

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Duke Power, a Division of Duke Energy Corporation	Docket Nos. ER96-110-013 EL05-4-000
Duke Energy Marketing America, LLC	ER03-956-006
Duke Energy Moss Landing LLC	ER98-2680-010
Duke Energy Morro Bay LLC	ER98-2681-010
Duke Energy Oakland LLC	ER98-2682-010
Duke Energy South Bay LLC	ER99-1785-009
Bridgeport Energy, LLC	ER98-2783-008

ORDER ON MARKET-BASED RATES

(Issued June 30, 2005)

1. In this order, the Commission revokes Duke Power's market-based rate authority in the Duke Power control area and directs Duke Power to file, within thirty days of the date of this order, a revised market-based rate tariff prohibiting sales at market-based rates in the Duke Power control area and providing for the default cost-based rates specified in an order issued on April 14, 2004,¹ to be effective as of the refund effective date in this proceeding.

¹ *AEP Power Marketing, Inc.*, 107 FERC ¶ 61,018 at P 151-55 (April 14 Order), *order on reh'g*, 108 FERC ¶ 61,026 (2004) (July 8 Order).

2. On February 14, 2005, Duke Power, a division of Duke Energy Corporation (Duke Power), made a filing (February 14 filing) in compliance with the Commission's order of December 15, 2004 in this proceeding.² In the December 15 Order, the Commission instituted a proceeding under section 206 of the Federal Power Act (FPA)³ to determine whether Duke Power may continue to charge market-based rates within the Duke Power control area based on Duke Power's failure of the wholesale market share screen for generation market power.⁴

3. In the February 14 filing, Duke Power submitted the instant Delivered Price Test (DPT) analysis to rebut the presumption of market power established by its failure of the wholesale market share screen in the Duke Power control area. As discussed below, we find that Duke Power has failed to rebut the presumption of market power in the Duke Power control area. Based on the results of the wholesale market share screen, the historical data, DPT for available economic capacity and economic capacity, and the Herfindahl-Hirschman Index (HHI) test, we find that Duke Power has market power in the Duke Power control area. The FPA requires that all rates charged by public utilities for the transmission or sale for resale of electric energy be "just and reasonable."⁵ Where there is a competitive market, the Commission may rely on market-based rates in lieu of cost-of-service regulation to ensure that rates are just and reasonable.⁶ Consistent with our precedent, the Commission authorizes sales of electric energy at market-based rates only if the seller and its affiliates do not have, or have adequately mitigated, market power in the generation and transmission of such energy, and cannot erect other barriers

² *Duke Power*, 109 FERC ¶ 61,270 (2004) (December 15 Order).

³ 16 U.S.C. § 824e (2000).

⁴ In the December 15 Order, the Commission accepted for filing the updated market power analyses filed by Duke Energy Marketing America LLC (DEMA), Duke Energy Moss Landing LLC (Moss Landing), Duke Energy Morro Bay (Morro Bay), Duke Energy Oakland LLC (Oakland), Duke Energy South Bay (South Bay), and Bridgeport Energy LLC (Bridgeport). Duke Power, DEMA, Moss Landing, Morro Bay, Oakland, South Bay, and Bridgeport are collectively referred to as the Duke Companies.

⁵ 16 U.S.C. § 824d(a) (2000).

⁶ *Cf. Elizabethtown Gas Co. v. FERC*, 10 F.3d 866, 870 (D.C. Cir. 1993) (discussing "just and reasonable" rate requirement of Natural Gas Act).

to entry by potential competitors.⁷ Thus, where, as here, a market-based rate applicant is found to have market power, it is incumbent upon the Commission to revoke such applicant's market-based rate authority.

4. Therefore, the Commission herein revokes Duke Power's market-based rate authority in the Duke Power control area.⁸ Accordingly, Duke Power is directed to file, within thirty days of the date of this order, a revised market-based rate tariff prohibiting sales at market-based rates in the Duke Power control area and providing for the default cost-based rates as specified in the April 14 Order to be effective as of the refund effective date in this proceeding. In addition, Duke Power is directed to provide cost support for these rates and provide a refund report based on the default rates. This filing is directed without prejudice to Duke Power's ability to propose tailored mitigation that would apply prospectively or to make sales under its existing Commission-approved cost-based rate tariffs. Further, where, as here, an applicant is found to have market power, we will no longer waive our otherwise applicable accounting regulations (*e.g.*, Parts 41, 101, and 141 of the Commission's regulations),⁹ and we will not grant blanket approval for issuances of securities or assumptions of liability pursuant to Part 34 of the Commission's regulations for the applicant and its affiliates.

5. This order will protect customers from unjust and unreasonable rates and charges that result from the exercise of market power and will establish just and reasonable rates for wholesale sales of energy and capacity by Duke Power in the Duke Power control area. The next updated market power analysis for the Duke Companies is due three years from the date of this order.

Background

6. On August 11, 2004, as amended on November 19, 2004 and November 24, 2004, Duke Power submitted for filing updated market power screens (August 11 filing) in

⁷ See, *e.g.*, *Heartland Energy Services, Inc.*, 68 FERC ¶ 61,223 at 62,060 (1994); *Louisville Gas & Electric Co.*, 62 FERC ¶ 61,016 at 61,143-44 (1993).

⁸ The revocation of Duke Power's market-based rate authority in the Duke Power control area does not apply to, or affect, existing market-based rate contracts that were entered into prior to the refund effective date in this proceeding.

⁹ *Id.* at P 150.

compliance with the Commission's April 14 Order and July 8 Order.¹⁰ The filing, as amended, indicated that Duke Power passed the pivotal supplier screen but that it failed the wholesale market share screen for each of the four seasons considered in the Duke Power control area.¹¹ As we stated in the April 14 Order, where an applicant is found to have failed either generation market power screen, such failure provides the basis for instituting a proceeding under section 206 and establishes a rebuttable presumption of market power in the resulting section 206 proceeding.¹² Accordingly, because Duke Power's August 11 filing indicated that it failed the wholesale market share screen, the Commission instituted in the December 15 Order a section 206 proceeding to investigate generation market power in the Duke Power control area. The Commission also established a refund effective date pursuant to the provisions of section 206.

7. As discussed in the April 14 and July 8 Orders, the screens are conservatively designed to identify the subset of applicants who require closer scrutiny. Accordingly, for the Duke Power control area, Duke Power was directed within 60 days from the date of issuance of the December 15 Order to: (1) file a DPT analysis; (2) file a mitigation proposal tailored to its particular circumstances that would eliminate the ability to exercise market power; or (3) inform the Commission that it will adopt the April 14 Order's default cost-based rates or propose other cost-based rates and submit cost support for such rates.¹³ In addition, as the Commission stated in the April 14 Order,¹⁴ the applicant or intervenors may present evidence such as historical sales data to support whether the applicant does or does not possess market power.

¹⁰ On August 17, 2004, Duke Power submitted an errata to its August 11 filing correcting pages to Exhibits DUK-1, DUK-5, DUK-6, DUK-7, DUK-8, DUK-9 and Workpapers (August 17 filing). However, as Duke Power states, none of these data changes impact its conclusions in any way.

¹¹ Duke Power's filing, as amended, shows that it has a market share as high as 72 percent in the Duke Power control area market.

¹² April 14 Order, 107 FERC ¶ 61,018 at P 201.

¹³ *Id.* at P 201, 207-09.

¹⁴ *Id.* at P 37 n.11.

Description of the Filing

8. In the February 14 filing, Duke Power submitted a compliance filing in accordance with the Commission's December 15 Order. Duke Power states that, consistent with the April 14, July 8, and December 15 Orders, it has prepared a DPT analysis for the Duke Power control area using the available economic capacity and economic capacity measures. Duke Power states that, to evaluate the competitiveness of the market, it applied these metrics to the Commission's pivotal supplier test, the market share test and the market concentration test using the HHI.

9. Duke Power states that, in order to give a clearer view of the actual competitive conditions in the Duke Power control area, it has evaluated the DPT data to ascertain: (1) how much of the wholesale customer load in the Duke Power control area is met by its own competitively-priced resources; (2) how much of that load can be considered uncommitted load and; (3) how much non-Duke Power available economic capacity is available to meet this uncommitted load.

10. Duke Power states that, although the initial DPT results indicate that Duke Power does not fall below the Commission's safe harbors in every analyzed time period and load condition, closer examination of the data, supported by the historical sales and transmission data that Duke Power previously submitted in this proceeding, confirms that Duke Power does not have the ability to affect market prices in its control area. Duke Power contends that it has successfully rebutted the presumption of market power for the Duke Power control area.

Notice and Responsive Pleadings

11. Notice of the Duke Power compliance filing was published in the *Federal Register*¹⁵ with interventions or protests due on or before March 4, 2005. North Carolina Municipal Power Agency Number 1 (Power Agency) filed comments on February 14, 2005. These comments submitted "information that may be of value to the Commission in its further deliberations in this docket." Power Agency states that it is an intervenor in the earlier proceeding leading to the December 15 Order and that it is one of five joint owners of the Catawba Nuclear Station, a facility constructed and operated by Duke Power. Power Agency states that it has not been prevented from participating in the regional power markets either as a buyer or seller. Power Agency describes several

¹⁵ 70 Fed. Reg. 9,635 (2005).

transactions within the Duke Power control area.¹⁶ It contends that its actual experience, to date, as a transmission-dependent utility in the Duke Power service area should be of interest to the Commission in evaluating the matters at issue in this proceeding.

12. On March 4, 2005, a motion to intervene and protest was timely filed by North Carolina Electric Membership Corporation (NCEMC). In its protest, NCEMC contends that its compilation of Open-Access, Same-Time Information System (OASIS) data from Duke Power shows much less available transfer capability in and out of the Duke Power control area than Duke Power's analysis. NCEMC argues that this analysis, together with its "actual experience in trying to transact with adjacent control areas, demonstrate that resources outside the Duke Power control area are often unable to compete for load within the Duke Power control area, thus raising a clear potential for Duke Power to exercise generation market power."¹⁷

13. NCEMC further contends that Duke Power's analysis rests heavily on projections of available transmission capability (ATC) between Duke Power and its neighboring control areas for the period March 2005 through March 2006. NCEMC contends that "these projections bear no relationship to projected ATCs reported on the relevant neighboring utilities' OASIS sites," citing to the OASIS sites of PJM Interconnection, LLC, Southern Company, and Carolina Power & Light.¹⁸

14. NCEMC states that Duke Power's claim that some 216 megawatts (MW) of ATC from Tennessee Valley Authority (TVA) is fully available to Duke Power-area customers is suspect because of the limitations on the availability to import power supplied by TVA.¹⁹

15. Finally, NCEMC describes its own experiences in trying to obtain supplies from others in the Duke Power control area. It concludes that the availability of competition in the Duke Power control area is not nearly as robust as is painted by Duke Power and, in any event, would be a costly alternative to pursue.

¹⁶ Power Agency Comments at 3-4.

¹⁷ NCEMC Protest at 4.

¹⁸ *Id.* at 6.

¹⁹ *Id.* at 6-11.

16. NCEMC requests that the Commission institute hearing procedures to investigate further Duke Power's ability to exercise market power in generation markets in its control area.

17. On March 22, 2005, Duke Power filed an answer to NCEMC's request for further hearing procedures. In its answer, Duke Power seeks to demonstrate that accepting NCEMC's ATC figures has no material impact on Duke Power's market power analysis, or the conclusion that Duke Power cannot exercise market power.²⁰ Duke Power contends that the other matters raised by NCEMC have no bearing on whether Duke Power has the ability to exercise generation market power and should not be used as a basis for a hearing.

Discussion

Procedural Matters

18. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2004), the timely, unopposed motion to intervene serves to make NCEMC a party to this proceeding.

19. Rule 213(a)(2) of the Commission's Rules of Practice and procedure, 18 C.F.R. § 385.213(a)(2), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept Duke Power's answer because it has provided information that assisted us in our decision-making process.

Delivered Price Test

20. In the April 14 Order, we stated that an applicant's failure of one or more of the indicative screens establishes a rebuttable presumption of market power. If such an applicant chooses not to proceed directly to mitigation, it must present a more thorough analysis using the Commission's DPT.²¹ The DPT is used to analyze the effect on competition for transfers of jurisdictional facilities in section 203 proceedings,²² using the framework described in Appendix A of the Merger Policy Statement and revised in Order

²⁰ Duke Power Answer at 2-5.

²¹ April 14 Order, 107 FERC ¶ 61,018 at P 105-12.

²² 16 U.S.C. § 824b (2000).

No. 642.²³ The DPT is a well-established test that the Commission has used routinely to analyze market power in the merger context for many years, and it has been affirmed by the courts.²⁴

21. The DPT defines the relevant market by identifying potential suppliers based on market prices, input costs, and transmission availability, and calculates each supplier's economic capacity, and available economic capacity each season/load condition.²⁵ The results of the DPT are then used to perform the pivotal supplier, market share and market concentration analyses. A detailed description of the mechanics of the DPT is provided in Appendix F of the April 14 Order and Appendix A of the Merger Policy Statement.

22. Using the economic capacity for each supplier, applicants should provide pivotal supplier, market share, and market concentration analyses. Examining these three factors with the more robust output from the DPT will allow applicants to present a more complete view of the competitive conditions and their positions in the relevant markets.²⁶

23. Under the DPT, to determine whether an applicant is a pivotal supplier in each of the season/load conditions, applicants should compare the load in the destination market to the amount of competing supply (the sum of the economic capacities of the competing suppliers). The applicant will be considered pivotal if the sum of the competing suppliers' economic capacity is less than the load level (plus a reserve requirement that is no higher than State and Regional Reliability Council operating requirements for reliability) for the relevant period. The analysis should also be performed using available

²³ *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 on reh'g*, Order No. 642-A, 66 Fed. Reg. 16,121 (2001), 94 FERC ¶ 61,289 (2001).

²⁴ *See, e.g., Wabash Valley Power Associates, Inc. v. FERC*, 268 F. 3d 1105 (D.C. Cir. 2001).

²⁵ Super-peak, peak, and off-peak, for Winter, Shoulder and Summer periods and an additional highest super-peak for the Summer.

²⁶ April 14 Order, 107 FERC ¶ 61,018 at P 107-08.

economic capacity to account for applicants' and competing suppliers' native load commitments. In that case, native load in the relevant market would be subtracted from the load in each season/load period. The native load subtracted should be the average of the actual native load for each season/load condition.

24. Each supplier's market share is calculated based on economic capacity (the DPT's analog to installed capacity). The market shares for each season/load condition reflect the costs of the applicant's and competing suppliers' generation, thus giving a more complete picture of the applicant's ability to exercise market power in a given market. For example, in off-peak periods, the competitive price may be very low because the demand can be met using low-cost capacity. In that case, a high-cost peaking plant that would not be a viable competitor in the market would not be considered in the market share calculations because it would not be counted as economic capacity in the DPT. Applicants must also present an analysis using available economic capacity (the DPT's analog to uncommitted capacity) and explain which measure more accurately captures conditions in the relevant market.

25. Under the DPT, applicants must also calculate the market concentration using the HHI based on market shares.²⁷ HHIs are usually used in the context of assessing the impact of a merger or acquisition on competition. However, as noted by the U.S. Department of Justice in the context of designing an analysis for granting market-based pricing for oil pipelines, concentration measures can also be informative in assessing whether a supplier has market power in the relevant market.²⁸

²⁷ The HHI is the sum of the squared market shares. For example, in a market with five equal size firms, each would have a 20 percent market share. For that market, $HHI = (20)^2 + (20)^2 + (20)^2 + (20)^2 + (20)^2 = 400 + 400 + 400 + 400 + 400 = 2000$. Equal-size firms in this illustration will not necessarily be observed in an actual market where one or more firms may have greater than a 20 percent market share and other firms less than a 20 percent market share. In that case, the HHI may be 2000 but the contributions of the individual firms to that concentration will vary.

²⁸ See Comments of the United States Department of Justice in response to Notice of Inquiry Regarding Market-Based Ratemaking for Oil Pipelines, Docket No. RM94-1-000 (January 18, 1994). "The Department and the Commission staff have previously advocated an HHI threshold of 2,500, and it would be reasonable for the Commission to consider concentration in the relevant market below this level as sufficient to create a rebuttable presumption that a pipeline does not possess market power."

26. A showing of an HHI less than 2500 in the relevant market for all season/load conditions for applicants that have also shown that they are not pivotal and do not possess more than a 20 percent market share in any of the season/load conditions would constitute a showing of a lack of market power, absent compelling contrary evidence from intervenors. Concentration statistics can indicate the likelihood of coordinated interaction in a market. All else being equal, the higher the HHI, the more firms can extract excess profits from the market. Likewise a low HHI can indicate a lower likelihood of coordinated interaction among suppliers and could be used to support a claim of a lack of market power by an applicant that is pivotal or does have a 20 percent or greater market share in some or all season/load conditions. For example, an applicant with a market share greater than 20 percent could argue that that it would be unlikely to possess market power in an unconcentrated market (HHI less than 1000).

27. As with our initial screens, applicants and intervenors may present evidence such as historical wholesale sales, which can be used to calculate market shares and market concentration and to refute or support the results of the DPT. In the April 14 Order, we encouraged applicants to present the most complete analysis of competitive conditions in the market as the data allow. We have used actual data in our analysis of mergers and other section 203 jurisdictional transactions to supplement or support the analysis of the effect of such transactions on competition. As we stated in Order No. 642:

If sales data indicate that certain participants actually have been able to reach the market in the past, it is appropriate to consider whether they are likely candidates to be included in the market in the future. It is for this reason that we will require a “trade data check” as part of the competitive analysis test.²⁹

28. Applicants are required to file historical trade and transmission service data that can be used to corroborate the results of the DPT. Applicants must provide actual trade data regarding electricity sales and purchases in which they participated for the most recent two years for which data are available, identifying the seller, the buyer, the characteristics of the product traded and the price.³⁰ Further, applicants must provide an explanation of any significant differences between the results obtained by the DPT and

²⁹ Order No. 642 at n. 41.

³⁰ Appendix A of the Merger Policy Statement (Order No. 592) also requires submittal of trade data as a check to compare actual trade patterns with the results of the DPT.

recent trade patterns. Applicants must also submit a description of all instances in the two years preceding the application in which transmission service on systems owned or operated by the applicants had been denied, curtailed or interrupted.

Duke Power's Delivered Price Test

Results

29. Duke Power submits that its DPT analysis under the available economic capacity measure indicates that it satisfies the Commission's standards for the pivotal supplier, but had market shares in excess of 20 percent in all season/load periods and market concentration statistics in excess of 2500 in the winter season/load periods but below 2500 in the remaining summer and shoulder periods. With respect to the economic capacity measure, Duke Power's DPT indicates that its market shares exceed 20 percent and the HHI exceeds 2500 for all ten season/load periods. Duke Power claims to not be a pivotal supplier under the economic capacity measure.

Commission Determination

30. In the February 14 filing Duke Power chose to submit the DPT using two separate sets of proposed prices. One set is system lambda, and the other is a range of market prices submitted to "reflect the full range of market and load conditions" as the "range of [system lambda] prices would have been very limited."³¹

31. System lambda, as reported on Commission Form No. 714, reflects the system incremental fuel cost of the least-cost dispatch of thermal units located in a control area.³² FERC regulations allow, "in support of the Delivered Price Test,"³³ the use of system lambda as a proxy for price³⁴ "if actual prices are unavailable."³⁵ However, actual energy

³¹ February 14 filing, Exhibit DUK-13 at 8.

³² Duke Power Co., FERC Form No. 714 submission for year ending December 31, 2003 at 10.

³³ 18 C.F.R. § 33.3(d) (2004).

³⁴ According to Electric Quarterly Report (EQR) data filed by Duke Power, the minimum sales price for short-term power sold by Duke Power at market-based rates ranged from \$17.00 per MWh to \$250.00 per MWh. The average sales price for short-term power was \$45.83 per MWh. System lambdas, by contrast, range from \$17.80 per MWh to \$44.90 per MWh. The average sales price annual system lambda is \$25.27 per MWh.

(continued)

prices are available from the EQRs.³⁶ Duke Power sells short-term energy under its market-based rate tariff to wholesale customers in the Duke Power control area, and we note that the range of market prices submitted by Duke Power in the February 14 filing better reflects these actual wholesale energy prices for 2003 and 2004 than does the use of system lambda as a proxy. Therefore, we will consider DPT results for only the range of market prices that Duke Power has submitted.

Economic Capacity

32. Duke Power's results for the economic capacity measure of the DPT, which does not include a native load deduction, exceed 65 percent in all seasons except for the off-peak shoulder period (55 percent). Duke Power states that its market share is greater than 69 percent at all times in both the summer and winter seasons and is as high as 77 percent in the winter season. The HHI is well above 2500 in all seasons, ranging from 3321 in the shoulder off-peak to 6116 in the winter super-peak and above 4491 in all but the shoulder off-peak period. Duke Power also states that it is not a pivotal supplier.

33. The Commission finds that in all ten of the season/load conditions examined under the economic capacity measure of the DPT, Duke Power's market share range is between 55.4 percent and 77.6 percent and that the HHI market concentration statistic exceeds 3000 in all seasons and load periods. In other words, Duke Power's DPT results under the economic capacity measure indicate that it owns approximately two-thirds of the generation in the Duke Power control area and that it is a highly concentrated market.³⁷

34. Duke Power did not properly perform the pivotal supplier analysis based on the economic capacity measure as required by the April 14 Order. The April 14 Order states that the applicant will be considered pivotal if the sum of the competing suppliers'

MWh. Moreover, system lambdas in summer are always below \$30 per MWh.

³⁵ 18 C.F.R. § 33.3(d)(6) (2004).

³⁶ See 18 C.F.R. § 35.10b and the EQR page on the FERC website <http://www.ferc.gov/docs-filing/eqr.asp>.

³⁷ The U.S. Department of Justice defines a highly concentrated market as one for which the HHI equals 1800 or more. U.S. Department of Justice & Federal Trade Commission, *Horizontal Merger Guidelines* § 4.15, 57 Fed. Reg. 41,552 (1992), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104.

economic capacity is less than the load level (plus a reserve requirement) for the relevant period.³⁸ However, Duke Power's pivotal supplier analysis using economic capacity is incorrectly calculated using wholesale market load, not total control area load. The competing suppliers' economic capacity is no more than 6,590 MW.³⁹ The sum of Duke control area load is no less than 8,754 MW in all seasons and load periods.⁴⁰ This means Duke is a pivotal supplier in all seasons and load periods.

Available Economic Capacity

35. Duke Power's DPT for available economic capacity indicates that while Duke Power claims that it is not a pivotal supplier, Duke Power's market share is high in most seasons. In the entire winter season, Duke Power's market share exceeds 50 percent, ranging from 53 percent to 61 percent. In the summer peak and off-peak periods, Duke Power's market share is about 41 percent with shares of 30 and 26 percent in the summer extreme peak and summer super peak periods, respectively. In the shoulder season, Duke Power's market share exceeds 35 percent in the peak periods, ranging from 35 percent to 38 percent. The only season where market share is below 20 percent is in the shoulder off-peak season and is about 2.4 percent. The HHI is greater than 2500 for the entire winter season, ranging from 3187 to 3965, approximately 2100 in the summer peak and off-peak periods, but less than 2500 for all other seasons.

Conclusion

36. The Commission finds that in all ten of the season/load conditions examined under the economic capacity measure of the DPT, Duke Power is pivotal, possesses market shares that range between 55.4 and 77.6 percent, and the HHI market concentration statistic exceeds 3300 in all seasons/load conditions and is above 5000 in six of the ten season/load conditions.

37. The Commission further finds that under the available economic capacity measure of the DPT, Duke Power possesses a market share in excess of 25 percent in all season/load conditions except the shoulder off-peak period. Further, the HHI exceeds 3000 in the winter periods.

³⁸ April 14 Order, 107 FERC ¶ 61,018 at P 108.

³⁹ February 14 filing, Exhibit DUK-14.

⁴⁰ *Id.* at Exhibit DUK-16.

Duke Power's Alternative Data

38. To rebut the presumption that it has market power, Duke Power submitted in the August 11 filing uncommitted load data, transmission access and congestion data, a comparison of the prices of Duke Bus Sales and directly comparable “off system sales” and “closely comparable” off system sales, and the results from request for proposals (RFPs). According to Duke Power, this information confirms the absence of evidence of market power and confirms that Duke Power does not play a dominant role in the short or long-term markets for the following reasons:

- (1) there is a relatively small amount of wholesale load in the Duke Power control area compared to the overall level of supply in the control area;
- (2) Duke Power does not own or control a substantial amount of temporarily excess generation in relation to the size of its own peak load, and thus is limited in the amount of firm long-term power it can sell from its own resources to load-serving entities (LSE)
- (3) the largest LSEs in the control area own a share of the Catawba Nuclear Generating Station which is a base load resource that provides them access to very low-cost energy; and
- (4) Duke Power's transmission system is generally not constrained.

Uncommitted Load

39. Duke Power argues that in every season and under every type of load condition, it has no ability to exercise market power because the uncommitted load that is shopping for supply can be met at least four times over by competitive, available generation not owned by Duke Power.⁴¹ Duke Power argues that this competitive supply would undermine any theoretical incentive for it to economically withhold generation to raise market prices.⁴² In the August 11 filing, Duke Power presents data indicating that wholesale customer load, calculated as the difference between Duke Power control area peak load and Duke Power peak load, is less than 2500 MW at peak relative to about 11,000 to 14,000 of seasonal uncommitted supply in the Duke Power control area, as calculated in the market share analysis.⁴³

⁴¹ February 14 filing, Transmittal Letter at 1.

⁴² February 14 filing, Exhibit DUK-13 at 2.

⁴³ August 17 filing, Exhibit DUK-1(Revised) at 17-18.

40. Duke Power refined this information in the November 24 data response by narrowing the wholesale load to what it calls the Non-Requirements LSEs that shop for power in 2003.⁴⁴ Duke does not provide the MWs of load of these entities but asserts that less than 25 percent of the total loads of these customers are supplied by the “market.”⁴⁵

41. Duke Power further expands this argument in the February 14 filing by supplying computations of uncommitted load for every time period required to be analyzed by the DPT.⁴⁶ Applying the data from the available economic capacity analysis, Duke Power concludes that there is more than sufficient competing supply that is economic and deliverable into the Duke Power control area to serve demand from wholesale customers located within the control area.⁴⁷ In the context of the available economic capacity analysis, Duke Power submits that on average, less than 100 MW of wholesale load is seeking supply.⁴⁸ According to Duke Power, the uncommitted load can be served without imports except in summer and shoulder period peak hours.⁴⁹

42. Duke Power’s “uncommitted load” data does not provide historical sales data and analysis as contemplated by the April 14 Order and July 8 Order. Indeed, the uncommitted load information is not based on historical sales data nor on Duke Power’s

⁴⁴ Duke Power’s November 24, 2004, supplemental response to the Commission’s deficiency letter issued on October 9, 2004. at 9.

⁴⁵ *Id.* at 10.

⁴⁶ Duke Power refined the data to include a Catawba Co-owner previously excluded and revised uncommitted load to 2722 MW at peak demand and 1196 MW in off-peak periods. Duke Power asserts that this wholesale load can largely be served directly from the output of the wholesale customers’ ownership interest in Catawba, with the remaining wholesale load ranging from zero in the off-peak periods to 1035 MW at the summer super peak. Uncommitted supply has also been refined; in particular, merchant generation is down from 2700 MW in the August 11 filing to 716 MW estimated to be economic in the DPT.

⁴⁷ February 14 filing, Exhibit DUK-13 at 2.

⁴⁸ *Id.* at 5.

⁴⁹ February 14 filing, Transmittal Letter and Exhibit DUK-13, Table 7.

shares of those historical sales. It is instead an extension of the pivotal supplier analysis, which does not present new information for consideration. However, even assuming that this type of data was consistent with the April 14 Order and July 8 Order, we cannot rely on the data presented by Duke Power because it is flawed.

43. The criteria used by Duke Power for identifying a “shopping” customer are not clearly defined and are inconsistently applied to customers who have the option to competitively procure wholesale power. It appears that customers who have gone to other suppliers for all or a portion of their requirements are “shopping,” whereas those who elected to stay with Duke Power in 2003 are “committed.” However, this approach is not fully documented and appears to have been inconsistently applied. Further, it fails to accurately represent the purchasing position of customers in the control area. For example:

- Duke Power’s data includes Rate Schedule 10-A customers in native load that are not “shopping” at wholesale and not part of the uncommitted load calculation. However, according to other sections of Duke Power’s filing, Rate Schedule 10-A has been unbundled since 1996, and customers who elect to take service under it have an annual renewal provision. Further, the current schedule will expire on December 31, 2006, and each party has a mutual right of cancellation by providing at least twelve months notice in advance of December 31, 2006. Nevertheless, Duke Power states that “the 10-A Customers have chosen to remain as full requirements customers of Duke Power. Duke Power classifies these customers as part of its native load.”⁵⁰ Based on the evidence before us, these customers appear to have the option to shop.
- South Carolina Electric & Gas Company (SCE&G) terminated its 10-A service effective December 31, 2003⁵¹ and was serving its own load at the time the November 24 data response was prepared. However, Duke Power’s uncommitted load calculation includes SCE&G load in native load.

⁵⁰ November 24, 2004, supplemental response to the Commission’s deficiency letter issued on October 9, 2004 at 9 n. 4.

⁵¹ *Id.*

- Although DUK-19 (Revised) states at page 17 that Catawba Co-owner PMPA is a wholesale customer, it was treated as native load in 2004 filings because it “will begin to shop for power effective 2006, but in 2003, obtained any power above its Catawba-served needs from Duke Power.”⁵² However, the August 11 filing indicates that PMPA had already conducted a RFP by the time of the filing and awarded a contract for service beginning in 2006. The February 14 filing appears to have corrected this misclassification where PMPA was instead included as part of the wholesale customers’ load.⁵³ Seneca (dynamically controlled) was included as a shopping wholesale customer in the August 11 filing but does not appear to be classified as such in the February 14 filing.⁵⁴

44. Further, Duke Power’s uncommitted load analysis, by focusing only on activity in short-term markets, does not reflect other information provided by Duke Power that during the same period of time customers were in the market for intermediate and long-term power. Indeed, the information that Duke Power has submitted regarding RFPs indicates that there is demand for intermediate and long-term wholesale power in the Duke Power control area. In particular, the RFP activity indicates that the Catawba Co-owners have significant demand above their Catawba entitlements and conducted RFPs to purchase additional supplies. Further, with regard to 10-A Customers, Duke Power states that it knows of no reason these customers could not successfully shop for long-term full requirements service from other suppliers.⁵⁵

45. The result of the uncommitted load analysis, that there is sufficient non-Duke Power capacity to serve wholesale load, is largely dependent on imports. Duke Power does not document or make a showing that the uncommitted supply it asserts could be imported is in fact available in the first-tier control areas.

⁵² *Id.*

⁵³ February 14 filing, Exhibit DUK-13 at 5 n. 8.

⁵⁴ *Id.* at 5.

⁵⁵ November 24, 2004, supplemental response to the Commission’s deficiency letter issued on October 9, 2004 at page 8.

46. Finally, Duke Power's analysis indicates that Duke Power controls from 26 to 61 percent of the available economic capacity in the Duke Power control area in each of the time/load periods examined.⁵⁶

47. Conceptually, Duke Power's uncommitted load analysis suggests that customers should rely on a market where the dominant firm does not participate. Duke Power has indicated that it has not responded to RFPs where it was the supplier potentially being replaced.⁵⁷ NCEMC has raised concern that this policy deprives it of a qualified bidder in its RFPs.

48. In short, Duke Power's uncommitted load approach is not properly documented, appears to be inconsistently applied, rests on implausible assumptions, fails to accurately represent the purchasing position of customers, suggests untenable market behavior, and is inconsistent with the actual historical sales data reported by Duke Power in its EQR. Therefore, based on the foregoing, the Commission cannot rely upon this analysis.

Duke Power's Position in Short-term and Long-term Sales

49. In Duke Power's February 14 filing, it identifies certain LSEs as currently shopping for power, and they are identified as the Non-Requirement LSEs. Duke Power then continues to attempt to identify the 2003 inbound schedules sinking at each LSE. Duke Power, however, does not specify the exact methodology used to determine how its transmission records were used to "generally determine" the location from where each purchase was made. Duke Power shows that, of these Non-Requirement LSEs' purchases, Duke Power had sold roughly four percent of the total for 2003, with no more than 11 percent to any one LSE.

50. Notwithstanding the lack of clarity regarding Duke Power's methodology in determining its percentage of short run sales to these LSEs, we do not believe that Duke Power presented an accurate picture of the market in its control area. As discussed with regard to Duke Power's uncommitted load analysis, excluding all currently contracted load is not an accurate description of the wholesale market as these loads may want to replace more expensive generation that they own or have contracted for with cheaper

⁵⁶ February 14 filing, Exhibit DUK-17 at line N. Actual sales transactions in the Duke Power control area as reported by Duke Power and other sellers in their EQRs indicate that Duke Power sold approximately 55 percent of wholesale sales during 2004.

⁵⁷ August 11 filing at 10 n 28.

available generation. Furthermore, as these long-term contracts expire, or if Duke Power's contracts are terminated on relatively short notice, as Duke Power describes can happen for the 10-A customers in particular, these customers should be included as part of the relevant market.⁵⁸

51. In the February 14 filing, as part of its historical data, Duke Power states that its long-term wholesale market is similar to its presence in the short-term market. Duke Power further states that it serves 300 MW of full requirements load to customers that voluntarily renewed their agreements after the advent of open access transmission in Order No. 888. The Catawba Co-owners and other wholesale customers have contracts with suppliers such as Dynegy, Inc., Southern Company, Progress Energy Carolinas, Progress Ventures, SCE&G, and Southeastern Power Administration (SEPA) to supplement their ownership interest in Catawba. These suppliers were chosen through RFPs, of which Duke Power states that it bid in 8 of the 11 RFPs and only won 2 of them, indicating that there is sufficient transmission capability available to import non-Duke Power from outside the control area.

52. NCEMC argues that Duke Power has painted a picture of a robustly competitive market, powered largely by economic access to large amounts of off-system capacity, which does not square with NCEMC's experience. NCEMC further states that the fact that Duke Power has not supplied NCEMC's need for additional capacity since 2001 does not mean that Duke Power lacks market power within its control area. Instead, it means that for four years since NCEMC terminated partial requirements purchases from Duke Power, Duke Power has not submitted competitive bids in response to NCEMC's RFPs. NCEMC's concern is that the largest supplier within the control area is in the best position to provide competitive power supply yet has shown little interest in doing so, while the transmission interface limitations on adjacent systems limit the ability to acquire resources from first-tier suppliers.

53. NCEMC states that the Commission's focus should be on whether the structure of the market will permit the robust competition necessary to produce just and reasonable wholesale prices without regulatory intervention.

⁵⁸ Duke Power states that it serves eight full requirement LSEs under its wholesale rate schedule 10-A. These entities are served at cost-based rates and their total aggregate load is approximately 300 MW, all of which is in the Duke Power control area.

54. In its answer to NCEMC's protest concerning RFPs, Duke Power states that in the August 11 filing, it did bid to provide power in each of the two RFPs that NCEMC has issued in the past three years. Duke Power further states that the fact that other parties located outside the Duke Power control area supplied power at terms presumably more advantageous to NCEMC does not indicate that Duke Power has market power. Duke Power continues that this rather confirms that wholesale customers have economic alternatives and that they can obtain sufficient transmission service to deliver this power into and within the Duke Power control area.

55. While Duke Power states that its long-term wholesale market is similar to its presence in the short-term market, that it serves full requirements load to customers that voluntarily renewed their agreements after the advent of open access transmission, and that it has participated in 8 of the 11 RFPs and only won two of them, that does not refute the fact that Duke Power has market power in its control area. Our analysis indicates that this additional evidence is not sufficient to rebut the presumption of market power. Duke Power has not demonstrated that the information regarding contract renewals or RFPs conducted is representative of the experience with long-term contracting that is occurring in the Duke Power control area. Nor has Duke Power documented that historical sales made to the sample of full requirements customers and those conducting RFPs represents the entire long-term market that is "shopping," or is even a representative sample. Also, similar to our analysis of Duke Power's short-term data, we are not convinced that Duke Power has accounted for all uncommitted load in its analysis of the long-term market. Furthermore, Duke Power's information portraying it as a relatively small participant in short-term and long-term markets is contrary to the information reported in its EQRs, which indicates that during 2004, Duke Power made 55 percent of the wholesale sales in the Duke Power control area. Our analysis indicates that Duke Power's additional evidence with regard to short-term and long-term sales is not sufficient to rebut the presumption of market power.

Availability of ATC

56. In the August 11 filing, Duke Power asserted that there was an abundance of transmission from neighboring control areas for generation in neighboring control areas to compete. In a data response filed on November 24, 2004 (November 24 data response), Duke Power provided the Base Firm ATC that was available for use by LSEs in the Duke Power control area for 2003. Duke Power also provided additional ATC data for the 12 hours when Duke Power made transactions at prices 5 percent greater than its comparable transactions. In its protest, NCEMC submitted data showing that for certain specific time periods, the ATC according to the neighboring regions was significantly lower. For example, NCEMC showed that Duke Power reported 2,222 MW of ATC for all months into Duke Power's control area, while the Southern Companies projected no

more than 702 MW of ATC in any hour. For any area to area ATC, a requestor of transmission service must obtain approval from both the sending and receiving area. For example if Southern Companies approve up to 702 MW of ATC to transfer and Duke Power approves up to 2,222 MW of ATC to transfer, then the most transmission service available to the customer on the Southern Companies-Duke Power tie is 702 MW. Accordingly, we agree with NCEMC that Duke Power has presented an incomplete picture of the availability of transmission capability in the Duke Power control area.

Prices of Duke Bus Sales

57. In the August 11 filing, Duke Power compared the prices for Duke Power's control area sales versus off-system sales. Duke Power's analysis attempted to show that since Duke Power was selling power nearly at the same price out of the control area as inside of the control area, it was not exercising market power. While the exact methodology of identifying comparable sales is unclear, Duke Power identified 40 out of 560 transactions where the price sold to the Duke Bus was more than 5 percent greater than the comparable sales. Duke Power further showed that 12 of the 40 identified sales had a price difference above \$10 compared to the comparable off-system sales.

58. Duke Power's argument that similar prices for sales within the control area and sales off-system are evidence that it was not exercising market power is of little value in assessing its potential to exercise market power under the Commission's generation market power analysis because it only serves to suggest that, if Duke Power has market power in generation, Duke Power did not act to capitalize on that market power during the time periods studied. In addition, we note that Duke Power's analysis that it did not exert market power in past periods likewise is of little use because such an argument does not address the Commission's concern as to whether a utility has the ability to exercise generation market power. Before authorizing an applicant to transact at market-based rates, the Commission must determine whether an applicant has the ability to exercise market power. Historically, the Commission's market power analysis has assessed the ability or potential of the applicant to exercise market power by examining the applicant's control of generation capacity and the generation controlled by other suppliers in the relevant market. The Commission will also consider the applicant's relative shares of historical sales as evidence of actual market conditions and the applicant's ability to exercise market power. To the extent that the Commission determines that an applicant has the ability to exercise market power, it is incumbent upon the Commission to deny market-based rate authority or impose mitigation to guard against the potential to exercise that market power.

Commission Conclusion

59. Duke Power's arguments do not rebut the results of the DPT analysis. As mentioned above, Duke Power has presented information showing that it fails the Commission's wholesale market share screen for each of the four seasons considered in the Duke Power control area. Duke Power argues that the Commission's wholesale market share screen would most likely overstate an applicant's share of off-peak uncommitted capacity in its own control area because it ignores the level of third-party loads during off-peak periods and the numbers of competitors available to serve those loads. Duke Power states that a more detailed analysis of the actual market conditions in its control area is required. However, after further review of the more detailed analysis of the actual market conditions in Duke Power's control area, provided through historical data, other information Duke Power considers relevant, and its DPT filed on February, 14, 2005, we find that Duke Power has market power in its control area.

60. Based on the results of the wholesale market share screen, the historical data, DPT for available economic capacity and economic capacity, and the HHI test, we find that Duke Power has generation market power in the Duke Power control area. In this regard, the April 14 Order stated, "...we will revoke the market-based rate authority in all geographic markets where an applicant is found to have market power." "Such applicants will be required to adopt some form of cost-based rates or other mitigation the applicant proposes and the Commission accepts."⁵⁹ We further clarified that, "[w]e will also allow applicants to propose case-specific mitigation tailored to their particular circumstances that eliminates the ability to exercise market power, or adopt cost-based rates such as the default rates herein."⁶⁰ However, in the instant proceeding, Duke Power has not availed itself of the opportunity of proposing tailored mitigation. Accordingly, the Commission has before it only the default cost-based rates as defined in the April 14 Order.

61. Because we find that Duke Power has market power in the Duke Power control area, the rates authorized by Duke Power's existing market-based rate tariff are not just and reasonable as they relate to sales in the Duke Power control area. To mitigate the potential for the exercise of generation market power in the Duke Power control area, we will direct Duke Power to submit a compliance filing to revise its market-based rate tariff to prohibit sales at market-based rates in the Duke Power control area and to provide for

⁵⁹ April 14 Order, 107 FERC ¶ 61,018 at P 150. The applicant has the option of withdrawing its market-based rate request in whole or in part.

⁶⁰ *Id.* at P 147.

the default cost-based rates specified in the April 14 Order⁶¹ for the Duke Power control area. Accordingly, Duke Power is directed to file, within thirty days of the date of this order, a revised market-based rate tariff prohibiting sales at market-based rates in the Duke Power control area and providing for the default cost-based rates specified in the April 14 Order to be effective as of the refund effective date of this 206 proceeding. In addition, Duke Power is directed to provide cost support for these rates. In particular, Duke Power is directed to provide the formulas and methodology according to which it intends to calculate incremental costs, as discussed below. Finally, Duke Power is directed to provide a refund report.⁶² In this regard, the default rates will be considered final rates and not subject to refund for purposes of calculating refund obligations.

62. As stated in the April 14 Order, default cost-based rates are as follows: (1) sales of power of one week or less will be priced at the applicant's incremental cost plus a 10 percent adder; (2) sales of power of more than one week but less than one year will be priced at an embedded cost "up to" rate reflecting the costs of the unit(s) expected to provide the service; and (3) sales of power for more than one year will be priced on an embedded cost-of-service basis and each such contract will be filed with the Commission for review and approved prior to the commencement of service.

63. The compliance filing directed herein is without prejudice to Duke Power proposing, on a prospective basis, case-specific mitigation tailored to its particular circumstances that eliminates its ability to exercise market power.

64. The compliance filing directed herein is also without prejudice to Duke Power's ability to make sales under its existing Commission-approved cost-based rate tariffs. However, to the extent that Duke Power elects to replace market-based rate sales in the Duke Power control area with cost-based rate sales pursuant to its existing cost-based rate tariffs, Duke Power is directed to so inform the Commission within 30 days of the date of issuance of this order and specify under which tariff(s) it intends to transact. Furthermore, we emphasize that the Commission has a statutory duty to ensure that

⁶¹ *Id.* at P 151-55.

⁶² As the Commission explained in the July 8 Order, "[i]n the event that the Commission makes a definitive finding of market power, revokes market-based rates and imposes cost-based rate mitigation, sales made on or after the refund effective date will be subject to refund, where the refund floor would be the default cost-based rate or the case-specific cost-based rate approved by the Commission, if any." July 8 Order, 108 FERC ¶ 61,026 at P 158.

jurisdictional rates are just and reasonable, whether cost-based or market-based, and the Commission reserves the right to investigate whether existing cost-based rates continue to be just and reasonable.

65. As we stated in the April 14 Order, where, as here, an applicant is found to have market power, we will no longer waive our otherwise applicable accounting regulations (*e.g.*, Parts 41, 101, and 141 of the Commission's regulations),⁶³ and we will not grant blanket approval for issuances of securities or assumptions of liability pursuant to Part 34 of the Commission's regulations for the applicant and its affiliates.⁶⁴

66. Duke Power must timely report to the Commission any change in status that would reflect a departure from the characteristics the Commission relied upon in granting market-based rate authority.⁶⁵ Order No. 652 requires that the change in status reporting requirement be incorporated in the market-based rate tariff of each entity authorized to make sales at market-based rates. Accordingly, Duke Power is directed, within 30 days of the date of issuance of this order, to revise its market-based rate tariff to incorporate the following provision:

[insert market-based rate seller name] must timely report to the Commission any change in status that would reflect a departure from the characteristics the Commission relied upon in granting market-based rate authority. A change in status includes, but is not limited to, each of the following: (i) ownership or control of generation or transmission facilities or inputs to electric power production other than fuel supplies, or (ii) affiliation with any entity not disclosed in the application for market-based rate authority that owns or controls generation or transmission facilities or inputs to electric power production, or affiliation with any entity that has a franchised service area. Any change in status must be filed no later than 30 days after the change in status occurs.

67. Duke Companies are directed to file an updated market power analysis within three years of the date of this order. The Commission also reserves the right to require such an analysis at any intervening time.

⁶³ April 14 Order, 107 FERC ¶ 61,018 at P 150.

⁶⁴ *Id.*

⁶⁵ *Reporting Requirement for Changes in Status for Public Utilities with Market-Based Rate Authority*, Order No. 652, 70 Fed. Reg. 8,253 (Feb. 18, 2005), FERC Stats. & Regs. ¶ 31,175 (2005).

The Commission orders:

(A) The Commission hereby revokes Duke Power's market-based rate authority in the Duke Power control area.

(B) Duke Power is directed, within 30 days of the date of this order, to revise its market-based rate tariff to prohibit sales at market-based rates in the Duke Power control area and to provide for the default cost-based rates for the Duke Power control area, as discussed in the body of the order.

(C) Duke Power is directed to file cost support, as discussed in the body of the order.

(D) Duke Power is hereby ordered to make refunds within 30 days of the date of this order, and file a refund report with the Commission within 15 days of the date refunds are made, as discussed in the body of the order.

(E) Duke Power is directed, within 30 days of the date of issuance of this order, to revise its market-based rate tariff to incorporate the change in status reporting requirement adopted in Order No. 652.

(F) Duke Companies' next updated market power analysis is due within three years of the date of this order.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.