Federal Energy Regulatory Commission
February 21, 2008
Open Commission Meeting
Statement of
Chairman Joseph T. Kelliher

Items E-2, E-3 and E-4, Cross-Subsidization Restrictions on Affiliate Transactions (Docket No. RM07-15-000), Blanket Authorization under FPA Section 203 (Docket No. RM07-21-000) and FPA Section 203 Supplemental Policy Statement (Docket No. PL07-1-001)

"It has been more than two years since enactment of the Energy Policy Act of 2005, which significantly expanded FERC's merger and corporate review authority. It did so by amending section 203 of the Federal Power Act to clarify our jurisdiction over holding company mergers, by granting FERC authority over certain holding company securities acquisitions, and by granting FERC authority to review disposition of generation facilities.

The Energy Policy Act largely codified the merger test used by FERC for some years, with one significant change, namely adding to the public interest determination a required finding that a transaction will not result in cross subsidization of a non-utility associate company or the pledge or encumbrance of utility assets for the benefit of an associate company, unless such pledge or encumbrance is in the public interest.

FERC acted quickly to implement its expanded corporate review authority, and the past two years have been very active. While we acted quickly, we have also been careful in how we exercised our expanded regulatory authority. Throughout this period, we have sought to facilitate transactions and investment in a capital intensive industry, while discharging our statutory duty to prevent the accumulation and exercise of market power. As we have implemented our expanded merger and corporate review authority, we have continued to review and act on proposed utility mergers.

Preventing cross subsidization is certainly not a new responsibility for FERC; it has been a core duty for the agency since 1935. However, normally we police cross subsidies when we review rates, rather than at the point of a merger. So, to that extent the cross subsidization provisions of the Energy Policy Act were new – charging us with assuring mergers will not result in improper cross subsidization.

We have taken a number of steps to strengthen our protections against cross subsidization. In our rulemaking implementing the revisions to section 203, we required merger applicants to demonstrate that a proposed merger would not result in inappropriate cross subsidization. We followed that action with a package of orders issued last July to strengthen our protections against cross subsidization.

Cross subsidization is a matter of concern to both federal and state regulators, since as a general matter the beneficiaries of cross subsidization protections are both retail consumers and wholesale captive customers. Knowing that, we have been careful in how we exercise our authority to avoid conflict with our state colleagues. Most state commissions have authority to review mergers of state regulated utilities, and most state commissions can impose so-called ring fencing or other conditions designed to protect retail consumers.

We worked closely with our state colleagues as we considered new safeguards against improper cross-subsidization. In particular, we invited state regulators from states with very strong protections to offer their views, namely Commissioner Ray Baum from Oregon and former Commissioner Robert Garvin from Wisconsin. We also benefited from the views of former Michigan Public Service Commission Chairman Steve Fetter and Commissioner Jimmy Ervin from North Carolina. We gave their views great weight in our deliberations.

Our central focus is the potential for cross subsidization by wholesale customers as a result of a proposed merger. While our primary means of protecting customers at the wholesale level is through rate mechanisms, we must also review whether additional protections are needed in the context of a proposed merger. If the answer is yes, FERC policy is that we will defer to state-imposed protections if they are sufficient to protect wholesale customers. If state commissions do not have authority to impose necessary protections or if state-imposed protections are not sufficient, we will act to fill any regulatory gap. If FERC were to take an expansive approach towards implementation of the new cross subsidization provisions in section 203, and adopt inflexible, mandatory federal standards, the result could be direct conflict with our state colleagues.

In the package of orders we approve today, we leave in place the supplemental merger policy statement adopted last summer but provide some additional clarifications. We also grant several additional blanket authorizations for public utilities to engage in certain corporate transactions where there is no potential to adversely affect market power or rates, and no opportunity for improper cross-subsidization. Finally, under our ratemaking authority, we codify restrictions on non-power goods and services transactions between utilities with captive customers and non-regulated affiliates. Importantly, these restrictions apply not only to utilities that may be seeking merger approval, but to all franchised public utilities that have captive customers or that own or provide transmission services over Commission-jurisdictional transmission facilities. These restrictions are in addition to the ones we impose on utilities with market-based rates and they will fill any regulatory gap in cross-subsidization protection. They will also provide greater regulatory certainty.

These orders recognize that cross subsidization is a common concern to both federal and state regulators, seek to avoid regulatory conflict, respect state authority, and attempt to harmonize federal and state regulation in this area.

These orders complete our initial implementation of the rules governing future FERC action on section 203 transactions. They also expand use of the Commission's ratemaking authority to protect against improper cross-subsidization on an ongoing basis."