

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: November 22, 2016

REGULAR _____ CONSENT X EFFECTIVE DATE _____ N/A _____

DATE: November 08, 2016

TO: Public Utility Commission

FROM: Kathy Zarate *KZ*

THROUGH: *JF* Jason Eisdorfer and *MA* Marc Hellman

SUBJECT: PACIFICORP: (Docket No. UI 380) Requests Approval of an Affiliate Interest Transaction with International Business Machines Corporation.

STAFF RECOMMENDATION:

The Public Utility Commission of Oregon (Commission) should approve PacifiCorp's (PacifiCorp or Company) application for approval of an Affiliate Interest Transaction with International Business Machines Corporation (IBM), an affiliated interest, subject to the following conditions:

1. PacifiCorp shall notify the Commission of any substantive changes to the agreements, including any material changes in price or other parameters. 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 under the agreements with IBM.
3. The Commission reserves judgment on the fairness and reasonableness of the agreements for ratemaking purposes.

DISCUSSION:

Issue

Whether the Commission should allow PacifiCorp to enter into an Enterprise Software and Support Option (ESSO) agreement with IBM, an affiliated interest, in order to purchase products and services from IBM, and a related Transaction Finance

Agreement (TFA), under which PacifiCorp will remit payments for the IBM products and service under the ESSO.

Applicable Law

PacifiCorp and IBM qualify as an affiliated interest. ORS 757.495 requires a public utility seek approval of contracts with affiliated interests within 90 days of execution of the contract. The required process for submitting an agreement for review by the Commission is set forth in ORS 757.015(2) and OAR 860-027-0040.

ORS 757.495(3) provides that the Commission may approve an affiliated interest agreement if the agreement is fair and reasonable and not contrary to the public interest. Under OAR 860-027-0048(4)(g), for cost allocation purposes, “when services or supplies are sold to an energy utility by an affiliate under contract, the transfer price shall be based upon the tariff or terms of the contract approved by the Commission under ORS 757.495.”

Pursuant to OAR 860-027-0000(2), the Commission may waive division 27 rule requirements for good cause shown.

The Commission need not determine the reasonableness of all financial aspects of the contract for ratemaking purposes, but rather reserves that issue for subsequent ratemaking proceedings. See *In re Avista Corp.*, OPUC Docket No. UI 306, Order No. 11-071 (Mar. 2, 2011).

Discussion and Analysis

PacifiCorp submitted this filing on September 28, 2016, as PacifiCorp is an indirect, wholly-owned subsidiary of Berkshire Hathaway Energy Company (BHE). BHE is a subsidiary of Berkshire Hathaway, Inc (Berkshire Hathaway). Berkshire Hathaway holds over five percent of IBM common stock. Berkshire Hathaway’s ownership interest in both PacifiCorp and IBM constitutes an affiliated interest.

The Company uses IBM technologies to support many of its key business functions. Specific examples of services PacifiCorp procures from IBM are support for customer service and billing, support for enterprise reporting and analytics in the Enterprise Data Warehouse, support for Corporate Enterprise Content Management for document storage, archiving and retrieval, and support for optimization of energy trading activities. The software IBM provides is proprietary and not available from other software providers.

PacifiCorp seeks with this application approval of an ESSO Agreement with IBM, which allows the Company to bundle certain software licensing purchases and support

services to achieve savings over the term of the contract. PacifiCorp anticipates saving approximately \$1,500,000 on a total-company basis over the term of the contract. PacifiCorp is also seeking approval of a related Transaction Finance Agreement (TFA) under which PacifiCorp will pay for IBM products and services purchased pursuant to the ESSO.

Staff's review of this application included examination of the Company's current ESSO, as well as PacifiCorp's prior agreements with IBM, including the related Commission Orders approving the agreements.¹ Staff also reviewed the Company's responses to the six Staff data requests issued in this filing.

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

Staff reviewed the confidential ESSO Agreement and TFA, and did not find any terms or conditions that would be unexpected or unusual. The ESSO Agreement includes only products and services provided by IBM to the Company that have been approved by the Commission in prior affiliated interest dockets.

Transfer Pricing

Because the products and services supplied by IBM are proprietary, the Company is unable to engage in a competitive bidding process. Without the software furnished by IBM, the Company would not be able to perform critical business functions. Procurement and installation of different reporting systems would require considerable time and expense. Through the Agreement, PacifiCorp will pay a lower price than it currently pays for services and products from IBM that have been previously approved by the Commission. PacifiCorp projects annual total company savings of approximately \$500,000.

PacifiCorp utilized its "sole source purchasing process" when negotiating the agreements between itself and IBM. The Company clarified in a data response that its "procurement policy allows for certain exceptions to the competitive solicitation process" when it would be "impossible, impractical, or otherwise...in the best interest of PacifiCorp and customers" for a supplier to be awarded a contract on a non-competitive

¹ See Order No. 12-227, Order No. 12-228, and Order No. 12-385 for examples of various recent affiliated interest agreements between PacifiCorp and IBM that have been approved by the Commission.

basis. PacifiCorp's policy requires all non-competitive procurements of \$20,000 or greater to be documented with a non-competitive procurement justification form and be approved by appropriate levels of management depending on the total value of the procurement.

Accordingly, Staff finds the pricing to be fair and reasonable, as the price are lower than those previously approved by the Commission.

Public Interest Compliance

The ESSO Agreement and corresponding TFA allow PacifiCorp to save money on its software and service expenses purchased from IBM. These cost reductions will be passed on to ratepayers in future general rate cases.

Staff finds the ESSO Agreement and corresponding TFA to be consistent with the public interest (customarily a no harm standard applied by the Commission) as customers will benefit from lower prices for necessary products and services.

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 ratemaking proceedings. Staff's recommended conditions above provide for Commission examination of PacifiCorp's records concerning the agreement as may be necessary.

Conclusion

Based on the review of this application, Staff concludes:

1. The application regards an affiliated interest agreement that is fair and reasonable and not contrary to the public interest with inclusion of the proposed ordering conditions; and
2. Necessary records are available.

PacifiCorp has reviewed this memo and has no objections or concerns.

PROPOSED COMMISSION MOTION:

Approve PacifiCorp's application for approval of the ESSO TFA agreements with IBM, an affiliated interest, subject to Staff's recommended conditions.