

ITEM NO. CA1

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: May 19, 2009**

REGULAR _____ CONSENT X EFFECTIVE DATE _____ N/A _____

DATE: April 28, 2009

TO: Public Utility Commission

FROM: Dustin Ball

THROUGH: Lee Sparling, Marc Hellman, and Michael Dougherty

SUBJECT: PACIFICORP: (Docket No. UI 284) Application of PacifiCorp Requesting Approval of Affiliated Interest Agreements with Constellation Energy Group.

STAFF RECOMMENDATION:

The Commission should approve PacifiCorp's (PacifiCorp or Company) application for approval of affiliated interest agreements with Constellation Energy Group (Constellation), an affiliated interest, and request for a waiver of filing requirements contained in OAR 860-027-0040, subject to the following conditions:

1. PacifiCorp shall provide the Commission access to all books of account, as well as all documents, data, and records that pertain to any transactions involving Constellation.
2. The Commission reserves the right to review, for reasonableness, all financial aspects of these transactions in any rate proceedings or alternative form of regulation.
3. PacifiCorp shall notify the Commission in advance of any substantive changes to the contracts, including any material change in price. Any such changes shall be submitted in an application for a supplemental order (or other appropriate format) in this docket.
4. PacifiCorp shall report to the Commission, as part of its annual affiliated interest report, all transactions entered into under the affiliated interest agreements with Constellation.

DISCUSSION:

PacifiCorp filed this application on March 17, 2009, pursuant to ORS 757.495(1), OAR 860-027-0040, and OAR 860-027-0043. PacifiCorp is an indirect wholly-owned subsidiary of MidAmerican Energy Holding Company (MEHC). MEHC currently holds 14.9 million shares (an approximate 7.45 percent interest) of Constellation Energy Group common stock, which in turn owns Constellation Energy Commodities, Inc. (collectively referred to as Constellation). Therefore, PacifiCorp and Constellation are affiliated interests pursuant to ORS 757.015.

PacifiCorp requests approval of its International Swap Dealers Association Master Agreement and Amendment Number One to the International Swap Dealers Association Master Agreement (collectively referred to as "ISDA") with Constellation. Additionally, PacifiCorp seeks a waiver of the filing requirements contained in OAR 860-027-0040.

PacifiCorp and Constellation entered into the ISDA with an effective date of December 13, 2001. Amendment Number one to the ISDA was effective July 5, 2007, and replaced a Master Power Purchase and Sale Agreement, which had been in place since September 10, 2001.

PacifiCorp's relationship with MEHC was established when it was acquired by MEHC on March 21, 2006. Constellation's relationship with MEHC was established on December 17, 2008, when MEHC acquired a substantial common stock position in Constellation as part of a termination of an acquisition agreement. All terms of the ISDA agreements were executed prior to the establishment of an affiliated interest between PacifiCorp and Constellation. With this application, PacifiCorp requests Commission authorization to continue to engage in business transactions with Constellation under the terms of the ISDA.

The ISDA governs a wide variety of financial transactions including, among other things, swaps and options; it also includes transactions in physical energy pursuant to the terms of a Power Annex. Before opting to transact with Constellation under the ISDA, the Company first seeks bids or otherwise reviews the applicable market to determine whether the Constellation price and product is desirable. Power transactions, entered into under the ISDA, are priced at market-based rates filed with the Federal Energy Regulatory Commission (FERC). Additionally, PacifiCorp includes transactions under the ISDA in its Electric Quarterly Report filed with FERC.

In addition to transactions subject to FERC-approved tariffs, PacifiCorp also purchases other products, such as renewable energy credits and daily call options, which are not subject to FERC-approved tariffs. During 2008, PacifiCorp purchased 50,000

renewable energy credits from Constellation for the vintage period July-December 2007 at \$6.00 per REC. This purchase was to supply the Company's Blue Sky voluntary program and the purchase was priced at market, which was lower than the voluntary program cost.

According to PacifiCorp, filing for approval of individual transactions under the ISDA would be cumbersome and inefficient. During 2008, PacifiCorp and Constellation conducted approximately 1,800 power transactions under the ISDA. Many of these transactions were entered into within short timeframes, often day-ahead or spot purchases. PacifiCorp is requesting a waiver of filing for approval for individual transactions based on their claim that such a requirement may place the Company at a competitive disadvantage in procuring physical and financial energy products. Additionally, to ensure adequate review of transactions entered into under the terms of the ISDA, the Company proposes to report these transactions in its annual affiliated interest report with the Commission.

Pursuant to OAR 860-027-0040(3)(b) services provided pursuant to a filed and approved FERC rate schedule would generally not require Commission approval; however, PacifiCorp and MEHC agreed to a different affiliated 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 Section 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 affiliated transactions which are subject to that agreement. The IASA is expected to address the provision of electric service 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.

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 Agreement

Staff did not observe any unusual terms and conditions of the Agreement. The Agreement itself does not obligate either party to transact. However, the ISDA operates as a master agreement that generally allows the Company and Constellation to conduct business with each other if so chosen. The ISDA governs numerous terms of the transactions between the parties, such as payments, obligations, terminations, thresholds, taxes, etc. The ISDA represents a management tool and serves as a “safe harbor,” which is subject to certain exemptions from bankruptcy provisions.

The terms and conditions of the Agreement do not appear to be contrary to the public interest.

Transfer Pricing

As previously mentioned, power transactions pursuant to the ISDA are priced at market-based FERC approved tariffs, while other products such as renewable energy credits and daily call options are priced at market rates.

Pursuant to OAR 860-027-0048(4)(f), allocation of costs by an Energy Utility:

“For generation, when services or supplies are sold to an energy utility by an affiliate, sales shall be recorded in regulated accounts at the market rate.”

Because the applicable rates are priced at market-based FERC-approved tariffs, or in the case of renewable energy credits and call options at the market rate, the Agreement’s pricing for power transactions meet the Commission fair pricing standard.

Public Interest Compliance

The power transactions which are entered into under the ISDA are federally regulated pursuant to terms and conditions approved by FERC. Additionally, prior to opting to transact with Constellation under the ISDA in any particular instance, PacifiCorp first seeks bids or otherwise reviews the applicable markets to determine whether the Constellation price and product is desirable.

Staff finds that the terms and conditions to the contract appear to be just and reasonable.

Records Availability, Audit Provisions, and Reporting Requirements

Order Conditions Number 1 and Number 4, listed above in the Staff Recommendations, afford the necessary Commission examination of PacifiCorp's records concerning the ISDA Agreements.

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 proposed ordering conditions.
2. Necessary records are available.

PROPOSED COMMISSION MOTION:

PacifiCorp's application for approval of affiliated interest agreements with Constellation Energy Group be approved subject to the four recommended conditions.