

PUBLIC UTILITY COMMISSION OF OREGON  
STAFF REPORT  
PUBLIC MEETING DATE: May 3, 2016

REGULAR \_\_\_\_\_ CONSENT X EFFECTIVE DATE \_\_\_\_\_ N/A \_\_\_\_\_

DATE: April 20, 2016

TO: Public Utility Commission

FROM: Brian Bahr <sup>BB</sup>

THROUGH: Jason Eisdorfer and Marc Hellman <sup>E</sup> <sup>A</sup>

SUBJECT: PACIFICORP: (Docket No. UI 368) Requests Approval of Affiliated Interest Transaction with Marmon Utility, LLC.

**STAFF RECOMMENDATION:**

The Public Utility Commission of Oregon (Commission) should approve PacifiCorp's (Company) application for approval of an affiliated interest Agreement (Agreement) with Marmon Utility, LLC (Marmon), an affiliated interest, subject to the following conditions:

1. PacifiCorp shall notify the Commission of any substantive changes to the Agreement, including any material changes in price or other parameters of the Agreement. Any such changes shall be submitted in an application for a supplemental order (or other appropriate format) in this docket.
2. PacifiCorp shall report to the Commission, as part of its annual affiliated interest report, all transactions entered into with Marmon.

**ISSUE:**

Whether PacifiCorp's request for approval of an Agreement with Marmon, an affiliated interest, should be approved.

**APPLICABLE LAW:**

PacifiCorp filed this application with the Commission on February 8, 2016, pursuant to ORS 757.495(1) and OAR 860-027-0040. PacifiCorp is an indirect, wholly-owned subsidiary of BHE, a subsidiary of Berkshire Hathaway, Inc. (Berkshire Hathaway).

Marmon is also a subsidiary of Berkshire Hathaway, and therefore, an affiliated interest of PacifiCorp.

An "affiliated interest," as defined in ORS 757.015(3), includes every corporation five percent or more of whose voting securities are owned by a corporation or person that also owns, or is part of a successive chain of ownership, five percent or more of the voting securities of a public utility. Berkshire Hathaway's ownership interest in both PacifiCorp and Marmon qualifies Marmon as an affiliated interest of PacifiCorp.

Application requirements for affiliated interest transactions are set forth in OAR 860-027-0040. OAR 860-027-0040(2)(g) requires that the application include the cost incurred and market value of the goods or services being provided.

The Commission reviews affiliated interest transactions to ensure they are fair and reasonable and not contrary to the public interest. ORS 757.495(3). Transactions between affiliated interests must be recorded at the lower of cost or market rate. OAR 860-027-0048(4)(e).

The Commission may waive any Division 27 rule for good cause shown. OAR 860-027-0000(2).

## **DISCUSSION AND ANALYSIS:**

### Background

The Company determined that the reliability of three of its transmission circuits needs to be addressed and improved. The circuits are located in Walla Walla, Washington, and Pendleton and Portland, Oregon. The Company sought to improve reliability of the circuits by "reconductoring" certain sections of the circuit with a spacer cable system. The only company currently manufacturing the spacer cable system required by the transmission circuits is Marmon, which is an affiliated interest of PacifiCorp.

### Analysis

Staff's review included examination of the Company's current application, including purchase orders for the cables, and responses from the Company to 15 Staff information requests. Staff investigated the following issues:

1. Terms and Conditions of the Agreement;
2. Transfer Pricing;
3. Public Interest Compliance; and
4. Records Availability, Audit Provisions, and Reporting Requirements.

*Terms and Conditions of the Agreement*

The purchase orders, included as Attachment A of the Company's application, include standard terms and conditions. According to the Company, the purchase orders were prepared in accordance with PacifiCorp's procurement policies and procedures and contain standard commercial terms and conditions to protect the Company's ability to provide safe and reliable service. Staff reviewed the purchase order for each of the three cable spacer systems and did not identify any unexpected or unusual terms or conditions.

*Transfer Pricing*

According to the purchase orders included in the Company's application, the purchase price of the spacer cable systems for the three locations, including installation materials and job support, is as follows:

<b>Location</b>	<b>Price</b>
Pendleton, OR	\$16,444
Walla Walla, WA	\$21,109
Portland, OR	\$49,568
<b>TOTAL</b>	<b>\$87,121</b>

The actual installation of the spacer cable systems is not included in the purchase from Marmon. Rather, installation will be performed by the Company at the following costs, which include labor and overhead:

<b>Location</b>	<b>Price</b>
Pendleton, OR	\$52,036
Walla Walla, WA	\$29,891
Portland, OR	\$99,931
<b>TOTAL</b>	<b>\$181,858</b>

The Company does not have any intercompany service agreement with Marmon; therefore, the Agreement is priced at Marmon's standard rates. Staff researched other companies providing similar systems and only found one, Southwire. In response to a request for information from Staff, the Company explained why Marmon was a more appropriate option than Southwire:

*PacifiCorp is aware of only one vendor that provides both materials and engineering of spacer cable systems- Hendrix, a subsidiary of Marmon Wire and Cable Company. Another vendor, Southwire Company, only manufactures the cable; for supply attachment hardware they use Hendrix hardware to augment their cable*

*application...Due to PacifiCorp's limited design experience with this technology, the Company looks at partnering with a provider that can provide a total package, from design to installation. PacifiCorp can mitigate long term support challenges in the event of a failure by choosing a provider that manufactures the total product solution and provides design-to-installation support.*

OAR 860-027-0048(4)(e) requires that the utility record the transaction at the lower of the affiliate's cost or market rate. In this particular transaction, Staff was unable to establish a market rate due to the limited number of companies providing similar goods and services. However, because Marmon is a competitive business, Staff can assume that Marmon's standard prices reasonably represent market rates. Additionally, the cost to Marmon of providing the cable spacer systems is not available to either the Company or Staff.

Given the lack of alternative options available to the Company and the fact that the transaction is significantly less than 0.1 percent of the Company's annual Oregon revenues and will have minimal impact on customers, Staff recommends a waiver, pursuant to OAR 860-027-0000(2), of the requirement that PacifiCorp record the transaction at the lower of the affiliate's cost or market rate.

#### *Public Interest*

The Commission customarily applies a "no harm" standard in determining what is "not contrary to the public interest" in matters involving affiliated interest transactions. See, e.g., *In the Matter of a Legal Standard for Approval of Mergers*, Commission Order No. 01-778 at 10 (Sept. 4, 2001). The impetus for the purchase of the cable spacer systems is repeated outages of the aforementioned circuits. According to the Company in a response to a request for information from Staff:

*Circuit 5W202 in Pendleton experienced seven sustained outages over the last five years, circuit 5W150 in Walla Walla sustained three outages over the last five years, and circuit 5P23 in Portland experienced three momentary interruptions within the last six months.*

In addition,

*The Company assesses historic outages for any given project. In the instances in Walla Walla and Pendleton, the historical outage causes have frequently been animal contact. The Company evaluated alternatives to reduce these types of outages, which*

*included “undergrounding” and “re-conductoring.” The cost of undergrounding wires exceeds the cost of overhead construction, and with the area’s habitat and river environment, was expected to be even more costly. Re-conductoring, on the other hand, uses spacer cable and was seen as a more effective environmental and economic solution.*

Specifically referring to the Portland location, the Company provided the following response:

*In Portland, the environmental exposures include both animals and deciduous trees. Review with vegetation management personnel and environmental staff indicated that substantial resilience against fault events could not be achieved without using either underground or spacer cable construction. Recent experience in Tulelake has demonstrated that spacer cable significantly enhanced the circuit’s resilience against animal contact (in an approximately six mile section adjacent to a wildlife sanctuary) and was much less costly than underground construction.*

As noted above, in response to a request for information from Staff, the Company stated that the 5P23 circuit in Portland had experienced three momentary interruptions over the past six months. However, when asked to compare the outage rate of the three circuits to the Company’s overall outage rate in terms of impact on customers, the Company responded with regard to the 5P23 Portland circuit “New circuit as of 2015; no statistics.” As such, Staff is not convinced the reconductoring of the 5P23 circuit in Portland was a prudent decision by the Company at this time.

The case for the other two circuits, 5W202 in Pendleton and 5W150 in Walla Walla, appears more robust than that for the 5P23 circuit in Portland. Nevertheless, Staff recommends that the prudence of the reconductoring of all three circuits be examined in detail in the Company’s next general rate filing. At this time, the Commission need not determine the reasonableness of all the financial aspects of the contract for ratemaking purposes.

#### *Records Availability, Audit Provisions, and Reporting Requirements*

Staff notes that the Commission retains the ability to review all affiliated transactions of the Company through both its annual affiliated interest report and in general rate case filings. Staff’s recommended conditions provide for all necessary Commission examination of PacifiCorp’s records concerning the Agreements.

Conclusion

The Company has reviewed this memo and has not communicated any objections or concerns. Based on the review of this application, Staff concludes:

1. The purchase orders do not appear to contain any unexpected or unusual terms or conditions;
2. The transfer pricing is fair and reasonable;
3. The Agreement is not contrary to the public interest and,
4. Necessary records are available.

**PROPOSED COMMISSION MOTION:**

Approve PacifiCorp's application for approval of an affiliated interest transaction with Marmon, subject to Staff's recommended conditions.