

108 FERC ¶ 61,004
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

Oklahoma Gas and Electric Company
NRG McClain LLC

Docket No. EC03-131-000

ORDER APPROVING CONTESTED SETTLEMENT OFFER,
SUBJECT TO THE COMMISSION'S MODIFICATIONS, AND AUTHORIZING
ACQUISITION AND DISPOSITION OF JURISDICTIONAL FACILITIES

(Issued July 2, 2004)

1. On August 26, 2003, Oklahoma Gas and Electric Company (OG&E) and NRG McClain LLC (NRG McClain) (collectively, OG&E) filed a joint application under section 203 of the Federal Power Act (FPA)¹ requesting that the Commission authorize the sale of certain jurisdictional facilities by NRG McClain to OG&E (the Transaction). In a December 18, 2003 Order,² the Commission found that the Transaction, without appropriate mitigation measures, would harm competition.³ Therefore, the Commission set the application for hearing in order to determine what mitigation measures should be imposed as conditions if the Commission were to approve the Transaction.

2. On May 10, 2004, the Motions Commissioner referred to the full Commission OG&E's motion for interlocutory appeal in which OG&E asked that its Offer of Settlement be certified to the full Commission and that the settlement be approved by the Commission. The OG&E Offer of Settlement, as revised below, is a reasonable resolution of this proceeding and therefore is approved. The settlement, as modified herein, puts in place sufficient mitigation measures that alleviate the market power effects

¹ 16 U.S.C. § 824b (2000).

² Oklahoma Gas and Electric Company and NRG McClain LLC, 105 FERC ¶ 61,297 (2004) (December 18 Order).

³ Id.

of the Transaction and therefore resolve the issues set for hearing in the December 18 Order. Accordingly, the Commission approves the Transaction as being consistent with the public interest.

3. This order benefits customers by ensuring that the Transaction will not adversely affect rates or competition in the marketplace.

I. Background

A. The Filing & December 18 Order

4. NRG McClain is a wholly-owned public utility subsidiary of NRG Energy, Inc, which, in turn, is wholly owned by Xcel Energy Inc. NRG McClain filed for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code on August 19, 2003. It has a 77 percent undivided interest in a 520 megawatt(MW) gas-fired combined-cycle electric plant in Oklahoma (McClain Facility).⁴

5. OG&E and NRG McClain have agreed that OG&E will acquire NRG McClain's interest in the McClain Facility, including associated jurisdictional transmission facilities.⁵ The Transaction enables OG&E to satisfy its native load service obligations and to fulfill its commitment under an Oklahoma Corporation Commission (OCC) settlement order (OCC Settlement Order) to acquire electric generating capacity of not less than 400 MW and to integrate that capacity into OG&E's generation system. OG&E states that the Transaction will enable OG&E to pass through fuel cost savings to customers taking service under retail and wholesale tariffs and rate schedules. Upon closing of the Transaction, OG&E will assume operating responsibility for the McClain Facility.

6. OG&E then filed this application. It noted that under the OCC Settlement Order, if OG&E is unable to acquire the generation by December 31, 2003, OG&E must credit \$25 million annually to its Oklahoma retail customers (at a rate of 1/12 of \$25 million per

⁴ Oklahoma Municipal Power Authority (OMPA), a wholesale customer of OG&E, owns the remaining 23 percent undivided interest. NRG McClain currently operates the McClain Facility.

⁵ OG&E and OMPA executed a Transmission Operation and Maintenance Agreement under which OG&E will maintain these transmission facilities, OMPA will continue to have the right to dispatch its share of the McClain Facility, and OMPA will have input on the scheduling of outages.

month for each month that the facility is not in place for the period from January 1, 2004 through December 31, 2006).

7. In the December 18 Order, the Commission reviewed OG&E's application under the Merger Policy Statement⁶ and found, as discussed further below, that the Transaction (without further mitigation) could harm competition in OG&E's market due to increases in OG&E's horizontal and vertical market power⁷ and thus was not consistent with the public interest. The Commission further stated that there was insufficient evidence in the record for the Commission to determine the mitigation measures it should impose as conditions if, and when, the Commission decided to approve the Transaction. Accordingly, the Commission set the application for hearing in order to address those issues and to develop a more complete record on which to make such a determination. In the December 18 Order, the Commission also found that the Transaction, if properly conditioned, would not harm wholesale electricity rates and that the Transaction will not affect state or federal regulation.

8. OG&E then filed a request for expedited reconsideration and/or rehearing and clarification of the December 18 Order.⁸ In the same pleading, OG&E filed an offer of

⁶ Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement, Order No. 592, 61 Fed. Reg. 68,595 (1996), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,044 (1996), reconsideration denied, Order No. 592-A, 62 Fed. Reg. 33,341 (1997), 79 FERC ¶ 61,321 (1997) (Merger Policy Statement); see also Revised Filing Requirements Under Part 33 of the Commission's Regulations, Order No. 642, 65 Fed. Reg. 70,983 (2000), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,111 (2000) (Order No. 642), order on reh'g, Order No. 642-A, 66 Fed. Reg. 16,121 (2001), 94 FERC ¶ 61,289 (2001). The Merger Policy Statement and Order No. 642 provide that the Commission will generally take account of three factors in its section 203 analysis: (1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation.

⁷ Horizontal market power is exercised when in order to increase profits, a firm drives up prices through its control of a single activity, such as electricity generation, and it controls a significant share of the total capacity available in that market. Vertical market power is exercised when a firm involved in two related activities, such as electricity generation and transmission, uses its dominance in one area to raise prices and increase profits for the overall enterprise.

⁸ See "OG&E" Request for Rehearing, Docket No. EC03-131-000 (2004) (January 20 Rehearing Request).

additional mitigation in order to allow prompt Commission approval of the Transaction (by obviating the need for the Commission to act on the merits of the rehearing requests).⁹

B. The Interlocutory Appeals

9. The procedural background resulting in these interlocutory appeals is as follows: On March 8, 2004, OG&E filed its unilateral Offer of Settlement, which is discussed below, to resolve the mitigation issue set for hearing in the December 18 Order. InterGen Services, Inc. and Redbud Energy LP (collectively, InterGen) filed comments opposing the OG&E Offer of Settlement and filed its own unilateral Offer of Settlement, which is also discussed below.

10. On April 12, 2004, the presiding administrative law judge (Presiding Judge) rejected the OG&E Offer of Settlement and, consequently, did not certify it to the Commission.¹⁰ On April 26, 2004, the Presiding Judge granted a motion by OG&E for reconsideration of the April 12 Order but again declined to certify the OG&E Settlement Offer to the Commission and denied OG&E's motion to seek interlocutory appeal.

11. Similarly, on April 30, 2004, the Presiding Judge rejected the InterGen Offer of Settlement.¹¹ OG&E filed with the Chairman, as Motions Commissioner, an interlocutory appeal of the April 12 Order, asking that the OG&E Offer of Settlement be certified to the Commission and that the Commission approve that settlement. On May 10, 2004, the Motions Commissioner referred to the full Commission OG&E's motion for interlocutory appeal.

12. On May 11, 2004, the Presiding Judge granted a motion by InterGen for reconsideration of the April 30 Order but declined to certify the InterGen Settlement Offer to the Commission and denied InterGen's motion to seek interlocutory appeal.

⁹ The Commission has not yet acted on the January 20 Rehearing Requests or OG&E's offer of additional mitigation that was contained in that filing. Those requests will become moot if OG&E accepts the revisions to its Offer of Settlement required by this order.

¹⁰ Oklahoma Gas and Electric Company and NRG McClain LLC, 107 FERC ¶ 63,009 (2004) (April 12 Order).

¹¹ Oklahoma Gas and Electric Company and NRG McClain LLC, 107 FERC ¶ 63,023 (2004) (April 30 Order).

InterGen filed with the Motions Commissioner an interlocutory appeal of the April 30 Order, asking that the InterGen Offer of Settlement also be certified to the full Commission and that the Commission approve that settlement. On May 18, 2004, the Motions Commissioner referred to the full Commission InterGen's motion for interlocutory appeal.

13. On May 21, 2004, AES Shady Point, LLC (AES) filed its unilateral Offer of Settlement, which is discussed below. On June 15, 2004, the Presiding Judge rejected the AES Offer of Settlement.¹² AES filed with the Chairman, as Motions Commissioner, an interlocutory appeal of the June 15 Order, asking that the AES Offer of Settlement be certified to the Commission and that the Commission approve that settlement. On June 24, 2004, the Motions Commissioner referred to the full Commission AES' motion for interlocutory appeal.

C. OG&E Offer of Settlement

14. OG&E states that its Offer of Settlement is intended to resolve the issues set for hearing in the December 18 Order (ensuring that the Transaction will not harm or undermine competition). It offers the following permanent and interim mitigation to address the adverse effect on competition that could result from the Transaction: First, as a permanent mitigation measure, OG&E states that it will construct a 600 MW "bridge" (600 MW Bridge) between InterGen's Redbud Energy Project (Redbud Facility)¹³ and OG&E's control area.¹⁴ InterGen's Redbud Facility is eligible to obtain that additional available transmission capacity (ATC), as well as other potential suppliers, under the Open Access Transmission Tariff (OATT).¹⁵ Second, as a permanent mitigation

¹² Oklahoma Gas and Electric Company and NRG McClain LLC, 107 FERC ¶ 63,047 (2004) (June 15 Order).

¹³ The Redbud Facility is a 1,200 MW combined cycle generating facility located in Luther, Oklahoma.

¹⁴ According to OG&E, the 600 MW Bridge will consist primarily of an upgrade to OG&E's Draper Substation. OG&E states that it will begin construction of the 600 MW Bridge as soon as the Commission approves the Transaction. It estimates that the 600 MW Bridge can be completed within eleven months.

¹⁵ OG&E explains that its offer to upgrade its system to create 600 MW of ATC does not mean that InterGen (or any other supplier) is guaranteed 600 MW of ATC or that InterGen will have guaranteed firm transmission service under the OATT to sell to customers, because those wholesale customers and any wholesale seller that sells power

measure, OG&E will construct a transmission upgrade at OG&E's Ft. Smith interconnection with Entergy Corporation's transmission system. Third, as an interim mitigation measure, during the period between the Commission's approval of the Transaction and the completion of the 600 MW Bridge, OG&E will redispatch (at no cost to InterGen) OG&E's generating units to enable the Redbud Facility to sell power (not to exceed 600 MW in the aggregate and subject to reliability constraints) to any wholesale customer in the OG&E control area that InterGen obtains during that period. Fourth, as an interim mitigation measure, OG&E states that it will establish an independent market monitor to address vertical market power concerns until the Southwest Power Pool (SPP) Regional Transmission Organization (RTO) is calculating and posting ATC, as OG&E proposed in its January 20 Rehearing Request. OG&E states that its proposal for an independent market monitor will be expanded (from its proposal in its January 20 Rehearing Request) to provide that that monitor will oversee OG&E's calculation of ATC and total transmission capacity (TTC) and will provide that data to the SPP RTO.¹⁶

D. InterGen Offer of Settlement

15. InterGen states that its Offer of Settlement would better resolve the issues set for hearing in the December 18 Order than would the OG&E Offer of Settlement. InterGen states that OG&E cannot mitigate its increased horizontal market power by simply providing an amount of transmission capacity equal to its 400 MW acquisition of the McClain Facility. According to InterGen, as market concentration increases, the anticompetitive consequences of the Transaction increase even more. In particular, using the Herfindahl-Hirschman Index (HHI) (which is a standard measure of market concentration) as a guide for defining the appropriate level of mitigation, InterGen states that more than 1,200 MW of generation is required to bring the HHI to pre-Transaction levels.

16. InterGen also states that the 1,200 MW needed to mitigate OG&E's increased market power must be more than simply theoretical capacity; it must also be deliverable to potential customers. If the power from Redbud Facility is unable to reach the

to them are not currently guaranteed either ATC or firm transmission service from the McClain Facility.

¹⁶ On March 29, 2004, Commission Trial Staff (Trial Staff) filed initial comments on OG&E's settlement offer. Those comments included an affidavit of Joseph P. Cholka of the Commission Trial Staff (Exhibit Staff-Aff-3) that proposed eight modifications to the OG&E market monitoring plan in ¶36. On April 6, 2004, OG&E agreed to all of these modifications (Exhibit OGE-Sett-2 at ¶25).

wholesale market, the firm transmission created by the upgrades is meaningless and the 1,200 MW will not provide effective mitigation. Therefore, InterGen proposes that OG&E be required to upgrade its transmission facilities to ensure that the entire 1,200 MW Redbud Facility is physically deliverable.

17. InterGen proposes that the Commission condition the Transaction on OG&E adopting an all-inclusive economic dispatch¹⁷ under which least-cost energy within OG&E's control area is dispatched. InterGen states that economic dispatch would: (1) ensure that InterGen's and other suppliers' additional supply of low-cost power will not be foreclosed from the market; (2) require OG&E to place independent generation capacity with similar operating characteristics on equal terms with the McClain Facility and OG&E's other resources; (3) and put OG&E in the same position it was prior to the Transaction.

18. InterGen states that in the absence of an RTO, the only mitigation that specifically addresses OG&E's increased vertical market power would be for an independent entity to perform OG&E's transmission function and to ensure that OG&E includes in its economic dispatch non-OG&E generators, such as the Redbud Facility. Therefore, InterGen supports the OG&E Offer of Settlement's proposal to use an independent market monitor, except that the market monitor should have more oversight responsibilities. For instance, the independent entity must: actively oversee OG&E's processing of transmission studies, requests for transmission service, ATC calculations, and interface with SPP; be independent of OG&E and all other market participants; be selected with the approval of the Commission and the OCC; and ensure that OG&E adheres to the least-cost, security constrained economic scheduling and dispatch requirement and that OG&E is not operating its generation or transmission facilities to foreclose competition or otherwise increase OG&E's costs to serve load. In addition, InterGen states that pending completion of the transmission upgrades needed to make all 1,200 MW of the Redbud Facility deliverable on a firm basis, OG&E should make as much of that plant deliverable on a firm basis as possible through the use of a security-constrained economic dispatch that includes all sellers willing to participate. InterGen states that the independent entity should also oversee the implementation of these interim mitigation measures.

¹⁷ Economic dispatch models the electric power system and dispatches the available generation resources to supply a given load for each control area in the most economic manner in real-time operation.

E. AES Offer of Settlement

19. AES proposes that a merit order bid system overseen by the OCC be implemented to mitigate OG&E's vertical and horizontal market power from the Transaction. According to AES, the proposal would function on a week-ahead basis would provide OG&E ratepayers with reduced costs, and would give economic competitors the opportunity to sell power within the OG&E market power area. AES states that this proposal, in conjunction with the independent market monitoring plan to oversee transmission dispatch, would mitigate market power issues raised by the Commission in the December 18 Order.

F. Comments on Offers of Settlement

20. The Arkansas Public Service Commission (APSC) filed comments stating that it was not taking a position on the OG&E Offer of Settlement. However, the APSC notes that if OG&E seeks to recover any costs related to the Transaction from its retail ratepayers in Arkansas, the APSC will address the Transaction in a retail proceeding. AES asserts that it cannot now take a position on the OG&E Offer of Settlement, because OG&E has not provided enough information or time for AES to analyze it. OMPA states that in light of the insolvency of NRG McClain, it is in the best interest of its customers for the McClain Facility to be bought by a solvent entity, such as OG&E. OMPA further notes that although it does not necessarily endorse the OG&E Offer of Settlement, it does seek prompt approval of the Transaction.

21. The Staff of the Public Utility Division of the Oklahoma Corporation Commission (PUD Staff) state that although it does not take a position on the merits of either of the Offers of Settlement, it supports the expedited resolution of this proceeding. The PUD Staff also states that given the direct and substantial effects that economic dispatch may have on Oklahoma's jurisdictional retail ratepayers, this issue is better suited for disposition by the OCC.

22. InterGen filed comments and reply comments opposing the OG&E Offer of Settlement. Because the substance of those comments is reflected in the discussion of InterGen's Offer of Settlement, we will not summarize InterGen's comments.

23. Trial Staff submitted initial comments on the OG&E Offer of Settlement. Subject to certain clarifications and modifications, the Trial Staff concludes that the OG&E Offer of Settlement is reasonable. In particular, Trial Staff states that its assessment of the competitive effects of the Transaction produced screen violations for economic capacity in all time periods and for available economic capacity in non-summer periods. Trial Staff concludes that the mitigation measures proposed in the OG&E Offer of Settlement

would prevent the proposed acquisition from increasing OG&E's horizontal and vertical market power, if they are clarified and modified in certain respects (all of which have been accepted by OG&E). Trial Staff states that the 600 MW Bridge will mitigate the horizontal and vertical competitive effects of the Transaction, because the alternate supply of 600 MW to the destination area will more than replace OG&E's proposed acquisition of 400 MW.

24. For the interim period before the completion of the 600 MW Bridge, Trial Staff proposes that OG&E increase some of the duties of the independent market monitor to give added assurance of effective mitigation. Among other things, the independent market monitor should follow short-term contract sales instead of daily changes in wholesale prices, as these contracts are a better indicator of market activity in the OG&E control area. The OG&E Offer of Settlement should also be modified to clearly state that OG&E must provide information on OG&E's short-term purchases and short-term sales and that the market monitor must oversee OG&E's redispatch during the interim period. With such changes, Trial Staff concludes that OG&E's independent market monitor will effectively mitigate the vertical market power concerns raised by the Commission in the December 18 Order.

25. OG&E filed initial comments on the InterGen Offer of Settlement. It points out that the InterGen Offer of Settlement raises issues with regard to the pre-Transaction market structure. According to OG&E, the Commission's precedent requires that any mitigation imposed on the Transaction be limited to addressing the effects of the proposed Transaction, not pre-existing market problems. Furthermore, the InterGen Offer of Settlement unduly burdens OG&E and the reliability of its system and is not necessary to address the competitive implications of the proposed Transaction. OG&E also states that its proposed mitigation measures better mitigate the effects of the Transaction and are far simpler to implement than the complete redesign of the market structure, as proposed by InterGen.

26. In addition, OG&E states that, contrary to InterGen's assertion, OG&E does not engage in uneconomic dispatch. OG&E asserts that it dispatches its system in order to meet its obligations in a reliable and cost-effective manner. OG&E also maintains that InterGen is attempting to change the market structure to increase its competitive position. OG&E notes that Commission precedent states that section 203 is not intended to protect competitors, but to protect competition for the benefit of customers. OG&E also submitted reply comments stating that InterGen's request for economic dispatch is tantamount to a demand for a region-wide generation power pool and that this request exceeds any mitigation proposal ever adopted by the Commission in a section 203 proceeding. OG&E also asserts that the creation of such a power pool could not be accomplished by OG&E acting alone; it would require legislative action by Arkansas and

Oklahoma, as well as the approval of Commission under section 205 of the FPA. Moreover, OG&E states that InterGen's demand for economic dispatch is unrelated to the effects of the Transaction.

II. Discussion

27. As discussed below, we approve the OG&E Offer of Settlement, subject to modification, because it will put in place mitigation, both interim and permanent, to prevent harm to competition in OG&E's market from the Transaction. As stated above, the OG&E Offer of Settlement includes all of the revisions proposed by Trial Staff, we specify additional revisions and clarifications herein. This will resolve the concerns about increases in OG&E's horizontal and vertical market power from the Transaction, while at the same time being neither unduly burdensome to OG&E nor in any way harming the reliability of its system. Accordingly, the Commission approves the Transaction, as modified, as consistent with the public interest.

28. Because we find that the OG&E Offer of Settlement, as revised, effectively mitigates OG&E's increased market power identified in the December 18 Order, we conclude that it is not necessary to adopt the additional mitigation measures proposed in the InterGen Offer of Settlement. In particular, because the OG&E Offer of Settlement, as modified, mitigates OG&E's horizontal and vertical market power resulting from the Transaction, we find that many of the mitigation measures proposed by the InterGen Offer of Settlement (such as an all-inclusive economic dispatch) are not necessary. Therefore, although we adopt some of InterGen's suggestions, we reject the InterGen Offer of Settlement to the extent that it differs from OG&E's settlement as modified.

A. Horizontal Market Power

29. In the December 18 Order, the Commission stated that “[t]he increase in horizontal market power [from the Transaction] is indicated by the horizontal screen failures. . . .”¹⁸ That order also directed OG&E to do a revised horizontal competitive analysis that assigns control to the sellers of certain expiring power purchase agreements in the pre-Transaction period, because those contracts would expire irrespective of the Transaction.¹⁹ Consistent with that directive, OG&E reanalyzed in its Offer of Settlement the effect on competition of the Transaction with respect to horizontal market power, attributing control of those contracts to the sellers rather than to OG&E, the

¹⁸ December 18 Order, 105 FERC ¶ 61,207 at P 30.

¹⁹ Id. at P 33.

buyer, in the pre-Transaction period. This analysis better reflects the effect of the Transaction. We note that in this revised analysis, the screen failures are larger and more systematic than those in OG&E's original analysis, indicating more of a need to mitigate the harm.

30. First, with regard to long-term mitigation, OG&E states in its Offer of Settlement that it will construct a 600 MW Bridge between the Redbud Facility and OG&E's control area and that this will address the Commission's concern regarding permanent market power problems from the Transaction. However, InterGen argues that merely replacing the generating capacity eliminated from the market by the Transaction will not restore competition because the HHI would still be at higher levels post-Transaction than it was pre-Transaction.²⁰ Therefore, InterGen argues that access to more than 1,200 MW of additional competing capacity is needed to bring the HHIs to their pre-Transaction levels and that OG&E should be required to "upgrade its transmission facilities to assure that the entire 1,200 MW Redbud Facility is physically deliverable."²¹ In addition, InterGen argues that if the 1,200 MW cannot reach the market, the transmission upgrades would not mitigate the Transaction's harm to competition. Accordingly, InterGen wants OG&E to do economic dispatch.

31. Contrary to InterGen's claims, the purpose of mitigation is not to restore the HHIs to their pre-Transaction levels, but to restore competition. Indeed, the purpose of the HHIs is to identify possible harm to competition that requires market power mitigation measures. In Order No. 642, the Commission noted that the competitive screen is only the first step in the analysis of a transaction's effect on competition, not the end of the analysis.²² The Commission also stated:

²⁰ To the extent that InterGen seeks to impose conditions to address pre-Transaction market issues, the Commission has held that the mitigation measures it will impose on a section 203 filing are "limited to remedying anticompetitive harms that result directly from the proposed merger, not mere competitive disadvantages that may have existed prior to the merger." *Entergy Services, Inc. and Gulf States Utilities Co.*, 64 FERC ¶ 61,001 at 61,013 (citation omitted), reh'g denied, 64 FERC ¶ 61,326 (1993). In other words, OG&E's increased market power resulting from the Transaction, not OG&E's pre-existing market power, must be mitigated.

²¹ InterGen Offer of Settlement, Explanatory Statement at 2.

²² Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,882.

The facts of each case (e.g., market conditions, such as demand and supply elasticity, ease of entry and market rules, as well as technical conditions, such as the types of generation involved) determine whether the merger would harm competition. When there is a screen failure, applicants must provide evidence of relevant market conditions that indicate a lack of a competitive problem or they should propose mitigation.²³

Furthermore, as the Commission noted in the Merger Policy Statement: “remedies should be clearly designed to mitigate the specific competitive problems identified in the analysis.”²⁴ Thus, even if an unmitigated proposed acquisition would increase market power, the Commission must still approve the transaction if its anticompetitive effects are properly mitigated and the transaction is otherwise consistent with the public interest.²⁵

32. Thus, the fact that post-Transaction HHIs are higher than the pre-Transaction HHIs is not a concern as long as mitigation measures resolve the competitive concerns raised by the Transaction. We find that it is not necessary to restore HHIs to pre-Transaction levels, because the offsetting of the 400 MW supply by access to an equivalent amount of alternative supply (i.e., the 600 MW Bridge) will address the concerns raised by the horizontal screen failures. In other words, by providing even more competing supply than is eliminated by the Transaction, the OG&E Offer of Settlement addresses the harm to competition resulting from increases in horizontal market power due to the Transaction. As a result of the 600 MW Bridge, any attempt by OG&E to exercise horizontal market power (i.e., increase price by reducing supply) would be no more successful than it would have been absent the Transaction, because the reduction in supply is offset by an alternate supply that customers can reach to avoid the attempted price increase. Thus, we find that the 600 MW Bridge is an appropriate structural remedy to the possible permanent horizontal market power problems posed by the Transaction.

²³ Id. (footnote omitted).

²⁴ Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,136 (1996). The Commission has also stated that “[t]he law restrains mergers that harm competition. . . . Because the law concerns itself with competition, rather than competitors.” Northeast Utilities Service Company, 56 FERC ¶ 61,269 at 62,066 (1991).

²⁵ Id. at 30,120 (“Although a competitive analysis pursuant to the Guidelines may show that a proposed merger would have anticompetitive effects, the Commission may be able to approve the merger as consistent with the public interest if appropriate mitigation measures can be formulated.”).

33. However, this does not address the horizontal market problems that exist in the interim until the 600 MW Bridge is operational. In addition, to long-term mitigation, the Commission has also stated that mitigation of a market power problem must be in place at the time a transaction is consummated.²⁶ The OG&E Offer of Settlement proposes that, during the period before completion of the 600 MW Bridge, OG&E will redispatch, at no extra cost to InterGen, OG&E's generating units to enable the Redbud Facility to obtain transmission to sell power (not to exceed 600 MW in the aggregate) to any wholesale customers within the OG&E control area that InterGen obtains during the interim period, subject to reliability constraints. The OG&E Offer of Settlement also proposes that an independent market monitor perform various functions, including overseeing OG&E's calculation of ATC and TTC.

34. Although we find that redispatch can be an effective interim mitigation measure, we note that if InterGen's access to OG&E's control area is hindered, the interim redispatch plan would not sufficiently preserve competition in the OG&E market. To ensure that the interim mitigation plan prevents this, the OG&E Offer of Settlement proposes that the independent market monitor oversee OG&E's implementation of the redispatch plan. We believe that OG&E's proposed market monitoring plan is a good start, but find that the proposed plan might not be a fully effective remedy. Therefore, we require that the scope of OG&E's market monitoring plan be expanded. Specifically, the independent market monitor must directly notify this Commission of any structural or operational problems that could prevent OG&E's horizontal and vertical market power from being properly mitigated. (We address below the specifics of the market monitoring plan related to the potential for OG&E to exercise vertical market power.) The market monitor must prepare and submit to the Commission a quarterly report within ten days of the end of each quarter (until the 600 MW Bridge is completed). That report must summarize its analysis and evaluation of market events that result in a significant increase in wholesale prices or the foreclosure of competition to rival suppliers and any other such anticompetitive conduct. In addition, because our timely awareness of, and response to, any Transaction-related anticompetitive effects resulting from the operation of OG&E's transmission system would be greatly limited by the filing of only quarterly reports, the market monitor must submit to the Commission any such other reports if the market monitor concludes that OG&E is implementing the redispatch plan in a manner that hinders competition. Such reports will be provided to the Commission promptly upon completion without waiting for the periodic quarterly report.²⁷

²⁶ December 18 Order at P 34 (citing *American Electric Power*, 90 FERC ¶ 61,242 at 61,789, order on reh'g, 91 FERC ¶ 61,129 (2000), order on compliance filing, 91 FERC ¶ 61,208 (2000). (AEP)).

²⁷ When filing reports, the market monitor may claim confidentiality under

B. Vertical Market Power

35. In the December 18 Order, the Commission explained that “[t]he increase in vertical market power comes from the fact that OG&E, a vertically integrated utility, would be adding 400 MW of generation capacity to its existing transmission and generation facilities, thus increasing its incentive (it already has the ability) to use its control of transmission facilities to disadvantage its competitors in wholesale power markets.”²⁸ We expressed concern about whether the Transaction would allow OG&E to use its transmission system to raise electricity prices and/or frustrate entry into the relevant wholesale electricity market (*i.e.*, deny rival suppliers access to that market). Accordingly, the Commission stated that mitigation was needed to ensure that the Transaction does not harm competition. In addition, OG&E’s analysis showed highly concentrated relevant markets, which (along with control of transmission) allows the exercise of vertical market power, so the Commission determined that OG&E could exercise vertical market power. In addition, the Commission also was not persuaded that SPP’s OATT²⁹ would fully mitigate increases in OG&E’s vertical market power.³⁰ Accordingly, the Commission stated that mitigation measures were needed to ensure that the Transaction does not harm competition by increasing OG&E’s vertical market power.

36. Competition can be harmed when a vertically integrated utility acquires a competitor in its control area because competing suppliers can be foreclosed from access to wholesale customers. There are a number of possible solutions to mitigate this

18 C.F.R. § 388.112 (20003), and others may challenge such a claim. We note that the our requirement that the independent market monitor submit various reports is based on the market monitoring plan that the Commission adopted in AEP to address its concerns with respect to the merger of American Electric Power Company (AEP) and Central and South West Corporation (CSW). See 91 FERC ¶ 61,208 at 61,746. In that case, the Commission found that the merger would increase AEP’s ability and incentive to use its transmission system to harm competition in wholesale electricity markets. While that merger combined a much larger system, more generation, and transmission than is the case in this proceeding, the economic issues are similar. As such, the role of the market monitor is substantively very similar in both cases, and the market monitoring plan in the AEP/CSW merger is a good model for the independent market monitor here.

²⁸ December 18 Order, 105 FERC ¶ 61,207 at P 30.

²⁹ OG&E’s transmission facilities are governed by SPP’s OATT.

³⁰ Id.

problem, including: (1) generation divestiture; (2) transmission expansion; and (3) an economic dispatch plan. The first two mitigation measures are structural solutions and address the problem by offsetting the amount of generation potentially foreclosed from access to customers. The third option, an economic dispatch plan, would address the problem by ensuring that suppliers have access to all wholesale customers in the market.

37. Intergen and AES have each proposed economic dispatch as a way of mitigating the increase in vertical market power resulting from the Transaction. As mentioned above, we agree that an economic dispatch plan would mitigate such market power. However, the OG&E Offer of Settlement proposes a structural remedy that would also mitigate OG&E's increased vertical market power. The OG&E Offer of Settlement proposes an effective transmission expansion (namely, the 600 MW Bridge) that addresses the increase in the ability to foreclose competition resulting from the Transaction. Such a measure improves market competitiveness by reducing concentration and increasing the entry of competing suppliers by ensuring better access to customers. Moreover, we note, given the circumstances here (i.e., according to OG&E's estimate, an interim mitigation measure is only necessary for the 11 months until the 600 MW Bridge is completed), economic dispatch would not provide timely mitigation to curb OG&E's increased vertical market power. The implementation of AES' and Intergen's economic dispatch proposals (in a manner that would be fair to all parties and would not jeopardize system reliability) would take much longer than the 11 months that OG&E estimates that it will take to complete the transmission expansion. With regard to that period, OG&E has proposed interim mitigation (i.e., the redispatch plan and oversight of that plan by the independent market monitor) for the period between the consummation of the Transaction and the completion of the 600 MW Bridge. We note that the Commission will consider undertaking further mitigation measures if the 600 MW Bridge is not operational within 11 months. Specifically, we would consider imposing further mitigation measures, including requiring OG&E to adopt an economic dispatch plan.

38. As noted, the OG&E Offer of Settlement proposes that the independent market monitor will oversee the calculation and posting of ATC and TTC for OG&E and will communicate such data to SPP. Nevertheless, Intergen argues that additional mitigation measures are necessary to minimize OG&E's ability to use control of its transmission system to cut off access by the Redbud Facility. In particular, Intergen requests that the Commission require OG&E to implement an economic dispatch plan that includes the Redbud Facility. Furthermore, InterGen proposes that an independent entity be hired to oversee OG&E's transmission operations and the implementation of its economic dispatch plan, if the Commission grants its request to implement such a plan.

39. We agree with InterGen that the independent market monitor's duties must be expanded beyond OG&E's proposal so that it oversees more of OG&E's transmission functions. The OG&E Offer of Settlement proposes that the independent market monitor must monitor whether InterGen's access to any wholesale customer in the OG&E control area is being limited by OG&E. Furthermore, it provides that the independent market monitor will have access to prices for OG&E's short-term purchases and sales to allow it to look for price changes related to congestion events, and that the independent market monitor will review ATC and TTC calculations for the 600 MW Bridge and monitor how OG&E awards transmission service, in addition to overseeing ATC and TTC for the OG&E system.³¹ We find that the independent market monitor performing the activities that OG&E proposes, as revised herein, will ensure that OG&E does not use its redispatch to limit competitors' access to transmission.

40. Furthermore, the Commission notes that it is not delegating its authority to the independent market monitor, and, in this regard, the independent market monitor can take no enforcement action other than filing complaints with the Commission.

41. The Commission finds that the combination of the 600 MW Bridge and the hiring of an independent market monitor to monitor, among other things, OG&E's actions with regard to the new ATC from the 600 MW Bridge and the transmission available from OG&E's redispatch offer will mitigate the increase in vertical market power resulting from the Transaction. Accordingly, we find that the OG&E Offer of Settlement, as modified, puts in place sufficient mitigation measures that alleviate the market power effects of the Transaction and therefore resolves the issues set for hearing in the December 18 Order.

³¹ We note that OG&E has filed to be part of the SPP regional transmission organization. Once SPP is calculating and posting ATC and TTC, this interim mitigation measure will not be necessary. This is similar to the situation in AEP. 90 FERC ¶ 61,242 at 61,789. In that case, the Commission eliminated AEP's ability to exercise vertical market power by requiring independent calculation and posting of ATC along with market monitoring. Id.

C. Effect on Rates

42. In the December 18 Order, the Commission found that the Transaction, if properly conditioned, would not harm wholesale electricity rates. The mitigation measures required in this order will ensure that the Transaction will not adversely affect wholesale rates.

The Commission orders:

(A) OG&E's Offer of Settlement is approved, subject to modification, as discussed in the body of this order.

(B) InterGen's Offer of Settlement is rejected in part, as discussed in the body of this order.

(C) AES's Offer of Settlement is rejected, as discussed in the body of this order.

(D) OG&E's proposed disposition of jurisdictional facilities is hereby authorized, as discussed in the body of this order.

(E) The foregoing authorization is without prejudice to the authority of the Commission or any other regulatory body with respect to rates, service, accounts, valuation, estimates or determinations of costs, or any other matter whatsoever now pending or which may come before the Commission.

(F) Nothing in this order shall be construed to imply acquiescence in any estimate or determination of cost or any valuation of property claimed or asserted.

(G) The Commission retains authority under sections 203(b) and 309 of the FPA to issue supplemental orders as appropriate.

(H) OG&E shall make appropriate filings under section 205 of the FPA, as necessary, to implement the transaction.

(I) OG&E shall notify the Commission within 10 days of the date that the acquisition and disposition of the jurisdictional facilities have been consummated.

By the Commission. Chairman Wood concurring with a separate statement attached.

(S E A L)

Magalie R. Salas,
Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Oklahoma Gas and Electric Company
NRG McClain LLC

Docket No. EC03-131-000

(Issued July 2, 2004)

WOOD, Chairman, concurring:

In many ways this case is like the scores of others that have been reviewed under this commission's standard merger analysis. The challenge here was to find appropriate mitigation to be put in place at the time the merger is consummated. Each region and each case presents different mitigation options.

As a general matter, I agree with the antitrust agencies' advice frequently given to FERC, which is that structural remedies are far more effective than behavioral remedies. This order appropriately relies primarily on transmission upgrades which will improve the structure of the market. However it also relies in part on market monitoring for a brief period of time to mitigate market power. I do not put much weight on monitoring to remedy the increase in market power from a merger because all it can do is identify a problem which then cannot be solved.

A preferable approach would incorporate an open regional economic dispatch process at this time. Economic dispatch is the process used in all electric systems to turn on and run generators in merit order, beginning with the lowest cost resources and moving up the generation stack when load is higher. It is a key determinant of which suppliers are in or out of the market on a day to day basis. An open dispatch would ensure that both affiliated and non-affiliated resources are able to provide service on the basis of merit and least cost to customers. Economic dispatch would directly prevent foreclosure from the market. True economic dispatch over a region (as contrasted to dispatch just within a single utility) increases efficiency and lowers wholesale and retail customers' bills.

The record before us included proposals for regional economic dispatch. I regret that we were unable to craft such an approach. As the order notes:

“...[G]iven the circumstances here (i.e., according to OG&E's estimate, an interim mitigation measure is only necessary for the 11 months until the 600 MW bridge is completed), economic dispatch would not provide timely mitigation to curb OG&E's increased vertical market power. The implementation of AES' and Intergen's economic dispatch proposals (in a manner that would be fair to all parties and would not jeopardize system reliability) would take much longer than

the 11 months that OG&E estimates it will take to complete the transmission expansion.”

I am encouraged by the comments of the Oklahoma Corporation Commission staff indicating that they recognize the “direct and substantial effects that economic dispatch may have on Oklahoma’s jurisdictional retail ratepayers.” I believe that the active leadership of the state commission will lead to the development of a long-term dispatch solution that saves customers money. I offer our services to the Oklahoma Corporation Commission in pursuing that end.

I note, also favorably, that OG&E is a member of the Southwest Power Pool, the nation’s latest RTO. I believe that to achieve true regionwide benefits, both timely transmission expansion (which we are getting in this case) and economically-efficient dispatch of all available generation resources, can best be managed under the RTO.

I wish we could have crafted an economic dispatch solution to be in place prior to consummation of this merger to more effectively mitigate market power and promptly bring efficiency benefits to customers.

Pat Wood, III
Chairman