

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: July 24, 2007**

REGULAR CONSENT EFFECTIVE DATE NA

DATE: June 18, 2007

TO: Public Utility Commission

FROM: Michael Dougherty

THROUGH: Lee Sparling and Marc Hellman

SUBJECT: PACIFICORP: (Docket No. UI 269) Application Requesting Approval of Rail Transportation Agreements with Burlington Northern Santa Fe Railway Company, an Affiliated Interest.

STAFF RECOMMENDATION:

The Commission should approve PacifiCorp's (PacifiCorp or Company) application concerning transportation agreements with Burlington Northern Santa Fe Railway Company (BNSF), subject to the following conditions:

1. The Company shall provide the Commission access to all books of account, as well as all documents, data, and records that pertain to any transactions with BNSF.
2. The Commission reserves the right to review, for reasonableness, all financial aspects of this transaction in any rate proceeding or alternative form of regulation.
3. PacifiCorp shall notify the Commission in advance of any substantive changes to the contract, including any material change in price. Any such change shall be submitted in an application for a supplemental order (or other appropriate format) in this docket.

DISCUSSION:

PacifiCorp filed this application on June 5, 2007, pursuant to ORS 757.495 and OAR 860-027-0040. PacifiCorp is a wholly owned subsidiary of MEHC¹ and as such, is an indirect subsidiary of Berkshire Hathaway Inc (Berkshire). Berkshire owns a 10.9 percent interest in BNSF. Therefore, PacifiCorp's relationship with BNSF establishes an affiliated interest, as defined in ORS 757.015(3).

PacifiCorp requests approval for Rail Transportation Agreements (Agreements) entered into between PacifiCorp and BNSF to provide transportation services from:

1. Various coal mines in the Wyoming Powder River Basin to PacifiCorp's David Johnston Steam Plant (David Johnston); and
2. Various coal mines in Wyoming, New Mexico, and Montana to PacifiCorp's Cholla Generating Station (Cholla).

Pursuant to OAR 860-027-0040(3)(b), this type of service provided pursuant to a contract filed and approved by the Surface Transportation Board (STB)² would generally not require Commission approval; however, PacifiCorp and MEHC agreed to a different affiliate transaction standard as part of PacifiCorp's acquisition by MEHC. In Commission Order No. 06-121 (UM 1209) granting approval of the acquisition of PacifiCorp by MEHC, the Commission adopted Commitment No. O3, which provides as follows:

“MEHC and PacifiCorp commit that they will interpret Oregon Revised Statutes Sections 757.015 and 757.495 to require Commission approval of any contract between PacifiCorp and (i) any affiliate of MEHC or (ii) any affiliate of Berkshire Hathaway. This shall include the IASA. MEHC and PacifiCorp intend that by obtaining Commission approval of the IASA, PacifiCorp will avoid the need to seek individual approval of affiliate transactions which are subject to that agreement. The IASA is expected to address the provision

¹ PPW Holdings LLC is wholly owned by MEHC. PPW Holdings LLC, in turn, owns 100 percent of the common stock of PacifiCorp, which represents 99.76 percent of the voting securities of PacifiCorp.

² The Surface Transportation Board (STB) was created in the Interstate Commerce Commission Termination Act of 1995 and is the successor agency to the Interstate Commerce Commission. The STB is an economic regulatory agency that Congress charged with the fundamental missions of resolving railroad rate and service disputes and reviewing proposed railroad mergers. The STB is decisionally independent, although it is administratively affiliated with the Department of Transportation. (www.stb.dot.gov)

of electric service to affiliates of MEHC or Berkshire Hathaway under tariff approved by state or federal authorities.”

As a result, PacifiCorp submitted this affiliated interest application consistent with Oregon Commitment O3.

Because these Agreements existed prior to MEHC's acquisition of PacifiCorp and prior to Berkshire's acquisition of 10.9 percent share of BNSF, PacifiCorp requests that the Commission approve the Agreements as affiliated interest agreements and allow PacifiCorp to continue purchasing services pursuant to the Agreements.

PacifiCorp estimates that it will pay approximately \$30 million per year for service under the Agreements with BNSF. PacifiCorp will record most of the charges related to the BNSF agreements in FERC Account 501, Fuel.

Issues

Staff investigated the following issues:

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

Terms and Conditions of the Agreements

Staff did not observe any unusual terms and conditions of the Agreements. The transportation service is offered pursuant to terms and conditions of the contracts that have been approved by the STB. Through these Agreements, BNSF provides rail transportation services.

Under Agreement BNSF-C-12123, BNSF transports coal obtained from eighteen mines in the Wyoming Powder River Basin to David Johnston near Glenrock, Wyoming. Under the agreement, BNSF transports a minimum of 3.5 million tons of coal per year for PacifiCorp. PacifiCorp manages the volume of coal per car and train as well as the origin of the coal shipments.

PacifiCorp also manages the unloading of the cars at the destination. BNSF sends empty trains with separated cars to the mines, loads the separated cars with coal, and then transports the coal across BNSF routes to David Johnston. PacifiCorp entered into BNSF-C-12123 with BNSF on January 26, 1998, to be effective until December 31, 2013, pursuant to 49 U.S.C. Section 10709. Under this section, railroads may enter into

railroad service contracts at terms and conditions specified in the contract, which are then approved by the STB.

Agreement BNSF-C-12470 governs transportation services for coal obtained from twenty mines located in Wyoming, New Mexico, and Montana, and delivered to Unit Four of Cholla Generation Plant near Joseph City, Arizona.

Similar to the agreement for David Johnston, BNSF transports a minimum of 3.8 million tons of coal per year for PacifiCorp. PacifiCorp manages the volume of coal per car and train as well as the origin of the coal shipments. PacifiCorp also manages the unloading of the cars at the destination. BNSF sends empty trains with separated cars to the mines, loads the separated cars with coal, and then transports the coal across BNSF routes to Cholla.

PacifiCorp entered into BNSF-C-12470 with BNSF and the Arizona Public Service Company on January 10, 2006, to be effective until December 31, 2017, pursuant to 49 U.S.C. Section 10709.

Transfer Pricing

As previously mentioned, PacifiCorp is procuring the transportation services at terms and conditions specified in the contract, which are approved by the STB. Pursuant to OAR 860-027-0048(4)(e), Allocation of Costs by an Energy Utility:

“When services or supplies (except for generation) are sold to an energy utility by an affiliate, sales shall be recorded in the energy utility's accounts at the approved rate if an applicable rate is on file with the Commission or with FERC.”

The Agreements set base rates per ton for coal transportation. These rates are adjusted quarterly based on changes to the All-Inclusive Index Less Fuel with Forecast Error Adjustment factor set by the Association of American Railroads. The Agreements also set minimum and maximum charges.

Although the above rule specifically mentions the Commission and FERC, Staff believes the Agreements' pricing meets the Commission's transfer pricing standard since the applicable rates are on file with STB, which is an economic regulatory agency.

Public Interest Compliance

PacifiCorp owns and operates many generation facilities, some of them fueled by coal. Coal-fired generation may be located near mine heads or may be located far away from a coal source. According to PacifiCorp, in situations where coal must travel a great

distance to reach the generation plant, railroad transportation service is less expensive than other potential transportation sources such as semi-truck hauling.

Additionally, rail service providers are somewhat analogous to public utilities in that they usually serve exclusive service territories with rates governed by the STB. While BNSF is not the only rail service company that could provide service to some of the mines, BNSF is the only rail service company that can provide transportation services to both David Johnston and Cholla.

These Agreements, which were originally negotiated as third-party agreements, serve the public interest by ensuring PacifiCorp obtains supplies for its coal-fired base load generation plants at rates overseen by a federal government agency.

Records Availability, Audit Provisions and Reporting Requirements

Order Condition Number 1, listed above in the Staff recommendation; affords the necessary Commission examination of PacifiCorp's records concerning this application.

Based on the review of this application, Staff concludes the following:

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

PacifiCorp has reviewed Staff's recommendation and does not object to the recommendation.

PROPOSED COMMISSION MOTION:

PacifiCorp's application for approval of the transportation agreements with BNSF, be approved subject to the three recommended conditions.