

124 FERC ¶ 61,239
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Sudeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Oklahoma Gas and Electric Company
Redbud Energy LP

Docket No. EC08-58-000

ORDER CONDITIONALLY AUTHORIZING DISPOSITION
OF JURISDICTIONAL FACILITIES

(Issued September 16, 2008)

1. Oklahoma Gas and Electric Company (OG&E) and Redbud Energy LP (Redbud Energy) (collectively, Applicants) request Commission authorization for a disposition of jurisdictional facilities (Transaction) pursuant to section 203 of the Federal Power Act (FPA)¹ resulting from the sale of 100 percent of the ownership interests in a generation facility (Facility) from Redbud Energy to OG&E. We have reviewed the Transaction under the Merger Policy Statement² and will authorize it as consistent with the public interest, subject to the condition discussed below to prevent increased market power.

¹ 16 U.S.C. § 824b (2006).

² See *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, FERC Stats. & Regs. ¶ 31,044 (1996), *reconsideration denied*, Order No. 592-A, 79 FERC ¶ 61,321 (1997) (Merger Policy Statement); see also *Revised Filing Requirements Under Part 33 of the Commission's Regulations*, Order No. 642, FERC Stats. & Regs. ¶ 31,111 (2000), *order on reh'g*, Order No. 642-A, 94 FERC ¶ 61,289 (2001) (Merger Filing Requirements); *Transactions Subject to FPA Section 203*, Order No. 669, FERC Stats. & Regs. ¶ 31,200 (2006), *order on reh'g*, Order No. 669-A, FERC Stats. & Regs. ¶ 31,214, *order on reh'g*, Order No. 669-B, FERC Stats. & Regs. ¶ 31,225 (2006).

I. Background

A. Description of Applicants

1. OG&E

2. OG&E is a wholly-owned subsidiary of OGE Energy Corp (OGE Energy). It serves retail customers in Oklahoma and western Arkansas, and sells electric power at wholesale to various buyers. It is a member of the Southwest Power Pool, Inc. (SPP) and owns the transmission facilities within its service territory, which are controlled by SPP.

3. OG&E is not authorized to make sales at market-based rates in its balancing authority area, and is authorized to offer cost-based service only for transactions of one week or less. Moreover, OG&E may not make any wholesale sales (cost-based or market-based) for durations of more than one week and less than one year, and agreements for a term of one year or more require prior approval by the Commission.³ OG&E has market-based rate authority for sales in directly interconnected first-tier balancing authority areas. OG&E has authority to sell energy imbalance service into the Southwest Power Pool, Inc. Energy Imbalance Service (SPP EIS) market at market-based rates.

4. OG&E has two principal affiliates, Enogex Inc. (Enogex) and OGE Energy Resources, Inc. (OGE Marketer), that are relevant to this application. Enogex is a wholly-owned subsidiary of OGE Energy and is engaged in gathering, processing, transporting, storing and marketing natural gas and natural gas liquids. It owns and

³ Application at 30. See also Application at 7, citing *Oklahoma Gas and Electric Co.*, 114 FERC ¶ 61,297 (2006) (Order on Mitigation). The Commission conditionally accepted OG&E's proposal to mitigate the presumption of market power in the OG&E balancing authority area (OG&E had failed the wholesale market share screen for market-based rate authority in its home balancing authority area) by adopting the Commission's default cost-based rates for sales of power of one week or less, committing not to make any sales of more than one week and less than one year in the OG&E balancing authority area, and committing to seek Commission authorization prior to the commencement of any contracts for long-term sales. The Commission further directed OG&E to file cost-based rate provisions for sales of power of one week or less in tariffs separate from its market-based rate tariffs. In a subsequent order, the Commission accepted OG&E's cost-based rate tariffs and directed further revisions to OG&E's market-based rate tariffs in compliance with the Order on Mitigation. *Oklahoma Gas and Electric Co.*, 123 FERC ¶ 61,012 (2008) (Order on Rehearing and Compliance).

operates approximately 8,200 miles of intrastate gathering and transportation pipelines in Oklahoma. It is subject to the Commission's regulation pursuant to section 311 of the Natural Gas Policy Act of 1978.⁴

5. OGE Marketer is a wholly-owned subsidiary of OGE Energy that markets energy products, including natural gas and electric power, and provides energy-related services. It does not own or control any generating resources; however, it is authorized to make wholesale power sales at market-based rates in first-tier markets. It is subject to the same terms as is OG&E regarding wholesale sales within OG&E's balancing authority area.⁵

2. Redbud Energy

6. Redbud Energy is a limited partnership created for the sole purpose of owning an interest in the Facility. It is authorized by the Commission to make wholesale sales at market-based rates.⁶ Redbud Energy only owns the limited transmission facilities necessary to interconnect the Facility to the OG&E transmission grid. All of the partnership interests in Redbud Energy are owned by Redbud Energy I, LLC, Redbud Energy II, LLC, and Redbud Energy III, LLC, each of which is an indirect, wholly-owned subsidiary of Kelson Holdings.

7. Two-thirds of the interests in Kelson Holdings are owned by Harbinger Capital Partners Master Fund I, Ltd. (Harbinger Capital), and the remaining one-third interest is owned by Harbinger Capital Partners Special Situations Fund LP (Special Situations Fund). Harbinger Capital and Special Situations Fund are separate investment funds that invest primarily in distressed/high-yield debt securities, "special situation" equities, and private loans and notes, including equity and debt securities of entities owning generation assets. The Commission has granted blanket authorization under FPA section 203 to Redbud Energy and the other public utility subsidiaries of Kelson Holdings for the transfer of up to 45 percent of Kelson Holdings' voting securities by a private placement.⁷

8. The Facility is a 1,195 megawatt (MW) (summer rating) combined-cycle electric generating facility located in Luther, Oklahoma. The Facility is interconnected with the

⁴ 15 U.S.C. § 3371 (2000).

⁵ Application at 8, *citing* Order on Compliance Filing, 114 FERC ¶ 61,297.

⁶ Application at 8.

⁷ *Id.* at 9, *citing* *Cottonwood Energy Company, LP*, 121 FERC ¶ 62,184 (2007). Private placement is the sale of a bond or other security directly to a limited number of investors.

OG&E transmission system. The jurisdictional facilities being transferred are the transmission facilities used to interconnect the generation units to the OG&E transmission system, generation step-up transformers, Redbud Energy's market-based rate tariff, and associated books and records.⁸

B. Description of the Transaction

9. Under the Purchase and Sale Agreement, OG&E will acquire the partnership interests in Redbud Energy from Redbud Energy I, LLC, Redbud Energy II, LLC, and Redbud Energy III, LLC. Immediately thereafter, OG&E will dissolve Redbud Energy and sell undivided interests of 36 percent and 13 percent in the Facility's assets to Oklahoma Municipal Power Authority (Oklahoma Municipal Power) and Grand River Dam Authority (Grand River Dam), respectively, under the Asset Purchase Agreement, while OG&E will retain a 51 percent interest. OG&E will operate the Facility on behalf of the joint owners. Each owner will schedule the dispatch of its share of the Facility's capacity. Each owner is entitled to sell its share of the Facility's capacity, and each is responsible for all expenses of scheduling, sale, transmission, or delivery of its share of the Facility's output. Each owner is also responsible for the costs of any new facilities that are constructed to satisfy an owner's request for transmission service. Moreover, each owner is required to enter into an individual fuel supply arrangement, although it may authorize an operations manager, or an agent, to purchase fuel for it.⁹

10. After the Proposed Transaction, OG&E, Grand River Dam, and Oklahoma Municipal Power will own undivided interests in the Facility in the following proportions: (1) OG&E will own 51 percent; (2) Grand River Dam will own 36 percent; and (3) Oklahoma Municipal Power will own 13 percent.¹⁰ These ownership interests entitle OG&E, Grand River Dam, and Oklahoma Municipal Power to proportionate shares of the Facility's capacity, giving them rights to approximately 610 MW, 430 MW, and 155 MW, respectively.¹¹

⁸ Application at 10. Applicants note that after the transaction is consummated, OG&E will file with the Commission a notice of change of status under FPA section 205 and a notice to cancel Redbud Energy's market-based rate tariff, and OG&E will assume Redbud Energy's interconnection agreement with OG&E.

⁹ Application at 12.

¹⁰ *Id.*

¹¹ Application at 12-13. We note that due to a typographical error, Applicants incorrectly attributed 155 MW to Grand River Dam and 430 MW to Oklahoma Municipal Power.

II. Notice and Responsive Pleadings

11. Notice of Applicants' filing was published in the *Federal Register*, 72 Fed. Reg. 17,967-68 (2008), with interventions and protests due on or before April 10, 2008. AES Shady Point, L.L.C. (Shady Point) filed a timely motion to intervene and a request for a limited extension of the comment period. Oklahoma Municipal Power filed a motion to intervene out of time. The Commission issued a Notice of Extension of Time to file comments up to and including April 18, 2008; thus, Oklahoma Municipal Power's motion became timely. Shady Point filed a timely protest on April 18, 2008. On May 6, 2008, OG&E and Redbud Energy filed a joint answer to Shady Point's protest.

III. Discussion

A. Procedural Matters

12. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2008), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

13. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2008), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept OG&E and Redbud Energy's joint answer because it has provided information that assisted us in our decision-making process.

B. Standard of Review under Section 203

14. FPA section 203(a)(4) requires the Commission to approve a transaction if it determines that the transaction will be consistent with the public interest. Under the Commission's regulations, its analysis of whether a transaction will be consistent with the public interest generally involves considering three factors: (1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation.¹² Section 203 also requires the Commission to find that the 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 the Commission determines that the cross-subsidization, pledge, or encumbrance will be consistent with the public interest."¹³ The

¹² See Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,111.

¹³ 16 U.S.C. § 824b(a)(4) (2006).

Commission's regulations establish verification and informational requirements for applicants that seek a determination that a transaction will not result in inappropriate cross-subsidization or pledge or encumbrance of utility assets.¹⁴

1. Effect on Competition

a. Horizontal Market Power Issues

i. Applicants' Analysis

15. Applicants identify three relevant products: non-firm energy, short-term capacity (firm energy), and long-term capacity. They identify three relevant geographic markets using the approach described in Appendix A of the Merger Policy Statement: the OG&E balancing authority area, the Grand River Dam balancing authority area, and the SPP EIS market.¹⁵ Applicants also analyze the first-tier balancing authority area markets (i.e., directly interconnected balancing authority area markets) and consider parties that have historically been customers of OG&E and Redbud Energy.¹⁶ In their examination of non-firm energy markets, Applicants use Economic Capacity (EC) and Available Economic Capacity (AEC), as defined in the Merger Policy Statement, to represent a supplier's ability to participate in the market.¹⁷ Applicants use the Delivered Price Test (DPT) to

¹⁴ 18 C.F.R. § 33.2(j) (2008).

¹⁵ In Exhibit J-1 at 15, Applicants note that while the Commission has not explicitly relied upon SPP as a relevant geographic market in a merger case, it has relied on the existence of the SPP Energy Imbalance Service market as sufficient reason to allow parties to sell into the Energy Imbalance Service market at market-based rates. *Southwest Power Pool, Inc.*, 114 FERC ¶ 61,289 (2006).

¹⁶ 18 C.F.R. § 33.3(c)(2) (2008). OG&E's first-tier balancing authority areas are the Public Service Company of Oklahoma, Western Farmers Electric Cooperative, Entergy Corp., Westar Energy, Grand River Dam, Southwest Power Administration (SWPA), and Associated Electric Cooperative, Inc.

¹⁷ Generally, "Economic Capacity" is the amount of capacity that could compete in the relevant market given market prices, running costs, and transmission availability. 18 C.F.R. 33.3(c)(4)(i)(A) (2008). "Available Economic Capacity" is based on the same factors, but subtracts the supplier's native load obligation from its capacity and adjusts transmission availability accordingly. 18 C.F.R. 33.3(c)(4)(i)(B) (2008).

evaluate the effect on competition in the relevant markets over 10 time periods (super-peak, peak, and off-peak periods for summer, winter, and shoulder seasons, along with an extreme summer super-peak).¹⁸

16. Applicants state that in order to select market prices for their DPT analysis, they reviewed historical system lambdas¹⁹ of OG&E, bilateral prices, real-time (Energy Imbalance Service) market prices, and a forecast of future market prices. They state that they selected their base-case market prices based primarily on SPP EIS historical real-time prices and a forecast of market prices in the SPP EIS market. Applicants used a \$250/megawatt hour price for the Summer Super Peak period, and they also performed a sensitivity analysis with prices 10 percent higher and lower.²⁰ They state that they reviewed the historical operation of generating facilities in the SPP in order to verify that their assumed market prices and input prices are consistent with historical and expected operation.²¹

17. Applicants analyze the effect of the Transaction on competition using the approach in Appendix A of the Merger Policy Statement for the year 2008. Applicants state that their analysis uses simultaneous import limit (SIL) calculations for Summer, Winter, and Shoulder 2008 seasons for the OG&E and Grand River Dam balancing authority areas and each of their first-tier balancing authority areas. The information was provided by OG&E transmission personnel. Applicants state that these studies are

¹⁸ Application Exhibit J-1 at 18-19. Applicants state that based on market prices and the incremental cost of the Facility, none of the off-peak periods is relevant to their analysis.

¹⁹ System lambda is the variable cost of the last kilowatt produced over a particular hour.

²⁰ Application Exhibit J-1 at 19-20. A sensitivity analysis in this context is a standard statistical procedure designed to test whether the results of the model change significantly due to small changes in key parameters of the model. Results that are not sensitive to changes in key parameters of the model are considered “robust.” For example, in the DPT, the results can be affected by changes in the assumed market price or input prices such as fuel costs. In Order No. 642, the Commission recognized the importance of sensitivity analyses: “[g]iven the importance of prices to the outcome of market definition, we will require applicants to perform sensitivity analyses of alternative prices on the predicted competitive effects. This provides us with an additional measure of confidence and assurance that results are reliable.” Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,891.

²¹ Exhibit J-1 at 20.

consistent with the Commission's requirements in market-based rate filings, except that they use a forward-looking snapshot instead of historical data. They state that the transmission studies also calculate the first contingency incremental transfer capability into the OG&E and Grand River Dam balancing authority areas.²² Applicants allocated transmission capacity using a pro rata or "squeeze-down" method.²³

18. Applicants report no screen failures for AEC for the SPP EIS market or for first-tier markets. They report two screen failures for AEC in the OG&E market (HHI²⁴ changes of 1,030 and 1,303 in highly concentrated markets). They report widespread screen failures in the Grand River Dam market (HHI changes ranging from 1,025 to 3,150 in highly concentrated markets). Applicants argue that these screen failures are driven, in part, by the fact that the market size changes after the Transaction. The market size changes because: (1) the analysis assumes that a portion of the power from the Facility, above the 150 MW that Grand River Dam currently buys under contract, is being transferred from the OG&E balancing authority area to the Grand River Dam balancing authority area, shrinking the former and expanding the latter; (2) during time periods when OG&E, Grand River Dam, or Oklahoma Municipal Power have an AEC

²² *Id.* at 17.

²³ Application Exhibit J-4 at 8. Under the "squeeze down" allocation method, shares of available transmission are allocated at each interface, diminishing as they get closer to the destination market. When economic supply competes to get through a constrained transmission interface into a control area, the transmission capability is allocated to the suppliers in proportion to the amount of economic capacity each supplier has outside of the interface.

²⁴ The Herfindahl-Hirschman Index (HHI) is a widely accepted measure of market concentration, calculated by squaring the market share of each firm competing in the market and summing the results. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases. Markets in which the HHI is less than 1,000 points are considered unconcentrated; markets in which the HHI is greater than or equal to 1,000 but less than 1,800 points are considered moderately concentrated; and markets where the HHI is greater than or equal to 1,800 points are considered highly concentrated. The Commission has adopted the Federal Trade Commission/Department of Justice Horizontal Merger Guidelines, which state that in a horizontal merger, an increase of more than 50 HHI in a highly concentrated market or an increase of 100 HHI in a moderately concentrated market fails the screen and warrants further review. U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, 57 Fed. Reg. 41,552 (1992), *revised*, 4 Trade Reg. Rep (CCH) ¶ 13,104 (April 8, 1997).

deficit pre-transaction, some portion of the additional generation supplied by the Facility first offsets any “negative” AEC, thereby reducing the sizes of the markets; and (3) transmission reservations will be required from SPP in order to deliver ownership shares of power from the Facility to loads after the Transaction i.e., once the facility is designated as a network resource, which could affect transmission availability.²⁵

19. Applicants argue that in this instance, the Commission’s standard methodology produces SIL values that understate the ability of external suppliers to deliver power to the OG&E market. Although the first contingency incremental transfer capabilities from OG&E’s first-tier markets into OG&E are relatively high, when one groups all the first-tier balancing authority areas together and considers them as a single exporting entity, the SIL values into the OG&E balancing authority area hit their limits in the first contingency incremental transfer capability analysis more quickly, resulting in low SIL values.²⁶ Applicants state that when all the first-tier balancing authority areas are treated as a single exporting entity, the most limiting constraint (i.e., the Entergy first contingency incremental transfer capability) restricts the overall SIL into the OG&E balancing authority area. This causes the SIL determination to stop, even though more power could be imported into the OG&E balancing authority area from one or more other sources. The result is that the SIL substantially understates import capability into a market from any particular direction.²⁷ Applicants therefore performed an analysis for the OG&E balancing authority area using first contingency incremental transfer capability data from AEP West to OG&E to measure the ability to import from a single source. This analysis shows a single AEC screen failure. Applicants state that this screen failure is eliminated by a slight change in market price (that is, it is not “robust”). They argue that because this screen failure occurs under conservative assumptions,²⁸ it is non-systematic.²⁹

²⁵ Exhibit J-1 at 27-28. Applicants state that while the SPP will conduct and approve the formal analyses required to grant the new transmission reservations, OG&E transmission personnel conducted studies indicating that dispatching the Facility to the new owners reduces the SILs into the OG&E and Grand River Dam balancing authority areas.

²⁶ Application Exhibit No. OGE-4 at 11.

²⁷ *Id.* at 12.

²⁸ The screen failure occurs in an analysis that includes existing contracts, even though these contracts cover only a small portion of the shoulder period.

²⁹ Exhibit J-1 at 32.

20. Applicants also performed a DPT analysis that assumes that Grand River Dam's share of Redbud Energy above its existing 150 MW contract amount remains inside the OG&E control area market. They made this assumption because Grand River Dam's current load and resource estimates show that it will not require its entire share from the Facility until 2015. Applicants reason that if Grand River Dam has no need of additional energy from the Facility in any given period, it will not dispatch its share of Redbud Energy in excess of 150 MW to serve its load.³⁰ This analysis shows AEC screen failures for Grand River Dam in its home market in the summer peak period and the shoulder super-peak period.³¹

21. Applicants point out that while the DPT is a useful tool to gauge the effect of a transaction on competition, the Commission looks beyond numerical screens.³² Applicants therefore supplement their DPT analysis with the following arguments as to why the Transaction raises no concerns with respect to horizontal market power:

- The Transaction is driven by the need to meet statutory load and reliability obligations. Applicants state that without their existing contracts with Redbud, OG&E, Grand River Dam, and Oklahoma Municipal Power would all require additional capacity to meet those obligations.³³
- There is limited load in the relevant balancing authority areas that is not already subject to long-term requirements contracts. There are no wholesale customers in the OG&E (with the exception of Oklahoma Municipal Power) or Grand River Dam balancing authority areas who are not already served under long-term contracts at fixed or formula rates.³⁴
- OG&E is not authorized to make sales at market-based rates in its balancing authority area, and is authorized to offer cost-based service only for transactions of one week or less. Moreover, OG&E may not make any wholesale sales (cost-based or market-based) for durations of more than one week and less than one year, and agreements for a term of one year or more require prior approval by the

³⁰ *Id.* at 29-30.

³¹ *Id.* at 33.

³² *Id.* at 12, citing *FPA Supplemental Policy Statement*, FERC Stats. & Regs. ¶ 31,253 (2007), order on clarification and reconsideration, 122 FERC ¶ 61,157 (2008).

³³ Exhibit J-1 at 21.

³⁴ *Id.* at 24.

Commission. Applicants assert that these limitations foreclose the opportunity for OG&E to exercise market power.³⁵ Applicants further state that sharing mechanisms put in place by various regulatory commissions further limit or eliminate any incentive for OG&E to increase prices in its balancing authority area. The Oklahoma Corporation Commission (Oklahoma Commission) and Arkansas Public Service Commission require that OG&E credit to retail customers 80 percent and 100 percent, respectively, of profits from off-system sales, and OG&E's Commission tariff requires it to credit certain wholesale customers 90 percent of the profits from off-system sales in some time periods.³⁶

- The SPP EIS market has Commission-approved market monitoring and mitigation measures in effect. The SPP market monitor may demand that any market participant violating the mitigation measures undergo corrective action or, without prior discussion or demand, the market monitor may implement any Commission-approved mitigation measures.³⁷
- The Facility provides a small share of generation in the SPP EIS market, and there is a significant amount of economically similar generation in the region. Applicants state that the SPP EIS footprint has about 47,000 MW of generating capacity, that there is more than 8,000 MW of gas-fired combined cycle capacity of similar vintage and operating characteristics as the Facility in SPP, and that almost 20,000 MW have been added in areas first-tier to the OG&E balancing authority area between 2000 and 2006. Applicants conclude that there is no shortage of capacity for customers seeking alternative sources of supply.³⁸
- In cases where the prospective purchasers have no incentive or ability to attempt to exercise horizontal market power, the Commission has relied on such factors to conclude that proposed transactions are consistent with the public interest.³⁹

³⁵ Application at 30.

³⁶ Exhibit J-1 at 25-26.

³⁷ Application at 29.

³⁸ Exhibit J-1 at 26.

³⁹ Application at 26-27, citing *Entergy Gulf States Inc.*, 121 FERC ¶ 61,182, at P 61-62 (2007).

22. While Applicants argue that the Transaction does not raise competitive concerns, OG&E commits to make transmission upgrades if the Commission requires it to do so as a condition of approval. OG&E will:

- (1) Re-conductor a 161 kV transmission line that runs between Entergy's Russellville North and ANO substations;
- (2) [u]pgrade terminal equipment in the Entergy Russellville South and Russellville East substations; and (3) [u]pgrade terminal equipment located in the Ozark substation in the Van Buren, Arkansas area of the SWPA transmission system.⁴⁰

23. Applicants performed DPT analyses for both the OG&E and Grand River Dam balancing authority areas that include these transmission upgrades. Their analyses show that the upgrades eliminate screen failures in the two markets.⁴¹

ii. Protest

24. Shady Point states that OG&E owns and/or controls virtually all generation in its service territory. It complains that OG&E does not procure long-term energy and capacity in a transparent, competitive manner.⁴² The Oklahoma Commission requires electric utilities to competitively bid energy needs of longer than one year, yet despite this requirement, OG&E refused to seek competitive bids for the long-term capacity needs that would be filled by its acquisition of the Facility. OG&E's acquisition of the Facility thus removes the primary competitor from OG&E's home market.⁴³

25. According to Shady Point, OG&E can exercise its market power to force competitors into firesale situations. Shady Point claims that without significant mitigation measures, OG&E will likely exercise its market power to foreclose Shady

⁴⁰ Application at 31. Applicants anticipate that these upgrades could require 27 months to complete (Exhibit No. OGE-4 at 18).

⁴¹ Application at 34.

⁴² Shady Point Protest at 2. Shady Point notes that OG&E has conducted solicitations for short-term peak period energy over the past two peak seasons and that both have been won by the Facility.

⁴³ Shady Point Protest at 2-3.

Point generation from any market opportunities and will seek to acquire Shady Point's Facility at a distressed price. The Commission should restrain OG&E's market power and promote the development of competition in OG&E's area.⁴⁴

26. Shady Point contends that OG&E has the incentive to use its market power to foreclose competitive access to wholesale markets in OG&E's balancing area. It states that OG&E is serving approximately 300 MW of wholesale capacity under contracts that will either expire or terminate by 2012. In addition, the proposed acquisition will remove a primary competitor to OG&E for wholesale customers that can choose not to renew their contracts with OG&E if competitive alternatives exist. Shady Point argues that OG&E's market power following the acquisition, coupled with its significant excess generation capacity as compared to its native load requirements, will create an effective barrier to other entities wishing to compete for wholesale customers. It further argues that OG&E will have sufficient market power to withhold its own generation from the market while signing wholesale customers to new long-term contracts, thereby foreclosing competitive entry that could restrain prices.⁴⁵

27. Shady Point contends that OG&E's market power analysis significantly understates the company's ability and incentive to withhold output. OG&E has overstated its own capacity needs; its claim that it expects to be short 424 MW in 2010 is 25 percent greater than the incremental capacity need that OG&E presented to the Oklahoma Commission in 2007. Moreover, OG&E's claimed capacity needs in 2012 are over 100 percent greater than the capacity need approved by the Oklahoma Commission. Shady Point states that the Oklahoma Commission made this determination after a complete analysis of OG&E's purported needs and of the testimony of witnesses that reviewed the resource model and its underlying assumptions. This gross overstatement of capacity need skews OG&E's Appendix A analysis to underestimate OG&E's market power following the acquisition.⁴⁶

28. Shady Point argues that the additional market power resulting from the Proposed Transaction is not *de minimis*. The additional market power should not be measured by comparing the Facility's generating capacity to the total capacity in the SPP EIS market.

⁴⁴ *Id.* at 3.

⁴⁵ *Id.* at 5-6.

⁴⁶ *Id.* at 3-5.

A better measure of the additional market power is a comparison of the Facility's capacity to the available capacity in OG&E's area that is not committed to native load and reserve requirements.⁴⁷

29. Shady Point challenges OG&E's argument that OG&E lacks an incentive to exercise market power because it is not allowed to keep all of the revenues from off-system sales. The fact that OG&E can retain *any* revenues from off-system sales creates sufficient incentive to exercise market power. Shady Point also maintains that additional incentive exists because of OG&E's ability to force asset sales at distressed prices.⁴⁸

30. Shady Point reasons that the Commission should condition any approval of the transaction on measures to promote a competitive market in OG&E's balancing authority area: (1) requiring OG&E to establish an economic dispatch process that includes merchant generators for all of OG&E's power needs; and (2) requiring OG&E to divest sufficient generation to offset the increased capacity it is acquiring with the Facility.⁴⁹

iii. Answer

31. Applicants state that Shady Point's claims of competitive injury are speculative and premature. Shady Point has a 300 MW generating facility whose entire output is sold to OG&E under a Power Sales Agreement. Applicants state that OG&E cannot terminate the Power Sales Agreement until January 2013. Shady Point is thus shielded from the harm it alleges may result from the Transaction until 2013. Applicants state that the market conditions in 2013 cannot be known now, and it is speculative to assume that Shady Point will be harmed as a result of the Transaction.⁵⁰

32. In response to Shady Point's complaint that OG&E did not seek competitive bids from other suppliers as an alternative to acquiring the Facility, OG&E says this is beyond the scope of this proceeding. Applicants assert that the correct forum is the Oklahoma Commission, and that a proceeding concerning the Transaction is now pending before that body.⁵¹

⁴⁷ *Id.* at 6.

⁴⁸ *Id.* at 7.

⁴⁹ *Id.*

⁵⁰ Answer to Protest at 3-4.

⁵¹ *Id.* at 4-5.

33. Applicants argue that Shady Point's assertion that OG&E has the means and incentive to exercise market power to force competitors into firesale situations is irrelevant to the Commission's review of the Transaction.⁵² Shady Point's concerns about OG&E's buyer market power are irrelevant because the Transaction does not change the number of buyers in the market. Applicants argue that even if OG&E has buyer market power, nothing in the Transaction changes OG&E's position as a buyer because Redbud Energy is a wholesale seller, not a wholesale purchaser.⁵³

34. Applicants challenge Shady Point's claim that Redbud Energy is distressed, that the sale of the Facility is at a firesale price, and that the Transaction is not at arms' length. Applicants state that Goldman Sachs, Inc. conducted a competitive sales process on behalf of Kelson Holdings, and that the parties vigorously negotiated the Power Sales Agreement. Applicants state that the sales price demonstrates that each party was on equal footing in the negotiations.⁵⁴

35. In response to Shady Point's assertion that OG&E may unilaterally foreclose other parties' market opportunities (and therefore force suppliers to sell at below-market prices), Applicants state that Shady Point offered no support for its claim in this regard. Moreover, that argument was rejected in *Xcel Energy Services, Inc.*⁵⁵ Applicants state that in that case, the Commission concluded that OG&E was properly relieved of the requirement to enter into new obligations or contracts with Qualifying Facilities⁵⁶ because the portion of the SPP in which OG&E and Shady Point are located is a competitive wholesale market that provides Qualified Facilities a meaningful opportunity to sell energy and capacity in long-term, short-term, and real-time markets to purchasers other than OG&E.⁵⁷

36. In response to the argument that OG&E has overstated its capacity needs, Applicants contend that their load forecasts were based on the most recent and most accurate data available. The Oklahoma Commission analysis that Shady Point cites

⁵² *Id.* at 5-6.

⁵³ *Id.* at 6.

⁵⁴ *Id.*

⁵⁵ *Id.* at 7, citing *Xcel Energy Services, Inc.*, 122 FERC ¶ 61,048, at P 31-40 (2008).

⁵⁶ Public Utility Regulatory Policies Act of 1978, 16 U.S.C. 824a-3 (2006).

⁵⁷ Answer to Protest at 7.

excluded wholesale requirements service, which is properly included in OG&E's load forecast. Applicants add that their AEC analysis is based on forecast 2008 conditions, not the 2010 or 2012 time period for which Shady Point disputes the forecast.⁵⁸

37. Countering Shady Point's argument that certain of OG&E's wholesale requirements customers have contracts that may terminate before 2012, Applicants state that these are long-term agreements with evergreen clauses that extend the agreements if the buyer wishes beyond the initial terms. Thus, these wholesale customers may choose to continue to be served by OG&E or, subject to the governing agreement's notice requirements, may enter into new agreements with alternative suppliers. Applicants state that there are very few wholesale customers in the OG&E balancing authority area whose load is not already served under full or partial requirements contracts. Applicants argue that, moreover, there is significant wholesale competition in the OG&E balancing authority area market, and that OG&E cannot raise barriers to entry or otherwise cut its current counterparties' access to the wholesale market.⁵⁹

38. Applicants challenge Shady Point's argument that OG&E should be required to analyze the available capacity in OG&E's area that is not committed to native load and reserve requirements, instead of the total capacity in the SPP EIS market. They state that they have analyzed the capacity available in the relevant market net of native load obligations and that no further analysis is required. Their analysis shows that the Transaction will have no adverse effect on competition. Their analysis of OG&E's share of total capacity in the SPP EIS market was only one of several studies they conducted.⁶⁰

39. Applicants challenge Shady Point's assertion that the requirement that Applicants credit some of the proceeds of off-system sales back to OG&E's customers is insufficient to deter the exercise of market power. They note that OG&E may make these off-system sales at market-based rates only outside of OG&E's balancing authority area.⁶¹

40. Applicants state that Shady Point has not supported its accusations that: (1) OG&E will use its market power to foreclose competitive access to wholesale markets in OG&E's balancing authority areas, or (2) OG&E's market power, coupled with its excess generation capacity following the acquisition, will create a barrier to entry to other entities who want to compete for wholesale customers. They challenge Shady

⁵⁸ *Id.* at 9.

⁵⁹ *Id.* at 9-10.

⁶⁰ *Id.* at 10.

⁶¹ *Id.*

Point's contention that OG&E would have sufficient market power to withhold its own generation from the market while simultaneously signing wholesale customers to new long-term contracts, thereby foreclosing competitive entry that could restrain prices.⁶²

41. Applicants argue that the Commission should reject the conditions that Shady Point requests be imposed on the Transaction. If the Commission concludes that adverse competitive effects would result from the Transaction, OG&E commits to specific transmission projects that would mitigate any adverse effects. Applicants state that Shady Point fails to even allege that the mitigation proposed in the application is inadequate. The Commission should also deny Shady Point's request that the Commission require OG&E to establish an economic dispatch process that would include merchant generators. The entity being acquired is a supplier, not a buyer, and the Transaction does not change the number of buyers in the relevant market. Applicants argue that the alleged need for economic dispatch was also rejected in *Xcel Energy Services*.⁶³ The Commission should also reject Shady Point's request that the Commission require OG&E to divest generation because Applicants' proposed transmission enhancements will reduce HHI levels in the relevant markets while increasing import capacity as well.⁶⁴

iv. Commission Determination

42. We are not convinced by Applicants' argument that the Transaction, without mitigation, will not harm horizontal competition. However, we agree with Applicants that their proposed mitigation upgrades to the Entergy interconnections will increase SIL values sufficiently to prevent competitive harm from the Transaction.

43. Under the Transaction, there would be significant harm to competition, as shown by the six screen failures in the Grand River Dam balancing authority area market, with HHI increases ranging from 1,025 to 3,150 points in highly concentrated markets, and an HHI increase of 1,303 points in the highly-concentrated Summer-Super Peak 2 in the OG&E balancing authority area market. As discussed below, there are several problems with Applicants' proposed alternative analyses, which show artificially low HHI changes.

44. Applicants' first contingency incremental transfer capability analysis artificially lessens the effect of the Transaction on the OG&E balancing authority area market. Order No. 642 requires that section 203 applicants consider the simultaneous import

⁶² *Id.* at 11.

⁶³ *Id.* at 13.

⁶⁴ *Id.* at 14-15.

capability into the relevant market when conducting a DPT.⁶⁵ Applicants aggregated the seven first-tier balancing areas into a single balancing area for the purposes of the SIL study. However, first contingency incremental transfer capability is not a simultaneous measure of import capability. First contingency incremental transfer capability measures the maximum increase in transfer that can take place between two selected subsystems without violating branch ratings or interface limits during single contingencies. As such, it is not simultaneous. Therefore, Applicants' Appendix A study using first contingency incremental transfer capability values does not satisfy the requirement in Order No. 642 that the DPT includes simultaneous transmission limits.

45. Applicants' next alternative analysis attributes the portion of energy from the Facility above 150 MW, which Grand River Dam currently needs,⁶⁶ to the OG&E balancing authority area. This analysis assumes that Grand River Dam could not import the excess capacity into its home balancing authority area, when in fact it can import *all* of this capacity into its home balancing authority area. Therefore, placing the capacity in the OG&E balancing authority area wrongly allows Applicants to prorate the amount of capacity that could enter the Grand River Dam balancing authority area and invalidates Applicants' AEC analysis.

46. Further, Applicants' decision to place this capacity in the OG&E balancing authority area is arbitrary. Applicants claim that Grand River Dam will not need the Redbud capacity because Grand River Dam will have excess capacity in its balancing authority area. Looking closer, while Grand River Dam will have 280 MW of excess capacity in 2009,⁶⁷ OG&E will simultaneously have an excess of 282 MW. Their contention that OG&E will need this capacity while Grand River Dam will not is therefore logically inconsistent.⁶⁸ We further note that, given that Applicants project Grand River Dam to need 282 MW of Redbud's capacity as soon as 2010, Applicants' assumption that only 150 MW of capacity flows into Grand River Dam's balancing authority area is not forward-looking, as the Commission requires.⁶⁹ Applicants understate the competitive effect of the Transaction in 2009 and 2010, for OG&E in its

⁶⁵ Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,892.

⁶⁶ Exhibit J-1 at 22.

⁶⁷ We note that Grand River Dam's excess capacity of 280 MW in 2009 is more than half of its share in the Facility of 430 MW.

⁶⁸ See Exhibit J-1 at 22-23.

⁶⁹ Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 33,368.

home market⁷⁰ and Grand River Dam in its home market. While Applicants are correct that market conditions in 2013 can be only imperfectly forecast; market conditions one and two years in the future can be better predicted and are much more important to our evaluation. Looking forward, the Transaction, without mitigation, would increase concentration in the Grand River Dam control area, which would decrease competition.

47. Applicants' further arguments as to why the Transaction does not raise horizontal competition concerns are likewise unpersuasive. First, OG&E is permitted to sell only at cost-based rates in its home balancing authority area because there is a presumption that OG&E has market power in its home balancing authority area, absent mitigation.⁷¹ Applicants' argument essentially is that the Commission should allow increases in the market power of mitigated entities. However, increases in market concentration, even in mitigated markets, still harm competition by decreasing competitive access to the market. Cost-based mitigation does not address the *structural* harm caused by transactions that increase market concentration. In addition, while the Merger Policy Statement discusses various forms of mitigation, it does not indicate that cost-based rates eliminate harm to competition. Cost-based rates mitigate the market power of an individual seller, but do not address the overall level of competition in the relevant market.⁷² Therefore, we will not accept cost-based rates as permanent mitigation. Second, while there is now limited load in the relevant balancing authority areas that is not already subject to long-term requirements contracts, we cannot assume that the situation will continue. Third, we will not rely on Applicants' analysis of the SPP footprint because that analysis ignores transmission constraints.

48. In *Entergy Gulf States, Inc.*, the acquiring company was significantly short of capacity (approximately 1200 MW) in the season/load conditions where the screen failures occurred. Therefore the Commission concluded that, "[p]hysical withholding of the Facility would require Entergy to purchase even more electric energy from elsewhere at a higher price, making a withholding strategy counterproductive," and found that the

⁷⁰ Grand River Dam's capacity requirement is projected to rise by 23 MW in 2009 and by an additional 133 MW in 2010. Attributing these larger fractions of Grand River Dam's share to its home market will diminish its presence in the OG&E market, raising OG&E's home market share, and creating significant screen failures.

⁷¹ Order on Mitigation, 114 FERC ¶ 61,297; Order on Rehearing and Compliance, 123 FERC ¶ 61,012.

⁷² Cost-based rates ensure that the rates charged by an individual seller are just and reasonable under FPA section 205. However, in a section 203 proceeding, the Commission reviews a transaction's effect on competition in the relevant market as a whole to ensure that the transaction is consistent with the public interest.

acquisition would not adversely affect competition.⁷³ In this case, OG&E does have excess capacity during the season/load conditions where the screen failures occur, and could benefit from higher prices in the market. Therefore, we conclude that the Transaction, without proper mitigation, will harm competition in the relevant market.

49. However, as stated above, we agree with Applicants that their proposed mitigation upgrades to the Entergy interconnections will increase SIL values sufficiently to prevent competitive harm from the Transaction. We thus agree with Applicants that the conditions that Shady Point requests are not needed. We find that Applicants have presented the analysis required by Order No. 642⁷⁴ demonstrating that their proposed measures adequately mitigate the potential harm to competition resulting from the Transaction by increasing the amount of import capability such that the increased amount of competing supply offsets the elimination of a competitor. We further agree with Applicants that the Oklahoma Commission's need determination excluded wholesale requirements service, which is properly included in OG&E's load forecast. Shady Point's complaint that OG&E does not procure long-term energy and capacity in a transparent, competitive manner is beyond the scope of this proceeding. We also reject Shady Point's contention that even with the mitigation Applicants proposed, OG&E would have sufficient market power to withhold its own generation from the market while simultaneously signing wholesale customers to new long-term contracts.

50. The Commission has stated that, "an up-front, enforceable commitment to upgrade or expand transmission facilities [may] mitigate market power, because the constraint relieved by such an upgrade or expansion no longer would limit the scope of the relevant geographic market."⁷⁵ Further, the Commission stated its intent to tailor conditions and remedies to address the particular concerns posed by a merger on a case-by-case basis."⁷⁶ The long-term remedy of expanding transmission is one that the Commission has said can be an acceptable remedy to competitive harm.⁷⁷ Therefore, we accept OG&E's commitment to make transmission upgrades as described herein, and make that a condition of this order.

⁷³ *Entergy Gulf States Inc.*, 121 FERC ¶ 61,182 at P 62.

⁷⁴ Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,897-98.

⁷⁵ Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,121.

⁷⁶ *Id.*

⁷⁷ *Id.* at 30,137.

51. Importantly, if the transmission upgrades are not completed as committed, the Commission intends to examine all of its options, as the Commission retains authority under sections 203(b) and 309 of the FPA to issue supplemental orders as appropriate. Moreover, the Applicants must inform the Commission of any change in circumstances that would reflect a departure from the facts the Commission relied upon in authorizing the Transaction, including facts related to its commitment to make transmission upgrades.

52. Specifically, OG&E has committed to approximately \$17 million worth of upgrades involving: (1) [r]e-conductor a 161 kV transmission line that runs between Entergy's Russellville North and ANO substations; (2) [u]pgrade terminal equipment in the Entergy Russellville South and Russellville East substations; and (3) [u]pgrade terminal equipment located in the Ozark substation in the Van Buren, Arkansas area of the SWPA transmission system. This commitment is more fully described at Ex. OGE-4 at 18-19. Based on OG&E's contention that these upgrades could require 27 months to complete, for purposes of this order, the Commission assumes that these upgrades will be completed within 27 months.

53. Because these upgrades may not be completed for some 27 months, they will not be in place at the time of the consummation of the Transaction. In previous section 203 cases involving mitigation that would not be in place at the time of consummation, the Commission has required interim mitigation.⁷⁸ Here, there will be Commission-approved mitigation in place in the relevant markets for all of OG&E's energy, capacity and energy imbalance sales in the interim period between consummation and the completion of the transmission upgrades.

54. We recognize that this interim mitigation is not a perfect remedy. However, as the Commission stated in the Merger Policy Statement, when permanent mitigation will take time, applicants may propose effective interim remedial measures until the permanent mitigation goes into effect. For energy and capacity sales in the OG&E balancing authority area, OG&E is not authorized to make sales at market-based rates, and is authorized to offer cost-based service only for transactions of one week or less. Moreover, OG&E may not make any wholesale sales (cost-based or market-based) for

⁷⁸ See, e.g., *Oklahoma Gas and Electric Co.*, 108 FERC ¶ 61,004 (2004); see also *American Electric Power Co. and Central and South West Corp.*, Opinion No. 442, 90 FERC ¶ 61,242, order on reh'g, 91 FERC ¶ 61,129 (2000) (affirming in relevant part), appeal denied sub nom. *Wabash Valley Power Association v. FERC*, 268 F.3d 1105 (D.C. Cir. 2001) (Opinion No. 442) (denying petition for review).

durations of more than one week and less than one year, and agreements for a term of one year or more require prior approval by the Commission.⁷⁹ This will restrain OG&E's ability to exercise horizontal market power in its home market.

55. Further, in the SPP EIS market, OG&E will be subject to Commission-approved market monitoring and mitigation measures in the interim period between consummation of the Transaction and the completion of the upgrades. As noted by Applicants, the SPP market monitor is responsible for monitoring market participant behavior to "remedy an actual or perceived potential abuse of market power or market design inefficiencies as part of its monitoring process."⁸⁰ In addition, the SPP market monitor may demand that any market participant violating the mitigation measures undergo corrective action or, without prior discussion or demand, the SPP market monitor may implement any Commission-approved mitigation measure. Therefore, we find that there is adequate interim mitigation to ensure that the Transaction will not adversely affect competition.

b. Vertical Market Power Issues

i. Applicants' Analysis

56. Applicants argue that the Transaction will not have an adverse effect on vertical competition. Redbud Energy owns only limited transmission interconnection facilities and natural gas transportation facilities associated with its existing interconnection to the ONEOK Partners, L.P. (ONEOK) intrastate pipeline. They conclude that the Transaction does not result in the acquisition of upstream assets by the purchasers and does not change the vertical competitive landscape. OG&E and Grand River Dam have

⁷⁹ In Order No. 697, the Commission stated that it would allow mitigated sellers to make market-based rate sales at the metered boundary with a balancing authority area in which the seller has market-based rate authority under certain circumstances, and the Commission adopted a standard tariff provision that mitigated sellers seeking to make such sales must adopt. *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, 72 Fed. Reg. 39,904 (July 20, 2007), FERC Stats. & Regs. ¶ 31,252, at P 830 (2007), *clarified*, 121 FERC ¶ 61,260 (2007) *order on reh'g*, Order No. 697-A, 73 FR 25832 (May 7, 2008), FERC Stats. & Regs. ¶ 31,268, at P 339, *clarified*, 124 FERC ¶ 61,055 (2008). In a compliance order on OG&E's mitigation proposal, the Commission stated that if OG&E wants to make market-based rate sales at the metered boundary, consistent with Order No. 697, it can adopt the relevant tariff provision. Order on Rehearing and Compliance, 123 FERC ¶ 61,012 at P 17. OG&E's filing in that regard is pending before the Commission in Docket No. ER97-4345-022, *et al.*

⁸⁰ Application at 29, citing Section 6.1, Attachment AG, of the SPP OATT.

transferred operational control of their transmission facilities to SPP, a Commission-approved regional transmission organization, and Oklahoma Municipal Power is not a transmission owner. Applicants state that OG&E's affiliate Enogex's ownership of intrastate natural gas pipeline systems in Oklahoma will not harm competition because there are numerous interstate natural gas pipeline systems in Oklahoma, and ONEOK intrastate systems provide competing natural gas transportation service.⁸¹

ii. Commission Determination

57. In mergers combining electric generation assets with inputs to generating power (such as natural gas transmission or fuel supply assets), competition can be harmed if the merger increases the merged firm's ability or incentive to exercise vertical market power in wholesale electricity markets.⁸² Here, Applicants have shown that the Transaction does not raise any of these concerns. With respect to the combination of generation and transmission assets, consistent with our finding in *PSEG Waterford Energy LLC*⁸³ and other cases, turning over functional control of an applicant's transmission facilities to a Commission-approved RTO mitigates vertical market power concerns.

2. Effect on Rates

a. Applicants' Analysis

58. Applicants argue that the Transaction will have no adverse effect on transmission rates. OG&E proposes a hold harmless provision that Applicants state is comparable to those previously approved by the Commission for transmission service providers using formula rates. Specifically, OG&E commits that: (1) for a five-year period beginning at closing, it will not seek to include in its annual transmission revenue requirement any transaction-related costs that are not offset by savings related to the transaction; (2) it will not seek to recover any acquisition premium through rates until it has obtained specific regulatory authority to do so; and (3) it will not include transaction-related costs in those transmission rates without specifically identifying them and demonstrating that the costs included in the rates are exceeded by the savings produced by the Transaction; and if there is a dispute, it will bear the burden of proof that the savings from the Transaction exceed the transaction costs charged to the customer.⁸⁴

⁸¹ Application at 32-33.

⁸² See Order No. 642, FERC Stats. & Regs. ¶ 31,111 at 31,904.

⁸³ *PSEG Waterford Energy LLC*, 112 FERC ¶ 61,308, at P 32 (2005).

⁸⁴ Application at 34-35.

59. With respect to power rates, Applicants state that the Transaction will not result in OG&E changing the rates it charges any captive wholesale customer. OG&E provides wholesale requirements service at stated rates under agreements that do not allow it to pass through transaction-related costs. Applicants state that OG&E makes wholesale sales outside of its home market at market-based rates and that any such agreements will be unaffected by the Transaction. Applicants argue that the Transaction will have no adverse effects on Redbud Energy's long-term wholesale sales customers because there are no long-term power sales agreements that extend beyond the anticipated closing date of the Transaction, other than certain agreements with OG&E, Oklahoma Municipal Power, and Grand River Dam that will be assumed as a result of the Transaction.⁸⁵

b. Commission Determination

60. We accept Applicants' commitment to hold transmission customers harmless from costs related to the Transaction. In addition, Applicants state that OG&E provides wholesale requirements service at stated rates under agreements that do not allow OG&E to pass through transaction-related costs. Therefore, we find that the Transaction will not adversely affect wholesale power rates. We note that nothing in the application indicates that rates to customers will increase as a result of the Transaction, and no customer argues otherwise. In addition, the Commission will be able to monitor the Applicants' hold harmless provision under the books and records provision of the Public Utility Holding Company Act of 2005.⁸⁶ Therefore, we find that the Transaction will not adversely affect rates.

3. Effect on Regulation

a. Applicants' Analysis

61. Applicants state that the Transaction will not impair state or federal regulation. It is subject to pre-approval by the Oklahoma Commission, which is authorized to evaluate the effect of the transaction on state regulation. Applicants state that OG&E's wholesale sales and transmission operations are subject to regulation by the Commission. Their retail operations are subject to state regulation in Oklahoma and Arkansas.⁸⁷

⁸⁵ *Id.* at 36.

⁸⁶ Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594, § 1266 (2005).

⁸⁷ Application at 37.

b. Commission Determination

62. We find that neither state nor federal regulation will be impaired by the Transaction. The Commission's review of a Transaction's effect on regulation is focused on ensuring that the transaction does not result in a regulatory gap at the federal or state level.⁸⁸ We find that the Transaction will not create a regulatory gap at the federal level, because the Commission will retain its authority over OG&E. In the Merger Policy Statement, the Commission stated that it ordinarily will not set the issue of the effect of a transaction on state regulatory authority for a trial-type hearing where a state has authority to act on a transaction. However, if the state lacks this authority and raises concerns about the effect on regulation, the Commission stated that it may set the issue for hearing and that it will address such circumstances on a case-by-case basis.⁸⁹ We note that no party alleges that regulation would be impaired by the proposed transaction, and no state commission has requested that the Commission address the effect on state regulation.

4. Cross-Subsidization and Encumbrance of Utility Assets

a. Applicants' Analysis

63. Applicants contend that the Transaction raises no concerns with respect to cross-subsidization of a non-utility associate company or any pledge or encumbrance of utility assets for the benefit of an associate company. Applicants verify that based on known or reasonably foreseeable information, the Transaction will not result in, at the time of the transaction or in the future: (1) transfers of facilities between a traditional public utility associate company that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, and an associate company; (2) any new issuances of securities by a traditional public utility associate company that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, for the benefit of an associate company; (3) any new pledge or encumbrance of assets of a traditional public utility associate company that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, for the benefit of an associate company; or (4) any new affiliate contracts between a non-utility associate company and a traditional public utility associate company that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, other than non-power goods and services agreements subject to review under sections 205 and 206 of the FPA.

⁸⁸ Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,124.

⁸⁹ *Id.* at 30,125.

b. Commission Determination

64. We find that based on the Applicants' affirmation in Exhibit M of the application,⁹⁰ the 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. We note that no protests regarding cross-subsidization were filed.

5. Accounting Analysis

65. OG&E provides *pro forma* accounting entries showing the proposed accounting for the Transaction. It would clear the Transaction through Account 102, Electric Plant Purchased or Sold, and records its undivided interest in the plant on its books consistent with Electric Plant Instruction No. 5, Electric Plant Purchased or Sold.⁹¹

66. OG&E also requests authorization to defer and amortize transaction-related costs that are not otherwise deferred under generally accepted accounting principles (GAAP) over a five-year period commencing on the closing date.⁹²

67. To defer the jurisdictional portion of the transaction-related costs not otherwise deferred under GAAP, the costs must be recorded in Account 182.3, Other Regulatory Assets, consistent with the instructions for that account. The instructions for Account 182.3 provide that this account shall include specific expenses that would be included in net income determinations in one period under the general requirements of the Uniform System of Accounts but for it being probable that such expenses will be included in a different period for purposes of developing rates. At this time, we cannot determine whether the costs at issue will ultimately be found to be recoverable in future rates. Therefore, OG&E must assess all available evidence bearing on the likelihood of rate recovery of these costs in periods other than the period in which they would otherwise be

⁹⁰ See 18 C.F.R. § 33.2(j)(1)(ii) (2008).

⁹¹ 18 C.F.R. Part 101 (2008).

⁹² In its application, OG&E indicates that *transaction-related costs* include the acquisition premium, transaction fees and related costs. We do not consider an acquisition adjustment (or premium) to be a transaction cost that is chargeable to expense as incurred. Therefore, our response refers to those transaction-related costs that would otherwise be charged to expense as incurred in accordance with the Commission's accounting requirements.

charged to expense.⁹³ If based on such an assessment, it decides that future rate recovery of the transaction-related costs is probable, then it may defer the costs in Account 182.3.⁹⁴

68. The instructions to Account 182.3 also require that amounts deferred in this account are to be charged to expense concurrently with the recovery of the amounts in rates. We will not authorize the proposed five-year amortization of deferred transaction-related costs at this time. This request is premature, and is more appropriately addressed in the rate proceeding in which ultimate recovery in rates is determined.⁹⁵ If rate recovery of all or part of the costs deferred in Account 182.3 is later disallowed, the disallowed amount shall be charged to Account 426.5, Other Deductions, in the year of disallowance.

69. OG&E must submit its final accounting entries for the acquisition and dissolution of Redbud Energy within six months of completion of the Transaction, consistent with the Commission policies discussed herein, and as outlined in the Ordering Paragraphs below.

The Commission orders:

(A) Applicants' Transaction is conditionally authorized, as discussed in the body of this order. Applicants shall notify the Commission within 10 days of the date that the Transmission Upgrades have been completed. Applicants shall file quarterly updates describing the progress of the Transmission Upgrades until they are complete.

(B) 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.

⁹³ See, e.g., *PJM Interconnection, LLC*, 109 FERC ¶ 61,012, at P 53-54 (2004), *order on reh'g*, 110 FERC ¶ 61,234 (2005).

⁹⁴ The term "probable" as used in the definition of regulatory assets refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved. *Revisions to Uniform System of Accounts to Account for Allowances under the Clean Air Act Amendments of 1990 and Regulatory-Created Assets and Liabilities and to Form Nos. 1, 1-F, 2, and 2-A*, FERC Stats. & Regs., Regulations Preambles January 1991-June 1996 ¶ 30,967 (1993).

⁹⁵ See *FirstEnergy Service Co.*, 110 FERC ¶ 61,230 (2005).

(C) 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.

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

(E) Applicants shall make any appropriate filings under section 205 of the FPA, as necessary, to implement the Transaction.

(F) If the Transaction results in changes in the status or the upstream ownership of Applicants' affiliated qualifying facilities, if any, an appropriate filing for recertification pursuant to 18 C.F.R. § 292.207 shall be made.

(G) OG&E shall account for the Transaction in accordance with Electric Plant Instruction No. 5 and Account 102, Electric Plant Purchased or Sold, of the Uniform System of Accounts. OG&E shall submit its final accounting entries within six months of the date that the transfer is consummated, and the accounting submissions shall provide all the accounting entries and amounts related to the transfer along with narrative explanations describing the basis for the entries.

(H) Applicants must inform the Commission of any change in circumstances that would reflect a departure from the facts the Commission relied upon in authorizing the Transaction; and

(I) Applicants shall notify the Commission within 10 days of the date that the Transaction has been consummated.

By the Commission. Commissioner Kelly concurring in part with a separate statement attached.
Commissioner Wellinghoff concurring with a separate statement attached.

(S E A L)

Kimberly D. Bose,
Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSIONOklahoma Gas and Electric Company
Redbud Energy LP

Docket No. EC08-58-000

(Issued September 16, 2008)

KELLY, Commissioner, *concurring in part*:

In its application, Oklahoma Gas and Electric Company (OG&E) commits to making certain transmission upgrades to mitigate the transaction's competitive harm, if the Commission requires it to do so as a condition of authorization. In this order, the Commission does impose such a requirement because we determine that the transaction will have a negative impact on competition due to horizontal market power issues. I write separately to clarify a point that the order does not address. The order does not discuss what costs are transaction-related costs subject to OG&E's hold harmless provision. I believe that the costs associated with OG&E's proposed transmission upgrades are transaction-related costs for which OG&E must provide this important consumer protection. The Merger Policy Statement found that a hold harmless provision should include "a commitment from the applicant that it will protect wholesale customers from any adverse rate effects resulting from the merger for a significant period of time following the merger."⁹⁶ In *Puget Energy, Inc.*, the Commission interpreted the hold harmless commitment to "include all merger-related costs, not only costs related to consummating the transaction."⁹⁷ Therefore, the requirements of the hold harmless provision apply to the transmission upgrades accepted as mitigation here, including the requirement that, for five-years from closing, OG&E will not seek to include these costs in its annual transmission revenue requirement absent a showing that they are offset by savings related to the transaction.

⁹⁶ *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, FERC Stats. & Regs. ¶ 31,044, at 30,124 (1996), *reconsideration denied*, Order No. 592-A, 79 FERC ¶ 61,321 (1997) (Merger Policy Statement).

⁹⁷ *Puget Energy, Inc.*, 123 FERC ¶ 61,050, at P 27 (2008) (citing *National Grid*, 117 FERC ¶ 61,080, at P 54 (2006)).

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For these reasons, I respectfully concur in part from this order.

Suedeen G. Kelly

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Oklahoma Gas and Electric Company
Redbud Energy LP

Docket No. EC08-58-000

(September 16, 2008)

WELLINGHOFF, Commissioner, *concurring*:

The Commission finds in today's order that, absent appropriate mitigation, the proposed transaction would result in significant harm to competition due to increased horizontal market power. The Commission also finds that in the long term, Applicants' commitment to complete approximately \$17 million worth of transmission upgrades will adequately mitigate that potential harm to competition. The Commission further finds that there is adequate interim mitigation – including existing restrictions on OG&E's energy and capacity sales in its balancing authority area, as well as Commission-approved market monitoring and mitigation measures in the SPP EIS market – to ensure that the proposed transaction will not adversely affect competition until those upgrades are complete.

I agree with the Commission's decision to require OG&E to complete the specified transmission upgrades as a condition of approving the proposed transaction. I also believe that the Commission has identified important interim mitigation measures. Beyond those actions, however, I would encourage OG&E to further consider demand resources as a mitigation measure. As the Commission has recognized, demand response and other demand resources can help reduce generator market power.⁹⁸ In addition, demand resources often can be implemented more quickly than transmission upgrades can be completed.

For this reason, I concur with today's order.

Jon Wellinghoff
Commissioner

⁹⁸ See, e.g., *Wholesale Competition in Regions with Organized Electric Markets*, Notice of Proposed Rulemaking, 122 FERC ¶ 61,167 at P 31, 119 (2008).

Document Content(s)

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