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BEFORE THE ARIZONA CORPORATION COMMISSION

JEFF HATCH-MILLER  
Chairman  
WILLIAM A. MUNDELL  
Commissioner  
MIKE GLEASON  
Commissioner  
KRISTIN K. MAYES  
Commissioner  
BARRY WONG  
Commissioner

Arizona Corporation Commission  
**DOCKETED**  
DEC 21 2006

DOCKETED BY nr

IN THE MATTER OF THE APPLICATION )  
OF THE MORENCI WATER AND )  
ELECTRIC COMPANY FOR APPROVAL )  
OF AN ELECTRIC SERVICE AGREEMENT )  
WITH PHELPS DODGE SAFFORD, INC. )

DOCKET NO. E-01049A-06-0615

DECISION NO. 69200

ORDER

Open Meeting  
December 19 and 20, 2006  
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. The Morenci Water and Electric Company ("MWE") is certificated to provide electric service as a public service corporation in the state of Arizona.

2. On September 25, 2006, Morenci Water and Electric Company ("MWE") filed an application for approval of an electric service agreement ("Agreement") with Phelps Dodge Safford, Inc. ("PD Safford"). The Agreement would govern the terms under which MWE would serve a new copper mine under development by PD Safford north of Safford, Graham County. The proposed Agreement is conditioned upon Commission approval of a service territory franchise agreement between MWE and Graham County Electric Cooperative, Inc. ("Graham") in whose service territory the new mine is located. The application for approval of a service territory franchise agreement between MWE and Graham was filed concurrently under Docket Nos. E-01749A-06-0616 and E-01049A-06-0616.

1           3.       MWE does not have a tariff specifically for large industrial customers such as PD  
2 Safford. Phelps Dodge Morenci, Inc. ("PD Morenci") is served by MWE under an electric service  
3 agreement similar to the proposed Agreement and approved by the Commission in Decision No.  
4 66937 (April 21, 2004). Under this agreement, PD Morenci pays a customer charge of \$500 per  
5 month, an energy charge per kWh equal to MWE's system average cost of electricity (including all  
6 transmission or wheeling charges, losses and all other charges which may be incurred by MWE in  
7 connection with purchasing electric energy for resale to its customers) and a markup of \$0.000350  
8 per kWh, and a transmission charge of \$0.001738 per kWh. Similarly, the proposed Agreement  
9 would have PD Safford pay a customer charge of \$500 per month, an energy charge per kWh  
10 equal to MWE's system average cost of electricity (including all transmission or wheeling charges,  
11 losses and all other charges which may be incurred by MWE in connection with purchasing  
12 electric energy for resale to its customers) and a markup of \$0.000350 per kWh, plus a franchise  
13 charge per kWh equal to the franchise fee amount assessed by Graham as agreed to in MWE's  
14 proposed service territory franchise agreement with Graham. For as long as the PD Safford loads  
15 do not exceed a peak demand of 10,000 kW for three consecutive months, the franchise fee is  
16 proposed to be \$0.000350 per kWh. After the load reaches 10,000 kW per month for three  
17 consecutive months, the same per kWh factor of \$0.000350 applies, but with a floor of \$3,000 per  
18 month and a ceiling of \$20,000 per month. After the initial franchise period, which extends ten  
19 (10) years beyond December 31 of the year PD Safford loads exceed 10,000 kW for three  
20 consecutive months, the franchise fee is calculated in the same manner, but the floor of \$3,000 is  
21 dropped. MWE's purchased power and fuel adjustor does not apply to PD Morenci and would not  
22 apply to PD Safford, because any increases or decreases in purchased power costs are reflected in  
23 the calculation of MWE's system average cost of electricity.

24           4.       Much of the proposed Agreement between MWE and PD Safford is identical to the  
25 agreement in force between MWE and PD Morenci. Primary differences are references to PD  
26 Safford rather than PD Morenci as party to the agreement, the Agreement being conditioned upon  
27 Commission approval of a Service Territory Franchise Agreement between MWE and Graham,  
28 reference to a required interconnection with Southwest Transmission Cooperative to access

1 wholesale supplies of power and energy for the mine, location of the mine near Safford, Graham  
2 County, Arizona, reference to a franchise charge component of MWE's billing to PD Safford equal  
3 to the amount charged to MWE by Graham, and lack of any reference to a separate transmission  
4 charge billing component.

5         5. MWE has arranged for an interconnection with the electrical transmission facilities  
6 of Southwest Transmission Cooperative ("Southwest") to provide access to wholesale market  
7 supplies of power and energy to accommodate PD Safford. An existing Southwest 230 kV line  
8 between the Morenci Substation and the Dos Condados substation runs adjacent to the  
9 southeastern section of the PD Safford area and passes across its southeastern corner. A new  
10 interconnection substation (Hackberry Substation) is required to provide service to PD Safford,  
11 and the contractor began construction of these facilities on September 28, 2006. Service will be  
12 provided to PD Safford at 69 kV.

13         6. The interconnection facilities required to serve PD Safford, including the Hackberry  
14 Substation, are being constructed jointly by Southwest and MWE and are being paid for jointly by  
15 Southwest and MWE. Most of the facilities will be paid for and owned on a 75 percent Southwest  
16 25 percent MWE basis. Staff has been informed by MWE that the MWE portion of the funding  
17 for these facilities will be provided by the Phelps Dodge Corporation to MWE as "paid-in capital."

18         7. PD Safford began construction of its 69 kV power distribution system within the  
19 PD Safford area in August 2006. PD Safford will pay for, own, operate and maintain the 69 kV  
20 power distribution system facilities within the PD Safford area. Graham has been providing, and  
21 will continue to provide, construction and other pre-commercial operations power to the PD  
22 Safford Mine site. This power has been served to PD Safford for the past six months under an  
23 existing Commission approved "Schedule B, General Service Small Commercial" tariff rate. It is  
24 being delivered to the site over an existing Graham-owned single-phase line and required no line  
25 extension. Graham revenue for this power has grown over the past six months from \$245 per  
26 month to about \$4,000 per month.

27         8. Prior to the completion of construction of the Hackberry Substation, MWE will  
28 enter into Service Agreements for both firm and non-firm transmission services from Southwest.

1 The firm agreement ("firm wheeling agreement") will be for 10 MW of firm point-to-point  
2 transmission service under Southwest's Open Access Transmission Tariff ("OATT") at approved  
3 rates. The non-firm agreement ("non-firm wheeling agreement") will be for deliveries to meet  
4 loads of the PD Safford mine in excess of such loads being served under the firm wheeling  
5 agreement, also under Southwest's OATT at approved rates. Both agreements will be effective the  
6 first day of the month following completion of the Hackberry Substation. The costs MWE would  
7 pay to Southwest for firm and non-firm transmission services would be recovered by MWE from  
8 PD Safford in the energy charge component of the billing discussed in Section 6 of the proposed  
9 Agreement.

10 9. MWE is presently on schedule to begin sales to PD Safford under this Agreement  
11 on February 1, 2007. Energy sales are expected to grow from 336,000 kWh in February 2007 to  
12 53,586,000 kWh in May 2008 and to remain at that level over the life of the mine, currently  
13 estimated to be 16-18 years. Monthly peak demands are expected to reach 80 MW by May 2008.  
14 A load factor of approximately 90 percent, similar to that experienced by PD Morenci, is expected.  
15 Monthly energy sales to PD Safford by May 2008 would be about 38 percent of current monthly  
16 sales to PD Morenci. PD Morenci's load accounts for almost 98 percent of MWE's service load,  
17 and the addition of PD Safford will raise the special contract (mining) load to over 99 percent of  
18 MWE's service load. MWE has stated that "in the event of a power shortage, the non-mining load  
19 would have priority and continue to receive power (given that the non-mining load will be less  
20 than 1 percent of MWE's load)."

21 10. The Agreement would remain in effect as long as PD Safford maintains any  
22 business operations in the PD Safford area. Either party could terminate the Agreement upon  
23 giving the other party six months prior written notice.

24 11. Phelps Dodge Corporation is a New York corporation headquartered in Phoenix  
25 and licensed to do business in the State of Arizona. MWE, an Arizona corporation, is a wholly  
26 owned subsidiary of Phelps Dodge Corporation. PD Morenci and PD Safford are Delaware  
27 corporations, licensed to operate in the State of Arizona, and are wholly owned by Phelps Dodge  
28 Corporation to own and operate their respective mining properties in Arizona.

1           12.     MWE included in its filing a request that its application be reviewed in an  
2 expeditious manner and the Agreement be approved no later than the Commission's Open Meeting  
3 in December 2006. In its filing, MWE also agreed to waive the statutory 30-day time period for  
4 review and approval of the Agreement until December 19, 2006.

5           13.     MWE has stated that the proposed Agreement is intended to pass all costs related to  
6 serving PD Safford on to PD Safford, and Staff has found no evidence that it would not.  
7 Therefore, Staff has recommended that the proposed electric service agreement be approved.

8           14.     Staff has also recommended that, for ratemaking purposes, Phelps Dodge  
9 Corporation's funding of the MWE portion of the interconnection facilities be treated as a  
10 contribution-in-aid-of-construction such that the contribution will offset these assets in MWE's  
11 rate base in future MWE rate proceedings.

12           15.     Staff has further recommended that the MWE-owned interconnection facilities be  
13 segregated in MWE's property accounting records from other MWE assets as a distinct category  
14 clearly identified as related to the PD Safford service area.

15           16.     Staff's intent is to ensure that PD Safford, and not other MWE customers, pay all  
16 costs in connection with the interconnection facilities constructed for the benefit of and to serve  
17 PD Safford. In order to assure that PD Safford, and not other MWE customers, pay all costs in  
18 connection with the interconnection facilities constructed for the benefit of and to serve PD  
19 Safford, maintenance costs for the MWE portion of the Hackberry Substation and other related  
20 interconnection facilities owned by MWE would have to be borne out of the markup portion of the  
21 energy charge (\$0.000350 per kWh). Staff has recommended that, within 60 days of a decision in  
22 this matter, MWE file with Docket Control an estimate of maintenance costs for MWE-owned  
23 interconnection facilities constructed to serve PD Safford for the first ten years both in dollars and  
24 in dollars per kWh. In addition, Staff has recommended that if maintenance costs for MWE-  
25 owned interconnection facilities constructed to serve PD Safford increase to a level above the  
26 markup portion of the energy charge (\$0.000350 per kWh), MWE negotiate a new electric service  
27 agreement with PD Safford and file an application with the Commission for approval of such  
28 ...

1 revised electric service agreement that would include a sufficient markup to cover then-current and  
2 expected maintenance costs.

3 17. Staff has also recommended that an officer of MWE certify to the Commission in  
4 writing, by docketing a statement no later than 30 days following a Commission Order in this  
5 matter, that it will ensure that all costs to serve PD Safford be borne by PD Safford and not by any  
6 other MWE customers both now and in the future.

7 18. Staff has further recommended that the Commission specify in its Order that  
8 approval of MWE's Agreement with PD Safford at this time does not guarantee any future  
9 ratemaking treatment of the Agreement with PD Safford.

#### 10 CONCLUSIONS OF LAW

11 1. The MWE is certificated to provide electric service as a public service corporation  
12 in the state of Arizona.

13 2. The Commission has jurisdiction over MWE and over the subject matter of the  
14 application.

15 3. The Commission, having reviewed the application and Staff's Memorandum dated  
16 December 5, 2006, concludes that it is in the public interest to approve the proposed Electric  
17 Service Agreement between MWE and PD Safford.

#### 18 ORDER

19 IT IS THEREFORE ORDERED that the proposed Electric Service Agreement between  
20 MWE and PD Safford is hereby approved.

21 IT IS FURTHER ORDERED that, for ratemaking purposes, Phelps Dodge Corporation's  
22 funding of the MWE portion of the interconnection facilities be treated as a contribution-in-aid-of-  
23 construction such that the contribution will offset these assets in MWE's rate base in future MWE  
24 rate proceedings.

25 IT IS FURTHER ORDERED that the MWE-owned interconnection facilities be segregated  
26 in MWE's property accounting records from other MWE assets as a distinct category clearly  
27 identified as related to the PD Safford service area.

28 ...

1           IT IS FURTHER ORDERED that, within 60 days of a decision in this matter, MWE file  
2 with Docket Control as a compliance item in this matter, an estimate of maintenance costs for  
3 MWE-owned interconnection facilities constructed to serve PD Safford for the first ten years both  
4 in dollars and in dollars per kWh.

5           IT IS FURTHER ORDERED that if maintenance costs for MWE-owned interconnection  
6 facilities constructed to serve PD Safford increase to a level above the markup portion of the  
7 energy charge (\$0.000350 per kWh), MWE negotiate a new electric service agreement with PD  
8 Safford and file an application with the Commission for approval of such revised electric service  
9 agreement that would include a sufficient markup to cover then-current and expected maintenance  
10 costs.

11           IT IS FURTHER ORDERED that an officer of MWE certify to the Commission in writing,  
12 by docketing as a compliance item in this matter, a statement no later than 30 days following a  
13 Commission Order in this matter, that it will ensure that all costs to serve PD Safford be borne by  
14 PD Safford and not by any other MWE customers both now and in the future.

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1 IT IS FURTHER ORDERED that approval of MWE's Agreement with PD Safford at this  
2 time does not guarantee any future ratemaking treatment of the Agreement with PD Safford.

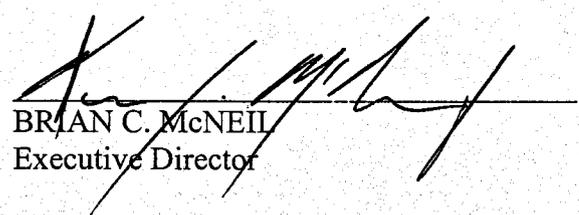
3 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

4 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

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7 CHAIRMAN COMMISSIONER

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9 \_\_\_\_\_  
10 COMMISSIONER COMMISSIONER COMMISSIONER

11 IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive  
12 Director of the Arizona Corporation Commission, have  
13 hereunto, set my hand and caused the official seal of this  
14 Commission to be affixed at the Capitol, in the City of  
15 Phoenix, this 21<sup>st</sup> day of December, 2006.

16   
17 BRIAN C. McNEIL  
18 Executive Director

19 DISSENT: \_\_\_\_\_

20 DISSENT: \_\_\_\_\_

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1 SERVICE LIST FOR: The Morenci Water & Electric Company  
2 DOCKET NO. E-01049A-06-0615

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