



section 206 of the Federal Power Act (FPA)<sup>4</sup> to determine whether Shell's market-based rate authority in the CSWS balancing authority area remains just and reasonable. Although Shell also submitted a delivered price test (DPT) analysis, we find that it has failed to rebut the presumption of horizontal market power. Accordingly, we direct Shell, within 60 days of the date of issuance of this order, to (1) show cause as to why the Commission should not revoke its market-based rate authority in the CSWS balancing authority area; (2) file a mitigation proposal tailored to its particular circumstances that would eliminate its ability to exercise market power; or (3) inform the Commission that it will adopt the default mitigation set forth in the Commission's regulations or propose other cost-based rates and submit cost support for such rates.<sup>5</sup>

## **I. Background**

2. Shell states that it is a power marketer which along with its affiliates owns or controls approximately 2,161 megawatts (MW) of generation located in the SPP region. In particular, Shell notes that it is affiliated with Llano Estacado Wind, LP (Llano Estacado), which owns and operates an 80 MW wind-powered generating facility in the Southwestern balancing authority area. In addition, Shell states that it controls the output of three non-affiliated generating facilities. According to Shell, it has an agreement with Tenaska Gateway Partners, Ltd. for the energy produced by its 863 MW generating facility and an agreement with Kiowa Power Partners, LLC for the energy produced by its 1,178 MW Tenaska Kiamichi generating facility. Shell states that both the Tenaska Gateway facility and the Tenaska Kiamichi facility are dually interconnected to the CSWS balancing authority area and the Electric Reliability Council of Texas (ERCOT). Finally, in the Western balancing authority area, Shell has identified an agreement it has with Western for the electrical energy produced by Western's 40 MW electric generating Anadarko facility, located in Anadarko, Oklahoma.

3. Shell states that it is a wholly-owned indirect subsidiary of Shell Oil Company, which is a wholly-owned indirect subsidiary of Royal Dutch Shell, plc. Shell also states that neither Shell nor any of its affiliates owns, operates, or controls interests in transmission or distribution facilities in the United States, except for the limited equipment necessary to interconnect individual generating facilities to the transmission grid and distribution facilities running from the grid and serving particular production fields for oil and gas. It further states that neither it nor any of its affiliates owns or controls any inputs to electric power production, as defined in section 35.36 of the Commission's regulations, in any relevant market. In addition, it states that it is not affiliated with any franchised public utility.

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<sup>4</sup> 16 U.S.C. § 824e (2006).

<sup>5</sup> 18 C.F.R. § 35.38 (2010).

4. On March 1, 2010, Shell filed an updated market power analysis, which shows that it fails the horizontal market share screen in the CSWS balancing authority area. Shell states that transmission constraints significantly limit the amount of generation that can be delivered by the Tenaska Gateway and Tenaska Kiamichi facilities into the CSWS balancing authority area. Shell further states that when those constraints and actual historical operations are taken into account, Shell's market share falls well below the Commission's 20 percent threshold. Shell also states that, due to physical deliverability constraints and market conditions, these generating facilities are almost always dispatched into ERCOT and very rarely dispatched into the CSWS balancing authority area. For these reasons, Shell concludes that it is not possible for Shell to exercise market power in the CSWS balancing authority area.

5. On April 12, 2010, Shell filed a supplemental affidavit describing how the Tenaska Gateway and Tenaska Kiamichi generating facilities are dually interconnected with both CSWS and ERCOT. The supplemental affidavit also provided data regarding the dispatch of those facilities into ERCOT.

6. On July 9, 2010, Shell submitted a DPT to rebut the presumption of market power arising from its failure of the market share screen in the CSWS balancing authority area.

## **II. Notices and Responsive Pleadings**

7. Notice of Shell's March 1, 2010 filing was published in the *Federal Register* with interventions or protests due on or before April 30, 2010.<sup>6</sup> None was filed.

8. Notice of Shell's July 9, 2010 filing was published in the *Federal Register* with interventions or protests due on or before July 30, 2010.<sup>7</sup> None was filed.

## **III. Discussion**

9. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, horizontal and vertical market power.<sup>8</sup> As discussed below, the Commission concludes that Shell has failed to rebut the presumption of horizontal market power that is established by its failure of the market share indicative screen in the CSWS balancing authority area; thus, it may not satisfy the Commission's standards for market-based rate authority.

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<sup>6</sup> 75 Fed. Reg. 11,155 (2010). We note that on March 17, 2010, the Commission issued an errata notice extending the comment period for the March 1 Filing to April 30, 2010.

<sup>7</sup> 75 Fed. Reg. 41,843 (2010)

<sup>8</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 62, 399, 408, 440.

**A. Horizontal Market Power**

**1. Indicative Screens**

10. The Commission has adopted two indicative screens for assessing horizontal market power: the pivotal supplier screen and the wholesale market share screen.<sup>9</sup> The Commission has stated that passage of both screens establishes a rebuttable presumption that the applicant does not possess generation market power, while failure of either screen creates a rebuttable presumption that the applicant has generation market power.<sup>10</sup> The Commission has stated that an applicant that fails one or more of the indicative screens is provided with several procedural options, including the right to challenge the presumption of market power by submitting a DPT analysis or actual historical sales data, or, alternatively, sellers may accept the presumption of market power and adopt some form of cost-based mitigation.<sup>11</sup>

11. Shell prepared the pivotal supplier and wholesale market share screens for the Southwestern, Western, and CSWS balancing authority areas, consistent with the requirements of Order No. 697.<sup>12</sup> Shell's study indicates that it passes the pivotal supplier and market share screens in both the Southwestern and Western balancing authority areas.<sup>13</sup> Shell passes the pivotal supplier screen but, according to its own filed study, does not pass the wholesale market share screen in the CSWS balancing authority area, as its market share exceeds 20 percent in two seasons.

12. Shell states that when transmission constraints and actual historical operations are taken into account, Shell passes both the pivotal supplier and market share screens in the CSWS balancing authority area. It states that transmission constraints significantly limit the amount of generation that can be delivered from the Tenaska Gateway and the Tenaska Kiamichi facilities into the CSWS balancing authority and that the Commission has stated that generator operating limits should be taken into account in transmission studies.<sup>14</sup> Shell submits information from studies conducted by American Electric Power

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<sup>9</sup> *Id.* P 62.

<sup>10</sup> *Id.* P 33, 62-63.

<sup>11</sup> *Id.* P 63. The results of the DPT can be used for pivotal supplier, market share, and market concentration analyses.

<sup>12</sup> *Id.* P 231-232.

<sup>13</sup> March 1 Filing, Transmittal Letter at 4, Affidavit of Julie Solomon at 2 (Solomon Affidavit).

<sup>14</sup> *Id.*, Transmittal Letter at 4, Solomon Affidavit at 9-10 (citing *AEP Power Marketing, Inc.*, 107 FERC ¶ 61,018, *order on reh'g*, 108 FERC ¶ 61,026 (2004)).

in 2001 and 2004 that, according to Shell, indicate that the ability of the Tenaska Gateway and Tenaska Kiamichi facilities to supply the CSWS balancing authority area is limited.<sup>15</sup> It also refers to a 2008 study by SPP.<sup>16</sup> It further states that the Tenaska Gateway and Tenaska Kiamichi facilities have not been dispatched into the CSWS balancing authority area since 2006 and that only 159 MWh of the combined output of the facilities were delivered into the CSWS balancing authority area during the relevant study period.<sup>17</sup> Shell also explains that it recently tested its ability to deliver the output of the Tenaska Kiamichi facility into SPP by submitting requests for transmission service for various amounts of energy. Specifically, Shell explains that it submitted requests for one day of firm point-to-point transmission service for the following amounts: 1120, 1020, 920, and 820 MWs. Shell maintains that SPP's response to these requests indicates that even daily transmission service was not available at these levels, which, according to Shell, reflects that there are some transmission limitations for delivering energy into SPP.<sup>18</sup>

### **Commission Determination**

13. The Commission has reviewed Shell's pivotal supplier and wholesale market share screens. We find that Shell passes the pivotal supplier and wholesale market share screens in both the Southwestern and Western balancing authority areas. Accordingly, we find that Shell satisfies the Commission's requirements regarding horizontal market power in the Southwestern and Western balancing authority areas.

14. With respect to the CSWS balancing authority area, however, Shell passes the pivotal supplier screen but does not pass the wholesale market share screen during the spring and summer seasons, where its market shares were 20.3 percent and 25.8 percent, respectively. While Shell has provided evidence regarding deliverability constraints and its historical sales into the CSWS balancing authority area, this information presents

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<sup>15</sup> *Id.*, Solomon Affidavit at 9 n.18 (stating that the 2001 American Electric Power study found that Tenaska Gateway "generation into the [American Electric Power] Transmission System must not exceed 634 MW," and that the 2004 study considered the Tenaska Kiamichi facility unavailable to supply the CSWS market and only 450 MW of the Tenaska Gateway facility available to supply the CSWS market).

<sup>16</sup> *Id.* at 10 n.19 (noting that the 2008 SPP study indicated that, in a combined Entergy-SPP market, the Tenaska Frontier plant in Entergy and the Tenaska Gateway plant in SPP were limited to a combined deliverability of 300 MW because of certain transmission limits).

<sup>17</sup> *Id.*, Transmittal Letter at 4, Solomon Affidavit at 9-11, Exhibit JRS-6a.

<sup>18</sup> July 9 Filing, Supplemental Affidavit of Julie Solomon at 4-5.

issues that should be considered as part of the investigation initiated below. As part of the investigation instituted below, Shell may provide additional historical sales and transmission data, which we will consider, along with the evidence already submitted. Accordingly, we turn to Shell's DPT for the CSWS balancing authority area.

## 2. Delivered Price Test

15. As the Commission has previously explained, the DPT identifies potential suppliers based on market prices, input costs, and transmission availability, and calculates each supplier's economic capacity and available economic capacity<sup>19</sup> for each season/load period.<sup>20</sup> Under the DPT, applicants must also calculate market concentration using the Hirschman-Herfindahl Index (HHI).<sup>21</sup> An HHI of less than 2,500 in the relevant market for all season/load periods, in combination with a demonstration that the applicants are not pivotal and do not possess more than a 20 percent market share in any of the season/load periods would constitute a showing of a lack of market power, absent compelling contrary evidence from intervenors. A detailed description of the mechanics of the DPT is provided in Order No. 697.<sup>22</sup>

16. As with our initial screens, applicants and intervenors may present evidence such as historical wholesale sales data, which may be used to calculate market shares and market concentration and to refute or support the results of the DPT. In Order No. 697, the Commission encouraged applicants to present the most complete analysis of competitive conditions in the market as the data allows.<sup>23</sup>

17. Shell's DPT analysis for the CSWS balancing authority area indicates that it is not pivotal in any season/load period using either the economic capacity measure or the

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<sup>19</sup> "Economic capacity" is the total generation capacity of a potential supplier that can compete in the destination market, given its costs and transmission availability. "Available economic capacity" is derived by subtracting each potential supplier's native load obligation from its total capacity and adjusting transmission availability accordingly. See Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 96 n.78.

<sup>20</sup> Super-peak, peak, and off-peak, for winter, shoulder, and summer periods and an additional highest super-peak for the summer.

<sup>21</sup> 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,  $HHI = (20)^2 + (20)^2 + (20)^2 + (20)^2 + (20)^2 = 400 + 400 + 400 + 400 + 400 = 2,000$ .

<sup>22</sup> FERC Stats. & Regs. ¶ 31,252 at P 104-117.

<sup>23</sup> *Id.* P 111.

available economic capacity measure.<sup>24</sup> When the economic capacity measure is used, Shell passes the market share screen in all seasons/load periods, but fails the market concentration analysis in eight out of ten seasons/load periods with HHIs ranging from 2,741 to 4,277. When the available economic capacity measure is used, however, Shell fails the market share analysis in seven seasons/load periods with market shares ranging from 29.3 percent to 37 percent but passes the market concentration analysis in all seasons/load periods.<sup>25</sup>

18. Shell argues that its DPT demonstrates that it does not have the ability to exercise market power in the CSWS balancing authority area. It contends that the high market concentration using the economic capacity measure is driven by American Electric Power's high market share, which is typical for an incumbent vertically-integrated utility in its own balancing authority area.<sup>26</sup> Shell further contends that its market shares using the available economic capacity measure are not dispositive and that the Commission has approved market-based rates where the applicant's market share in a DPT exceeded 20 percent in certain season/load conditions.<sup>27</sup> Shell also notes that in those periods where its market share exceeds 20 percent, the HHIs are generally less than 1,700.<sup>28</sup>

19. Shell also submitted historical sales data to rebut the results of the indicative screens for the CSWS balancing authority area. Specifically, Shell submitted data from its Electric Quarterly Reports indicating that Shell only made 125 MWh of sales into the CSWS balancing authority area during the study period and that the HHI for "actual historical short-term sales" during this period was approximately 2,000. Shell argues that this data demonstrates that Shell did not exercise market power in the CSWS balancing authority area.<sup>29</sup>

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<sup>24</sup> July 9 Filing, Supplemental Affidavit of Julie Solomon at 2 (Supplemental Affidavit).

<sup>25</sup> *Id.*, Exhibit JRS-1.

<sup>26</sup> *Id.*, Supplemental Affidavit at 10.

<sup>27</sup> *Id.* at 10-11 (citing *Kansas City Power and Light Co.*, 113 FERC ¶ 61,074, at P 26,31 (2005); *PPL Montana, LLC*, 115 FERC ¶ 61,204, at P 42 (2006); *PacifiCorp*, 115 FERC ¶ 61,349, at P 29-30, 32-34 (2006); *Tampa Elec. Co.*, 117 FERC ¶ 61,311, at P 26-27 (2006)).

<sup>28</sup> *Id.*, Supplemental Affidavit at 11.

<sup>29</sup> *Id.* at 12.

### Commission Determination

20. After weighing all of the relevant evidence, the Commission finds that the aforementioned screen failures merit further investigation into whether or not Shell has market power in the CSWS balancing authority area.

21. The Commission has previously noted that the DPT does not function like the initial screens – i.e., failure of either the economic capacity or available economic capacity analyses does not result in an automatic failure of the test as a whole. Neither measure is definitive; the Commission weighs the results of both the economic capacity and available economic capacity analyses and considers the arguments of the parties.<sup>30</sup>

22. The Commission has recognized that not all generation capacity is available all of the time to compete in wholesale markets and that some accounting for native load requirements is warranted.<sup>31</sup> In the DPT analysis, available economic capacity accounts for native load requirements. As noted above, using the available economic capacity measure, Shell passes the pivotal supplier and market concentration analyses in all seasons/load periods, but fails the market share analysis in seven out of ten seasons/load periods. Specifically, its market share in the CSWS balancing authority area is 29.7 percent in the shoulder peak period, 30.7 in the shoulder super-peak period, 32 percent in the winter peak period, 29.3 percent in the winter super-peak period, 31.9 percent in both the summer peak and super-peak 2 periods, and 37 percent in the summer super-peak 1 period.

23. While available economic capacity reflects native load obligations when assessing the potential for horizontal market power, a clear distinction between generation serving native load and generation competing for wholesale load is not easily made. The Commission therefore also considers economic capacity in assessing horizontal market power.<sup>32</sup> Using the economic capacity measure, Shell passes the pivotal supplier and market share analyses in every season/load period; however, its HHIs exceed 2,500 in eight out of ten seasons/load periods.

24. In summary, after weighing all of the relevant evidence, the Commission concludes that, based on Shell's DPT, Shell may have the ability to exercise market power in the CSWS balancing authority area. Therefore, we will institute a proceeding in Docket No. EL10-83-000, pursuant to section 206 of the FPA, to determine whether

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<sup>30</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 13, 112 (stating that the Commission will weigh both available economic capacity and economic capacity).

<sup>31</sup> See, e.g., *Dogwood Energy LLC*, 132 FERC ¶ 61,120, at P 21 (2010) (*Dogwood*); *Sierra Pac. Power Co.*, 126 FERC ¶ 61,283, at P 21 (2009) (*Sierra*).

<sup>32</sup> *Dogwood*, 132 FERC ¶ 61,120 at P 22; *Sierra*, 126 FERC ¶ 61,283 at P 22.

Shell's market-based rate authority for the CSWS balancing authority area remains just and reasonable. Under the section 206 proceeding established herein, Shell must show cause, within 60 days of the date of issuance of this order, as to why the Commission should not revoke its market-based rate authority in the CSWS balancing authority area. In this regard Shell may present additional evidence such as historical sales and transmission data to rebut the Commission's finding that it has the ability to exercise market power in the CSWS balancing authority area.<sup>33</sup> As discussed above, the Commission will further examine, in conjunction with other evidence submitted in the section 206 investigation instituted below, the evidence Shell has submitted regarding deliverability constraints and historical sales in the CSWS balancing authority area. In the alternative, Shell may (1) file a mitigation proposal tailored to its particular circumstances that would eliminate the ability to exercise market power; or (2) inform the Commission that it will adopt the Commission's default cost-based rates or propose other cost-based rates and submit cost support for such rates.

25. In cases where, as here, the Commission institutes a section 206 investigation on its own motion, the Commission is required to establish a refund effective date that is no earlier than publication of notice of the Commission's initiation of its investigation in the *Federal Register*, and no later than five months subsequent to that date. In order to give maximum protection to customers, and consistent with our precedent,<sup>34</sup> we will establish a refund effective date at the earliest date allowed. This date will be the date on which notice of our investigation in this proceeding is published in the *Federal Register*.

26. In addition, section 206 requires that, if no final decision has been rendered by the earlier of the refund effective date or the 180-day period commencing upon initiation of a proceeding pursuant to this section, the Commission shall state the reasons why it failed to do so and shall state its best estimate as to when it reasonably expects to make such a decision. We expect that we should be able to render a decision within five months of the date that Shell submits the filing ordered below, or April 29, 2011.

## **B. Vertical Market Power**

27. In cases where a public utility, or any of its affiliates, owns, operates, or controls transmission facilities, the Commission requires that there be a Commission-approved open access transmission tariff on file before granting that utility or affiliate market-based rate authorization.<sup>35</sup>

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<sup>33</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 117.

<sup>34</sup> See, e.g., *Canal Electric Co.*, 46 FERC ¶ 61,153, *order on reh'g*, 47 FERC ¶ 61,275 (1989).

<sup>35</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 408.

28. Shell states that neither it nor its affiliates own, operate, or control transmission facilities in the United States, except for the limited equipment necessary to interconnect individual generating facilities to the transmission grid and distribution facilities running from the grid and serving particular production fields for oil and gas, and therefore, do not have transmission market power.

29. The Commission also considers a seller's ability to erect other barriers to entry as part of the vertical market power analysis.<sup>36</sup> The Commission requires a seller to provide a description of its ownership or control of, or affiliation with an entity that owns or controls, intrastate natural gas transportation, storage, or distribution facilities; sites for generation capacity development; and physical coal supply sources and ownership of or control over who may access transportation of coal supplies (collectively, inputs to electric power production).<sup>37</sup> The Commission adopted a rebuttable presumption that the ownership or control of, or affiliation with any entity that owns or controls, inputs to electric power production does not allow a seller to raise entry barriers but will allow intervenors to demonstrate otherwise.<sup>38</sup>

30. Shell states that neither it nor its affiliates in the United States owns or controls any inputs to electric power production in the relevant markets.<sup>39</sup>

31. The Commission also requires sellers to make an affirmative statement that they have not erected barriers to entry into the relevant market and will not erect barriers to entry into the relevant market.<sup>40</sup> Shell affirmatively states that neither it nor its affiliates have erected barriers to entry in the relevant markets and will not erect barriers to entry in the relevant markets.<sup>41</sup>

32. Shell included an asset appendix as required by Order No. 697.<sup>42</sup>

33. Based on Shell's representations, we find that it satisfies the Commission's requirements for market based rate authority regarding vertical market power.

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<sup>36</sup> *Id.* P 440.

<sup>37</sup> *Id.* P 448; Order No. 697-A, FERC Stats. & Regs. ¶ 31,268 at P 176; Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 at P 38.

<sup>38</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 446.

<sup>39</sup> March 1 Filing, Transmittal Letter at 4.

<sup>40</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 448.

<sup>41</sup> March 1 Filing, Transmittal Letter at 5.

<sup>42</sup> Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 894-895.

The Commission orders:

(A) Shell's updated market power analysis for the Southwestern and Western balancing authority areas is accepted for filing.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Commission by section 402(a) of the Department of Energy Organization Act and by the FPA, particularly section 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the FPA (18 C.F.R., Chapter I), the Commission hereby institutes a proceeding in Docket No. EL10-83-000 concerning the justness and reasonableness of Shell's market-based rates, as discussed in the body of this order.

(C) The Secretary shall promptly publish in the *Federal Register* a notice of the Commission's initiation of the proceeding under section 206 of the FPA in Docket No. EL10-83-000.

(D) The refund effective date in Docket No. EL10-83-000, established pursuant to section 206(b) of the FPA, shall be the date of publication in the *Federal Register* of the notice discussed in Ordering Paragraph (B) above.

(E) For the CSWS balancing authority area, Shell is directed, within 60 days from the date of issuance of this order, to (1) show cause as to why the Commission should not revoke its market-based rate authority in the CSWS balancing authority area; (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 Commission's default cost-based rates or propose other cost-based rates and submit cost support for such rates.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.