** associated with a monthly surcharge. The Office is concerned with this provision since it is likely that ECAM rates would be based on an interim rate while auditing of the ECAM account is performed.

In Data Request 1.7 the Office asked:

If an ECAM is implemented Section 4.8 of the ESA allows Kennecott to request a calculation of the lump-sum annual amount to satisfy its obligation rather than paying a monthly surcharge. Please describe precisely how the lump sum annual amount will be calculated.

Response: Similar to other customers, a surcharge will be determined annually to establish a targeted level of cost recovery due to the balance in the ECAM account. The Schedule 9 rate would apply to Kennecott and be multiplied against their forecast load for the 12 months of the collection period of the ECAM amortization. Once the annual estimated level is determined, it would be discounted at the carrying charge rate applied to the ECAM balance to determine the present value for up-front payment by Kennecott. If Kennecott paid this annual amount, at the end of the period, a true-up would occur to determine any residual amount of the balance due to or from Kennecott relative to the remaining balance in the ECAM deferral collected from other customers.

Analysis

The audit period for a potential ECAM is unknown. Some audits of Questar Gas' 191 account have taken over a year to complete⁴. It is likely that the "end of the period" in the response to OCS data request 1.7 refers to the annual determination of target levels, which would likely result in an interim rate, since waiting for a Commission final order following each audit of the ECAM account would not avoid the **Confidential**. A lump sum payment based on interim rates would require a true up mechanism. If Kennecott's calculated annual lump sum adjustment amount is less than its fair share of approved ECAM costs the difference could be allocated to other customers. As a result those customers could pay higher rates and a greater share of ECAM costs than what should appropriately be allocated to them.

The Office does not oppose the concept of Kennecott's option to make an annual lump sum ECAM payment, rather we advocate that the Commission must implement a disciplined process by which the lump sum is determined including a means to true up a payment based on interim rates. Another key element of the process would be transparency. The process must be public, including a public hearing to determine the lump sum amount, so that all parties can be confident that the amount assigned to Kennecott is appropriate and that other customers are not incurring higher rates as a result of this ESA provision.

If the Commission approves this ESA it should not allow the lump sum payment provision to be utilized until details of how such a public process would occur are defined.

⁴ Most parties have indicated an expectation that although an audit of RMP's ECAM account would likely be a more intensive process than the audit of Questar Gas' 191 account, it would fundamentally be operated in a similar manner.

Otherwise, customers cannot be confident that this contract will result in just and reasonable rates.

3 Recommendations

The Office recommends that the Commission deny approval of the ESA based on the lack of evidence that it is necessary and in the public interest.

However, if the Commission chooses to approve the contract the Office recommends that:

- 1) In the case of rate increases associated with RMP General Rate Cases or MPA cases all components of Kennecott's rates be increased uniformly with Schedule 9 and Schedule 31 rates;
- 2) The Commission clearly indicate the adjustment mechanism is intended as an interim solution and that the Company not be allowed to use approval of this contract with its interim solutions as evidence of reasonableness for any future contracts; and
- 3) Prior to Kennecott making any lump sum payment for ECAM rates there should be a process in place, including a public hearing, to determine the amount of the payment and the means to true up payments based on interim rates. These proposed payments should be brought before the Commission for specific approval.