

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Westar Energy, Inc.
ONEOK Energy Services Company, L.P.

Docket No. EC06-48-000

ORDER CONDITIONALLY AUTHORIZING DISPOSITION
AND ACQUISITION OF GENERATING AND JURISDICTIONAL FACILITIES

(Issued May 22, 2006)

1. On December 21, 2005, Westar Energy, Inc. (Westar Energy) and ONEOK Energy Services Company, L.P. (ONEOK Energy Services) (collectively, Applicants) filed an application under section 203 of the Federal Power Act (FPA)¹ for authorization for a disposition and acquisition of jurisdictional and generating facilities in connection with the sale of the approximately 300 MW single cycle natural gas-fired combustion turbine Spring Creek generating facility (Facility) and associated transmission facilities.² The proposed transaction also includes the transfer from ONEOK Energy Services to Westar Energy of a wholesale power purchase agreement (Power Purchase Agreement). The Power Purchase Agreement provides for the sale to the Oklahoma Municipal Power Authority (OMPA) of approximately 75 MWs of capacity and associated energy from the Facility. The jurisdictional facilities include step-up transformers, generation lead lines and switchyard facilities necessary to interconnect the Facility to Oklahoma Gas & Electric Company's (OG&E) transmission system, as well as the Power Purchase Agreement. The Commission has reviewed the proposed transaction under the Commission's Merger Policy Statement³ and Order No. 669.⁴ We will conditionally

¹ 16 U.S.C. § 824b (2000), *amended by* Energy Policy Act of 2005 § 1289, Pub. L. No. 109-58, 119 Stat. 594, 982-93 (2005) (EPAAct 2005).

² *Transactions Subject to FPA Section 203*, Order No. 669, FERC Stats. & Regs. ¶ 31,200 (2005), *order on reh'g*, Order No. 669-A, 71 Fed. Reg. ¶ 28,422 (May 16, 2006).

³ *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, 61 Fed. Reg. 68,595 (1996), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,044 (1996), *reconsideration denied*, Order No. 592-A, 62 Fed. Reg. 33,341 (1997), 79 FERC ¶ 61,321 (1997) (Merger Policy Statement); *see also Revised Filing Requirements Under Part 33 of the Commission's Regulations*, Order No. 642, 65 Fed. Reg. 70,984 (2000), FERC Stats. &

authorize the proposed transaction, which includes mitigation of market effects through transmission upgrades. We find that with the mitigation, the transaction is consistent with the public interest and otherwise meets the requirements of section 203 of the FPA.

I. Background

A. Description of the Parties

2. Westar Energy is a public utility engaged in the generation, transmission, distribution and sale of electricity. Its retail operations are regulated by the Kansas Corporation Commission (Kansas Commission), and its electric sales at wholesale and transmission services in interstate commerce are regulated by the Commission. Westar Energy's transmission system is in eastern and central Kansas and is under the functional control of the Southwest Power Pool, Inc. (SPP), which is a Commission-approved regional transmission organization.⁵ Westar Energy has authority to sell electric energy and capacity at negotiated, market-based rates.⁶

3. ONEOK Energy Services is a Texas limited partnership and wholly-owned subsidiary of ONEOK, Inc., a diversified energy company. ONEOK Energy Services is a wholesale power marketer that has been authorized by the Commission to sell energy and related products at negotiated, market-based rates.⁷ It owns the Facility, which is in Logan County, Oklahoma, in the OG&E control area. ONEOK Energy Services is not affiliated with any public utility that operates a state-franchised service area.

B. The Proposed Transaction

4. Applicants propose that ONEOK Energy Services sell, and Westar Energy acquire, the Facility and associated transmission facilities, as well as any related books, records, and accounts. In addition, the Applicants request authorization for ONEOK

Regs., Regulations Preambles July 1996-December 2000 ¶ 31,111 (2000), *order on reh'g*, Order No. 642-A, 66 Fed. Reg. 16,121 (2001), 94 FERC ¶ 61,289 (2001) (Merger Filings Requirements Rule).

⁴ Order No. 669.

⁵ *Southwest Power Pool, Inc.*, 109 FERC ¶ 61,009 (2004), *order on reh'g*, 110 FERC ¶ 61,137 (2005).

⁶ *Western Resources, Inc.*, 83 FERC ¶ 61,110 (1998).

⁷ *ONEOK Power Marketing Company*, Docket No. ER98-3897-000 (Sept. 8, 1998) (Letter Order). The Commission accepted ONEOK Energy Marketing and Trading Company's updated market power analysis in *ONEOK Energy Marketing and Trading Company, L.P.*, 109 FERC ¶ 61,124 (2004).

Energy Services to transfer to Westar Energy the Power Purchase Agreement. Westar Energy intends to designate the Facility as a network resource and obtain firm transmission from SPP to import power from the Facility to serve the growing needs of its customers. It expects to use the Facility primarily as a peaking facility. Westar Energy proposes that if the SPP requires construction of less than 225 MW of firm transmission capacity to designate the Facility as a network resource, that Westar Energy will, at its discretion, either construct additional transmission capacity or divest economically comparable generating units. If some or all of the 225 MW can be imported prior to transmission upgrades or divestiture, Westar offers interim mitigation of selling, at cost-based rates, peaking energy and/or capacity equal to the necessary permanent transmission upgrades or generation divestiture. Consideration for the proposed transfer of the facility is over \$10,000,000, thus triggering FPA section 203.⁸

II. Notice of Filing and Responsive Pleadings

5. Notice of Applicants' filing was published in the *Federal Register*, 71 Fed. Reg. 595 (2006), with comments, protests or interventions due on or before January 13, 2006. On January 4, 2006, OMPA requested more time. The Commission granted an extension to February 6, 2006.

6. OG&E filed a motion to intervene on February 6, 2006. Timely motions to intervene and protests were filed by OMPA and the Kansas Power Pool.⁹ On February 21, 2006, Applicants filed a request for leave to file an answer and an answer. On March 8, 2006, OMPA filed a request for leave to reply and a reply. On March 13, 2006, OMPA followed up by submitting the work papers supporting its March 8 reply. On March 23, 2006, Applicants filed a reply to OMPA's reply.

7. On April 11, 2006, the Commission issued an order directing Applicants to release material to OMPA representatives. Applicants originally filed the information as non-public along with a proposed protective order under which the non-public information would be released to qualified Reviewing Representatives who executed the protective order. The order directed Applicants to release any withheld information to all qualified

⁸ Article 3.1 of the 10/21/05 draft contract states that the consideration is "(a) an amount in case equal to \$53,000,000 (the 'Purchase Price') and (b) the assumption of the Assumed Liabilities."

⁹ OMPA filed its motion to intervene on January 13, 2006, and its protest on February 6, 2006. After ONEOK Energy Services raised issues regarding the confidentiality of a portion of the material filed by OMPA, OMPA withdrew the public and non-public versions of its original February 6 protest, and filed corrected public and non-public versions on February 7, 2006. Kansas Power Pool filed its motion to intervene and protest on February 6, 2006.

OMPA Reviewing Representatives within five days, and gave OMPA seven days after receipt in which to file any comments based on such new information. On April 19, 2006, OMPA filed timely supplemental comments after reviewing the protected material. On April 25, 2006, Applicants filed a reply to OMPA's supplemental comments.

III. Discussion

A. Procedural Matters

8. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

9. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2)(2005), prohibits an answer to a protest or an answer unless otherwise ordered by the decisional authority. We will accept Applicants' answer, OMPA's March 8, reply, and Applicants' March 23 reply because they have provided information that assisted us in our decision-making process.

B. Standard of Review Under Section 203

10. Section 203(a) of the FPA provides that the Commission must approve a disposition of facilities if it finds that the disposition "will be consistent with the public interest."¹⁰ The Commission's analysis of whether a disposition is consistent with the public interest generally involves consideration of three factors: (1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation.¹¹ EAct 2005 amended section 203 to specifically require that the Commission also determine that the disposition 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.¹²

¹⁰ 16 U.S.C. § 824b(a)(4) (2005).

¹¹ *Supra* note 3.

¹² EAct 2005 § 1289, 119 Stat. 982-83, to be codified at 16 U.S.C. § 824b(a)(4).

1. **Effect on Competition**
 - a. **Market Power Issues**
 - i. **Applicants' Analysis**

11. Applicants retained Ms. Julie Solomon to analyze the effect of the proposed transaction on competition. Ms. Solomon analyzed two products, non-firm energy and capacity, which she examined across the Westar Energy and OG&E control areas and the control areas directly interconnected with Westar Energy. She looked at economic capacity (EC)¹³ and available economic capacity (AEC)¹⁴ both before and after construction of transmission upgrades needed for Westar Energy to designate 225 MWS from the Facility to be a network resource for the native load in its home control area. She examined four time periods: super peak periods for summer, winter and shoulder seasons, plus extreme summer super-peak, as the Facility is a peaking facility.¹⁵

12. Applicants' analysis finds no competitive concerns before the Facility is designated as a network resource. Although Applicants' analysis finds the Westar Energy market to be highly concentrated for EC both pre- and post- transaction, the change to the Herfindahl-Hirschman Index (HHI)¹⁶ is below the Commission's threshold

¹³ "The amount of generating capacity owned or controlled by a potential supplier with variable costs low enough that energy from such capacity could be economically delivered to the destination market. Prior to applying the delivered price test, the generating capacity meeting this definition must be adjusted by subtracting capacity committed under long-term firm sales contracts and adding capacity acquired under long-term firm purchase contracts (*i.e.*, contracts with a remaining commitment of more than one year). The capacity associated with any such adjustments must be attributed to the party that has authority to decide when generating resources are available for operation. Other generating capacity may also be attributed to another supplier based on operational control criteria as deemed necessary, but the applicant must explain the reasons for doing so." 18 C.F.R. § 33.3(c)(4)(i)(A) (2005).

¹⁴ "Available economic capacity means the amount of generating capacity meeting the definition of economic capacity less the amount of generating capacity needed to serve the potential supplier's native load commitments . . ." 18 C.F.R. § 33.3(c)(4)(i)(B) (2005).

¹⁵ Application at 6.

¹⁶ "The HHI statistic is a measure of market concentration and is a function of the number of firms in a market and their respective market shares. The HHI statistic is calculated by summing the squares of the individual market shares, expressed as percentages, of all potential suppliers to the destination market." 18 C.F.R. § 33.3(c)(5) (2005).

in all time periods. The proposed transaction also passes the Competitive Analysis Screen for AEC in all time periods.¹⁷

13. Applicants' analysis concludes that, with the Facility designated as a network resource, any increase in Westar Energy's share of the OG&E market is below the Commission's thresholds under relevant load conditions. The analysis assumes that the Facility would remain available to provide non-firm energy within the OG&E market even after it is designated a network resource.¹⁸

14. While Applicants' analysis with the Facility as a network resource shows some screen failures for the EC measure, Applicants assert that the EC measure is a poor indicator in this instance due to the lack of retail competition in Kansas and Westar Energy's obligation to serve its native load customers. Applicants contend that AEC is more relevant because, unlike EC, it accounts for Westar's native load commitments, and urge the Commission to give it more weight, as it did in *Nevada Power Company*.¹⁹ Under Applicants' analysis, the proposed transaction passes using AEC in three out of four relevant time periods (failing only during winter super-peak time period), and the market is generally unconcentrated, with Westar Energy's shares of the market ranging from 11 percent to 23 percent.²⁰

15. Applicants also claim that it is premature to find any adverse competitive effects given that Westar Energy likely will have to provide transmission upgrades in order to get the Facility treated as a network resource. Applicants state that "[t]o the extent 225 MW of upgrades are necessary in order to designate 225 MW of the Facility's capacity as a Westar Energy network resource, the upgrades will preserve the current competitive balance."²¹ Applicants state that mitigation need not restore HHIs to pre-transaction levels where transmission upgrades provide access to competing generating capacity, citing *Oklahoma Gas & Electric Company and NRG McClain LLC (OG&E)*.²² Should the Commission determine that mitigation is necessary because SPP requires Westar Energy to construct less than 225 MWs of firm transmission, Westar Energy proposes to, "in its sole discretion," either construct additional transmission capacity or divest economically comparable generating units, or do a combination of both, to achieve necessary mitigation (up to 225 MWs). Under Applicants' proposal, the mitigation

¹⁷ Application at 7.

¹⁸ *Id.* at 7.

¹⁹ 113 FERC ¶ 61,265 at P 15 (2005) (*Nevada Power*).

²⁰ Application at 7-8.

²¹ *Id.* at 9.

²² 108 FERC ¶ 61,004 at P 32 (2004); application at 9.

would be the difference between 225 MWs and the amount of transmission that SPP requires Westar Energy to construct to import power from the Facility on a firm basis.²³

16. As for vertical market power, Applicants state the proposed transaction will not have adverse competitive effects because Westar Energy's transmission facilities are under the functional control of the SPP. In addition, the proposed transaction does not involve the sale, disposition, or change in control over inputs to generation.²⁴

ii. Protests

17. OMPA and Kansas Power Pool raise the following issues: (1) Applicants' study and mitigation understate capacity under Westar Energy's control; (2) the proposed divestiture option will not mitigate market power or transmission constraints; (3) Westar Energy has not committed to upgrades before importing power on a firm basis; (4) Kansas transmission is already highly constrained; and (5) it is premature to make conclusions regarding mitigation.

18. Protestors allege several defects in Applicants' analysis that cause it to understate the capacity under Westar Energy's control. They object to Applicants' deduction of 75 MWs of capacity based on the OMPA-ONEOK Energy Services contract, questioning whether Westar Energy will actually acquire ONEOK's existing 75 MW obligation to OMPA. Even if Westar Energy assumes the 75 MW obligation, the contract gives the seller considerable control over the output; thus, the full 300 MW capacity of the Facility should be attributed to Westar Energy for both EC and AEC.²⁵ In addition, OMPA questions whether, given Westar Energy's relationship with the 1,200 MW Redbud generation facility, Redbud's generating capacity should be attributed to Westar Energy's supply under the EC and AEC screens.²⁶ OMPA notes that Applicants' analysis makes no reference to Redbud, and alleges that Westar Energy has failed to provide necessary information regarding its relationship with respect to the Redbud facility.²⁷

19. OMPA alleges that Applicants' analysis does not provide all of the information required under 18 CFR § 33.3(d)(3) (2005), which specifies the information applicants must provide regarding long-term purchase and sales. Specifically, OMPA alleges that Applicants have failed to provide the following information: duration of the contract,

²³ Application at 9-11.

²⁴ *Id.* at 11-12.

²⁵ Kansas Power Pool protest at 8-9; OMPA protest at 9-12.

²⁶ Under the terms of the Redbud Energy Management Agreement (Redbud Agreement), Westar Energy is the Energy Manager for the Redbud facility.

²⁷ OMPA protest at 12-15.

provisions regarding renewal of the contract, priority or degree of interruptibility; and information on provisions of contracts which confer operational control over generation resources to the purchaser. Therefore, Applicants have not supported the long-term contract assumptions used in their Appendix A analysis.²⁸ In addition, OMPA claims that Applicants' analysis underestimates peak destination prices, which reduces the amount of Westar Energy's capacity that is economic, thus understating its market shares and concentration for both the Westar Energy and OG&E control areas. Using appropriate market shares and concentration could lead to more serious screen violations.²⁹

20. OMPA hypothesizes that Applicants' AEC calculation used native load commitment measured at the time of Westar Energy's needle peak. It advocates a more conservative approach, such as the one used by Westar Energy itself in its market-based rate compliance filing in ER03-9-004, *et al.* According to OMPA, a more conservative approach "will raise the HHI levels and changes in HHI for the [AEC] screens significantly."³⁰

21. OMPA says that if the Commission reruns the Appendix A analysis with OMPA's corrections, additional and more serious screen violations will be found for both the Westar Energy and OG&E control areas. For example, attributing Redbud's capacity to Westar Energy dramatically increases Westar Energy's market share in the OG&E control area from approximately 13 to 17 percent, adding 86 to 100 points to the HHI change reported by Applicants, which was about 3-10 points. According to OMPA, the change in HHI would be above 50, and given the highly concentrated OG&E market, this would fail the EC screen even when the Facility is not designated as a network resource.³¹ With the Facility designated as a network resource, OMPA's adjustments would result in significant increases to the HHIs using the AEC screens. OMPA contends that its proposed corrections would affect both EC and AEC.³²

22. OMPA urges the Commission to find that the proposed transaction is likely to harm competition. According to OMPA, even without these adjustments, Applicants' Appendix A analysis shows screen violations in over a third of the time periods,

²⁸ *Id.* at 15-17.

²⁹ *Id.* at 17-18.

³⁰ *Id.* at 19, *quoting* Frayer Aff., Question 3.6.

³¹ *Id.* at 20.

³² *Id.* at 21.

including all EC time periods and two AEC periods when the Facility is considered a Westar Energy network resource.³³

23. OMPA attempts to distinguish the *Nevada Power* case,³⁴ where the Commission relied heavily on AEC results. It notes that Nevada Power was a significant net purchaser of generation, which reduced its incentive to raise prices for wholesale products that it would need to buy to serve its load. In addition, Nevada Power did not have market-based rate authority in the areas where the screen violations occurred, while Westar Energy has such authority in the OG&E control area. Finally, the proposed transaction in *Nevada Power* freed up transmission import capability, improving access to external trading hubs.³⁵

24. OMPA also alleges additional harm beyond what is shown by screen violations. According to OMPA, the market is already highly concentrated in over half of the studied time periods for the Westar Energy control area, and the proposed acquisition will aggravate the situation.³⁶ OMPA claims that limited supply choices affect its ability to serve loads in both OG&E and Westar Energy control areas; it already has trouble getting power to the Kansas Power Pool loads.³⁷ The proposed acquisition would enhance Westar Energy's ability and incentive to bid strategically, worsening OMPA's current difficulties.³⁸ OMPA notes in particular that two out of the more than 100 flowgates in the SPP footprint (the Kildare-Cresswell and South Coffeyville Dearing flowgates) represent over 55 percent of all transmission load relief (TLR) events in the fourth quarter of 2004 and 100 percent of TLR events in the first quarter of 2005. The North American Electric Reliability Council deems a significant amount of capacity in SPP to be uncommitted due to lack of firm transmission paths that would make it deliverable to load.³⁹ OMPA's expert discusses scenarios in which management of congestion could be used to raise prices and profits. According to OMPA, the existence of the SPP does not prevent this behavior because generators control dispatch decisions, which directly affect the extent and timing of transmission congestion.⁴⁰

³³ *Id.* at 22, we note that OMPA is incorrect; there is only one screen failure for AEC.

³⁴ 113 FERC ¶ 61,265 (2005).

³⁵ OMPA protest at 23.

³⁶ *Id.* at 27.

³⁷ *Id.* at 28.

³⁸ *Id.* at 29.

³⁹ *Id.* at 32.

⁴⁰ *Id.* at 33.

25. OMPA also alleges that the proposed transaction would eliminate ONEOK Energy Services, an independent competitive force, enhancing Westar Energy's position in both its own control area and the OG&E control areas.⁴¹ This would discourage new, independent generators from entering the market, leaving only three independent merchant plants in the Westar Energy and OG&E control areas.⁴² The transmission constraints make it difficult to secure a transmission path to deliver output to a wholesale customer, such as OMPA.⁴³

26. Turning to the question of what mitigation is needed to prevent harm to competition, OMPA claims that the mitigation proposed by Applicants is inadequate. It complains that the mitigation plans lacks specificity in that Westar Energy proposes to reserve for itself unilateral authority to determine whether to mitigate through transmission upgrades, divestiture of generation, or a combination of both. Divestiture would not be effective mitigation, and might increase Westar Energy's market power should the units be retired rather than sold.

27. Protestors also challenge whether a MW-for-MW offset⁴⁴ will address the competitive harms associated with the proposed transaction, noting that “[t]ransmission is not a MW-for-MW substitute for generation,” and in some circumstances could actually complement generation in bidding strategies, increasing market power concerns.⁴⁵ They cite the *OG&E* case as an instance where additional transmission capacity did not necessarily mitigate the competitive harm associated with a transaction.⁴⁶ In addition, protestors allege that the lack of specifics regarding potential transmission upgrades makes it impossible to assess the effect of the proposed mitigation. Furthermore, Westar Energy only proposes to construct the difference between the 225 MWs and that which SPP may require on firm basis for the Facility to get designated as a network resource; therefore, only that difference would be contestable transmission capacity.⁴⁷

⁴¹ *Id.* at 34-35.

⁴² *Id.* at 35. OMPA actually says “ONEOK,” but appears to mean OG&E.

⁴³ *Id.* at 36.

⁴⁴ Offset the 225 MWs of the Facility's capacity designated as a network resource by providing 225 MW of additional transmission or reducing generation by 225 MW or a combination of the two.

⁴⁵ OMPA protest at 38-39, *quoting* Frayer Aff., Question 7.3.

⁴⁶ *Id.* at 38; *citing* *OG&E*, 108 FERC ¶ 61,004 at P 32.

⁴⁷ *Id.*

28. Protestors question Applicants' contention that the units proposed for divestiture are "economically comparable" to Spring Creek. Protestors contend that the units are not comparable in location or cost; they are located in a different part of the SPP market, on opposite sides of the constrained flowgate connecting Westar Energy with OG&E. The proposed plants are also less efficient, and are fifty or more years old. Protestors state that the proposed plants are of little value to Westar Energy, which will retire the plants if they cannot be sold.

29. OMPA also proposes that Westar Energy be required to offer it cost-based sales to remedy Westar Energy's increased market power in the Westar Energy and OG&E control areas. OMPA also requests that the Commission require a modification of the scheduling provisions, with no rate increase, to enable OMPA to compete against Westar Energy.⁴⁸

iii. Applicants' Response to Protests

30. Applicants note that protestors have not performed a delivered price test analysis to support their arguments and argue that this leaves Applicants' analysis uncontradicted. They urge the Commission to reject OMPA's "strategic bidding" and "strategic dispatch" analyses.⁴⁹ They say that SPP will probably require significant transmission upgrades in order for the Spring Creek plant to be designated as a network resource, and that the upgrades will allow new economic non-firm energy transactions to occur during the portions of the year in which Spring Creek is not operating. Applicants argue that the only mitigation necessary, if any, is the amount of transmission Westar Energy will use to import the 225 MWs.⁵⁰

31. Applicants challenge protestors' claim that the transaction will exacerbate existing constraints. The Commission's evaluation of a section 203 filing should be limited to the anticompetitive harms resulting directly from the proposed transaction, not problems that existed before, citing *Entergy Services Inc.*⁵¹

32. Applicants state that whether OMPA consents to the contract assignment is irrelevant to the Commission's findings; OMPA's argument that the 75 MWs should be attributed to Westar Energy because OMPA has not consented to the assignment is erroneous. Westar Energy says that it will only seek to have 225 MWs designated as a network resource regardless of whether the 75 MW contract is assigned, so 75 MW will

⁴⁸ *Id.* at 48.

⁴⁹ Applicants' answer at 2.

⁵⁰ *Id.* at 3.

⁵¹ 64 FERC ¶ 61,001 at 61,013, *reh'g denied*, 64 FERC ¶ 61,326 (1993).

stay in the OG&E control area either way.⁵² Applicants also clarify that their EC analysis included the full 300 MW, and that it is appropriate to exclude OMPA's firm entitlement to 75 MW from the AEC analysis.⁵³

33. Applicants say that OMPA's argument with respect to the Redbud facility is a collateral attack on the Commission's decision in *Redbud Energy LP*.⁵⁴ In that case, the Commission determined that Redbud Operating Company, LLC, is the operator of that facility. According to Westar Energy, its role as "marketing agent" for the Redbud facility does not confer operational control over the facility. It cites numerous provisions of the Redbud Energy Management Agreement (Redbud Agreement) that limit Westar Energy's authority. Therefore, the 1,200 MWs in generation from the Redbud facility should not be attributed to Westar Energy.⁵⁵

34. Applicants also refute OMPA's contention that their analysis should have assumed peak hour prices of \$150/MWh instead of \$125/MWh. First, the results were similar when their analyst used even higher market prices of \$250/MWh, and protestors have not shown the use of the \$150/MWh price would affect the analysis. According to Applicants, there are no actual hourly prices for the SPP because it does not operate centralized day-ahead and real-time markets, as do other regional transmission organizations.⁵⁶

35. Applicants contest OMPA's claim that Westar Energy's native load obligation should be calculated using the lowest seasonal peak load. Applicants' analysis examined load levels during the top ten percent of load hours during summer, winter and shoulder periods, consistent with the Commission's instructions for the delivered price test. OMPA's analysis does not appear to follow the Commission's methods for measuring native load and is not reliable.⁵⁷

36. Applicants counter OMPA's contention that if HHI were recalculated using appropriate assumptions (those urged by OMPA), greater market concentration would be found. They state that OMPA's analysis relied on the assumptions least favorable to Applicants, regardless of whether they are supported by facts, consistent with Commission policy, or even internally consistent. Even if OMPA's analysis were

⁵² Applicants' answer at 14-16.

⁵³ *Id.* at 16.

⁵⁴ 111 FERC ¶61,397 (2005).

⁵⁵ Applicants' answer at 18-21.

⁵⁶ *Id.* at 23-24.

⁵⁷ *Id.* at 24-26.

correct, it would only justify mitigation, which Westar Energy already has proposed. According to Applicants, alleged errors in their delivered price tests analysis in the Westar Energy control area would not affect mitigation, which does not depend on the size of any screen failure; mitigation is intended to restore competitive balance.⁵⁸

37. Applicants state that OMPA's concern with EC screen failures is inconsistent with current Commission policy that recognizes that the AEC measure should be weighed more heavily where, as here, a utility retains a significant native load obligation with no prospect of it being lifted.⁵⁹ Applicants contest OMPA's argument that since native load obligations are not constant, the AEC measure is not significant. Applicants allege that protestors have failed to distinguish *Nevada Power*, which supports relying more heavily on AEC than EC.⁶⁰

38. Applicants allege that OMPA misinterpreted the work papers supplied by Ms. Solomon, and that some of the analysis in the work papers is an alternative analysis, not the one Ms. Solomon relied on in arriving at her conclusions.⁶¹

39. Applicants urge the Commission to reject OMPA's "strategic bidding" argument – that Westar Energy will use the Facility to engage in strategic bidding to withhold output and raise wholesale prices. Instead, the Commission should continue its policy of examining market concentration as detailed in Appendix A of its Merger Policy Statement. Applicants claim that OMPA's strategic bidding analysis contains numerous mistakes that skew results against Westar Energy. Even with all of OMPA's erroneous assumptions, the end result shows fairly minor changes to profits. OMPA's argument unreasonably suggests that Westar Energy would risk sanctions for this minor benefit.⁶²

40. Similarly, Applicants ask the Commission to reject OMPA's strategic dispatch argument, which is that the transaction will enable Westar Energy to engage in strategic dispatch to create congestion on its interface with OG&E, thus increasing prices. According to Applicants, strategic dispatch, if successful, would raise prices by less than one-half of one percent, a minor benefit considering the risk involved in such behavior. OMPA's arguments are based on faulty assumptions, such as Ms. Frayer's failure to take into account the 75 MW contract with OMPA for output from the Spring Creek facility and her treatment of the Redbud plant as under the control of Westar Energy.⁶³

⁵⁸ *Id.* at 26-27.

⁵⁹ *Id.* at 28, citing *Nevada Power*, 113 FERC ¶ 61,265 (2005).

⁶⁰ Applicants' answer at 12-14.

⁶¹ *Id.* at 29-30.

⁶² *Id.* at 30-33.

⁶³ *Id.* at 33-37.

41. Applicants next attack OMPA's complaint that the proposed transaction will eliminate a competitor. According to Applicants, the Commission focuses on the effect a transaction will have on market concentration, not preservation of a certain number of "independent" competitors. The important issue is whether other competitors are unaffiliated with the Applicants. OMPA's argument assumes that ONEOK Energy Services has been a competitor in the Westar Energy market, but in fact ONEOK Energy Services has not made any sales into the Westar Energy control area over the past two years.⁶⁴

42. Turning to the issue of mitigation, Applicants claim that their mitigation plan is sufficient. According to Applicants, OMPA has conceded that Westar Energy's mitigation proposal restores market concentration screens to pre-acquisition levels, but alleges the plan is not sufficient to mitigate alleged harm. Westar Energy says that its proposal to construct transmission as required by the SPP in order to designate the Facility as a network resource and to replace existing transmission capacity used up as a result is adequate mitigation, citing *OG&E*.⁶⁵ Applicants contend that there is no need for the Commission to delay its decision pending the SPP determination regarding any transmission upgrades necessary to designate the Facility a network resource.

43. Applicants attack OMPA's argument that the divestiture or retirement of the Gill and Hutchinson units is inadequate mitigation because those units are not in the OG&E control area. According to Applicants, their proposal reasonably addresses the screen violations, which occur in the Westar Energy market; the fact that it would be more beneficial to OMPA to provide mitigation in the OG&E control area is irrelevant. Applicants also contest OMPA's argument that the Hutchinson and Gill plants are not economically comparable to Spring Creek, stating that the age and operating characteristics are not relevant; what is relevant is the "general location" and "cost characteristics" of the units proposed for divestiture.⁶⁶

44. Westar Energy also refutes Kansas Power Pool's argument that Westar Energy's commitment to sell power at cost-based rates is inadequate to protect the Kansas Power Pool. Applicants reiterate that mitigation is intended to protect competition, not competitors. In addition, Westar Energy's proposal to provide interim mitigation, if needed by offering cost-based power sales is not ambiguous.⁶⁷

⁶⁴ *Id.* at 37-38.

⁶⁵ 108 FERC ¶ 61,004.

⁶⁶ Applicants' answer at 43, citing *Exelon Corporation*, 113 FERC ¶ 61,299 at P 45 (2005).

⁶⁷ *Id.* at 43-44.

45. Applicants say that the Commission should not direct Westar Energy to make cost-based sales to OMPA. According to Applicants, OMPA's reliance on the Commission's market-based power sales policy in the context of section 205 proceedings is not relevant in a section 203 proceeding. The Commission's existing policy does not impose retroactive remedies on previously negotiated contracts, such as OMPA's. Applicants urge that the issue of when and where Westar Energy may be required to sell power at cost-based rates belongs in Westar Energy's pending triennial market-based rate review case.

iv. OMPA's Reply

46. OMPA alleges that Applicants have not provided all the required information, and encourages the Commission to set the matter for hearing if the Commission does not reject the application. It states that Applicants failed to identify the Redbud Agreement in their initial filing and did not provide any information regarding it until Applicants' response to OMPA's protest. OMPA also complains that its reviewing representatives were denied access to portions of the Redbud Agreement even after they signed the non-disclosure agreement. The Commission should require Westar Energy to provide OMPA with the complete Redbud Agreement, and OMPA should be given an opportunity to comment on the agreement after it has been given full access.⁶⁸

47. According to OMPA, the information to which it has been denied access is highly relevant, and includes pricing terms of the Redbud Agreement. The calculation of Westar Energy's compensation for marketing services affects Westar Energy's incentives to market Redbud's generation.⁶⁹

48. OMPA questions Westar Energy's motive in seeking to buy the Spring Creek plant: "Westar Energy's willingness to sell or retire capacity within its control area in order to acquire capacity outside its control area, the use of which as a network resource apparently will necessitate considerable transmission upgrades, calls into question the *bona fides* of Westar Energy's claimed need."⁷⁰ OMPA also questions whether Westar Energy actually intends to designate Spring Creek as a network resource. Westar Energy may intend to use Spring Creek to participate in other markets, including SPP's proposed

⁶⁸ OMPA reply at 4-6.

⁶⁹ *Id.* at 6-7. This information was provided to OMPA representatives after the Commission issued its order directing release of the information.

⁷⁰ *Id.* at 7.

Energy Imbalance Service market.⁷¹ OMPA encourages the Commission to send this case to hearing to resolve some of these questions.⁷²

49. OMPA continues to argue that the Redbud Agreement confers control on Westar Energy, and, therefore, that the plant should be attributed to Westar Energy. Characterizing Westar Energy as Redbud's "agent" does not mean Westar Energy does not have control. The Redbud Agreement effectively merges Redbud's marketing operations with Westar Energy's, giving Westar Energy the ability to control whether the capacity reaches the market. For example, OMPA points to section 2.3 of the Redbud Agreement, which states that Westar Energy "shall be the contracting party with all respective Third Party suppliers, Power Purchasers, Transporters and Transmission Providers, and under all Fuel Supply Agreements, Power Sale Agreements, Related Agreements, and agreements for Risk Management Transactions and Other Transactions." Section 2.5 prevents Redbud from marketing output from the plant without Westar Energy's involvement. Section 5.6 provides for "Co-Location" of Redbud and Westar Energy personnel. Section 7.4(c) gives Westar Energy the sole right to market Ancillary Services except for those that are solely within Redbud's authority to market as a power generator. OMPA also claims that Exhibit D, Operating and Dispatch Procedures, specifies that dispatch instructions come from Westar Energy.⁷³

50. OMPA alleges that under the Redbud Agreement, Redbud would benefit if Westar Energy successfully raised prices in the OG&E control area, where the Redbud output is sold. Even if Westar Energy could not withhold output from Redbud itself, it could raise prices by withholding Spring Creek output, benefiting Redbud and Westar Energy to the extent that each of their compensation is tied to Redbud's revenues. OMPA states that it needs access to the entire Redbud Agreement because of its importance to the analysis.⁷⁴

⁷¹ The Energy Imbalance Service market will give SPP market participants access to a broader imbalance energy market to address scheduling deviations, instead of paying for regulation services under the SPP OATT. OMPA argues that scheduling restrictions on the ONEOK-OMPA contract will likely make it impossible for OMPA to follow SPP dispatch instructions, thus preventing it from using Spring Creek to participate in the Energy Imbalance Service market, preventing OMPA from lowering its costs. The contract restrictions will make it less likely that OMPA will schedule energy out of Spring Creek at all. OMPA asserts that Westar will have full control of the plant to bid into (or withhold from) the Energy Imbalance Service market.

⁷² OMPA reply at 8.

⁷³ *Id.* at 10-11.

⁷⁴ *Id.* at 11-12.

51. Next, OMPA defends other proposed adjustments to the competitive screen analysis submitted by Applicants. It continues to assert that the full 300 MW output of Spring Creek should be attributed to Westar Energy for purposes of the AEC analysis, claiming that unless OMPA consents, Westar Energy will not assume ONEOK Energy Services' 75 MW obligation to OMPA.⁷⁵ OMPA refutes Applicants' claim that the issue of control is not relevant to the AEC analysis, stating that EC is the starting point for AEC, and EC is defined as "'the amount of generating capacity owned or controlled by a potential supplier'"⁷⁶ Although native load commitments are deducted from EC to derive AEC, OMPA alleges that the ONEOK Energy Services–OMPA contract does not impose a native load commitment on Westar Energy.⁷⁷

52. Additionally, OMPA alleges that Westar Energy will be able to bid the additional 75 MWs of capacity into the proposed hourly EIS market because of the inflexible scheduling provisions in the ONEOK Energy Services–OMPA contract, which preclude OMPA from bidding into the proposed hourly market.⁷⁸

53. OMPA contends that Westar Energy's long-term purchase and sales agreements warrant closer examination in order to determine what should be attributed to Westar Energy. OMPA states that Applicants have not adequately supported their claim that all of Westar Energy's long-term sales qualify as native load obligations.⁷⁹

54. OMPA defends its argument that Applicants' peak hour price assumptions were incorrect and its use of Electric Reliability Council of Texas prices to extrapolate the relationship between peak hour prices and prices during other hours of the day and apply the relationship to SPP prices. It defends its approach as consistent with the Commission's position on proxies.⁸⁰ OMPA continues to assert that Applicants' use of a \$125 MWh price instead of the \$150 MWh advocated by OMPA excludes 264 MWs of capacity, understating Westar Energy's market share. Although Applicants ran an analysis at \$250 MWh super peak, that analysis brings other capacity into the market, diluting Westar Energy's market share. Therefore, the \$250 MWh analysis does not take care of any problems from the use of the \$125 MWh price.⁸¹

⁷⁵ *Id.* at 12-13.

⁷⁶ *Id.* at 13, quoting 18 C.F.R. § 33.3(c)(4)(i)(A).

⁷⁷ *Id.* at 13.

⁷⁸ *Id.* at 14.

⁷⁹ *Id.* at 14-15.

⁸⁰ *Id.* at 16-17.

⁸¹ *Id.* at 18.

55. OMPA explains that it did not re-run the delivered price test because it did not have access to CRA International's proprietary model, but says that the Commission and Applicants are able to re-run the analysis with OMPA's proposed modifications.⁸² Applicants could have re-run the model using the proposed adjustments to demonstrate that the transaction would pass the competitive screen. Applicants may not have made such a claim because they ran the analysis and the results were not favorable to their position.⁸³

56. OMPA asserts that its strategic bidding analysis should be considered, and that, contrary to Appellants' claim, the Commission has undertaken such supplemental analysis in the past, citing *Duke Energy Corp. and Cinergy Corp.*⁸⁴ OMPA also states that Ms. Frayer re-ran her strategic bidding model assuming that Redbud is independently controlled, and determined that Westar Energy would be motivated to use Spring Creek capacity more often if it did not control Redbud. This allows Westar Energy to "self-manage" congestion and artificially increase prices in its control area. Although gross profits would be less, the incremental effect of the Spring Creek acquisition would be more significant. OMPA also re-ran the ConjectureMod⁸⁵ assuming that Westar Energy had an obligation of 75 MWs to OMPA and found that the effect of the contract was "inconsequential," with post-acquisition profits still substantially above the status quo.⁸⁶

57. OMPA encourages the Commission to consider price increases of just a few percentage points, noting that the five percent price increase is used in analyzing mergers, it is not a tolerance for price increases. OMPA also challenges Westar Energy's assertion that Westar Energy's obligation to share wholesale market revenues with retail customers minimizes its incentive to engage in strategic behavior, noting that the obligation to share only applies to asset-based sales. In addition, Westar Energy can keep wholesale revenues that exceed the three-year average.⁸⁷

58. OMPA responds to Applicants' query regarding whether Westar Energy would engage in strategic bidding given the risk of violating anti-manipulation rules. It says that OMPA's expert considered such risks in her analysis. OMPA states that Westar Energy would have to engage in fraud or deceit in order to be guilty of market manipulation, but that Westar Energy could behave in way that would raise prices

⁸² *Id.* at 18.

⁸³ *Id.* at 19.

⁸⁴ 114 FERC ¶ 61,297, P 74, n. 62 (2005); OMPA reply at 20.

⁸⁵ An iterative model of strategic bidding developed by London Economics.

⁸⁶ OMPA reply at 21-22.

⁸⁷ *Id.* at 23.

without using fraud or deceit. In addition, there is no guarantee that Westar Energy would be caught if it engaged in such behavior; therefore, there is still a risk of strategic bidding.⁸⁸

59. OMPA distinguishes *Nevada Power*⁸⁹ based on the fact that Nevada Power was a significant purchaser in the wholesale market, diminishing its incentive to raise prices in those markets, while Westar Energy is apparently long in capacity. In addition, the proposed transaction in *Nevada Power* freed up transmission capacity. Moreover, OMPA states that the Commission was less concerned about screen failures in *Nevada Power* because the market was not highly concentrated and Nevada Power's market share was not significant.⁹⁰

60. OMPA refutes Applicants' claim that the Commission is not concerned about the loss of a competitor when conducting a section 203 analysis. It notes that the Commission has found that "the elimination of a competitor may harm competition by increasing the merged firm's ability to raise price by withholding output."⁹¹ OMPA also challenges Applicants' assertion that there is no loss of a competitor in this case because ONEOK Energy Services has not competed against Westar Energy and will remain a competitor after it sells the Spring Creek facility. OMPA states that ONEOK Energy Services' 2004 and 2005 Electric Quarterly Reports show sales in markets common to Westar Energy, such as OG&E. In addition, OMPA disagrees with Appellants' claim that ONEOK will continue to be a competitor, given that ONEOK Energy Services will have sold its only plant in the SPP market.⁹²

61. OMPA also explains why it did not oppose OG&E's acquisition of the NRG McClain facility. In that case, OMPA was co-owner of the facility in question, and NRG McClain had filed for Chapter 11 bankruptcy protection. OMPA wanted the facility to be purchased by OG&E to ensure that OMPA could use it to serve its customers. OMPA asks the Commission to disregard Applicants' argument that its behavior is inconsistent in the two cases.⁹³

⁸⁸ *Id.* at 24.

⁸⁹ 113 FERC ¶ 61,265.

⁹⁰ OMPA reply at 25.

⁹¹ *Id.* at 26, quoting *Exelon Corp.*, 113 FERC ¶ 61,299, P 55 (other citations omitted).

⁹² *Id.* at 26.

⁹³ *Id.* at 26-27.

62. Turning to the issue of mitigation, OMPA states that Applicants have not shown that their proposed mitigation will restore competition, only that it will restore megawatts. OMPA continues to argue that a megawatt-for-megawatt addition of transmission will not necessarily eliminate Westar Energy's ability and incentive to engage in strategic bidding. OMPA's expert has concluded that "transmission expansion is not enough to eradicate Westar Energy's strategic behavior and resulting price increases due to the acquisition."⁹⁴ In addition, OMPA says that divestiture of the Gill and Hutchinson units would not be effective mitigation because the units are on the opposite side of a constrained interface from the Spring Creek facility. OMPA also asserts that the Gill and Hutchinson units are older and more costly to run, and, thus, are not comparable to Spring Creek.⁹⁵

63. OMPA defended its request that the Commission mitigate Westar Energy's increased market dominance by modifying the ONEOK Energy Services agreement to allow OMPA to request schedule changes with a frequency that would allow it to compete with Westar Energy in the Energy Imbalance Service market. OMPA disputes Applicants' argument that modification of the ONEOK Energy Services – OMPA contract must meet the *Mobile-Sierra* public interest standard. According to OMPA, if the parties agree to a contractual change, the public interest standard is not relevant. Therefore, if Westar Energy agrees to the change, such a review is not necessary.⁹⁶

v. Applicants' Reply

64. Applicants state that OMPA's argument with respect to control of the Redbud Facility continues to be misguided. According to Westar Energy, its role as marketing agent for the Redbud Facility does not confer operational control over the facility. It states that the Redbud Agreement explicitly withholds control from Westar Energy as a matter of law.

65. Applicants reiterate their argument that protestors have failed to distinguish *Nevada Power*.⁹⁷ They state that using the AEC measure, there is only a single screen failure, which arises only when Westar Energy designates Spring Creek as a network resource and constructs the transmission upgrades necessary to do so. Citing *OG&E*,⁹⁸

⁹⁴ *Id.* at 28, quoting Frayer Supplemental Testimony, Question 3.5.

⁹⁵ *Id.* at 28.

⁹⁶ *Id.* at 28-29.

⁹⁷ 113 FERC ¶ 61,265.

⁹⁸ 108 FERC ¶ 61,004.

Applicants argue that the fact that Westar Energy will replace any firm import capability “used up” by designating Spring Creek as a network resource fully addresses any harm to competition.⁹⁹

vi. Protestor’s Supplemental Comments

66. On April 19, 2006, OMPA submitted its response relating to the protected information released under the Commission’s order. OMPA claims that the Redbud Agreement gives Westar Energy “strong incentives to increase prices in areas where Westar [Energy] markets the Redbud output, e.g., the [OG&E] control area, including using withholding from the Spring Creek plant to do so.”¹⁰⁰ Alternatively, Westar Energy could withhold Redbud output to raise prices. According to OMPA, Redbud would be unlikely to complain if Westar Energy engaged in such practices because the practices would raise Redbud’s gross profits. OMPA argues that Westar Energy’s acquisition of the Spring Creek facility would increase Westar Energy’s incentive to operate its generation facilities in a manner that limits transmission availability across the OGE-Westar Energy interface, enabling Westar Energy to prevent OMPA from serving the Kansas Power Pool.¹⁰¹

67. According to OMPA, Westar Energy’s transmission upgrade mitigation proposal is insufficient. OMPA notes that it appears that none of the cost of the upgrades will be assigned to Westar Energy. OMPA also alleges that SPP’s newly released aggregate study indicates that Westar Energy sought designation of 300 MWs of Spring Creek as a network resource, not 225 MWs, as claimed by Westar Energy. OMPA urges the Commission to assume that Westar Energy controls the Redbud capacity for purposes of analyzing the competitive effects of Westar Energy’s acquisition of the Facility and whether Applicants’ proposed mitigation is sufficient.¹⁰²

vii. Applicants’ Reply to Supplemental Comments

68. On April 25, 2006, Applicants filed a reply to OMPA’s supplemental comments regarding the Redbud Agreement. Applicants argue that OMPA has failed to show that Westar Energy’s compensation under the Redbud Agreement overrides explicit contractual provisions giving Redbud ownership and control over the Redbud facility.¹⁰³ Applicants state that Westar Energy cannot unilaterally determine when and to whom the

⁹⁹ Applicants’ reply at 2.

¹⁰⁰ OMPA supplemental comments at 4.

¹⁰¹ *Id.* at 5.

¹⁰² *Id.* at 5-6.

¹⁰³ Applicants’ reply to comments at 1.

power is sold, as the Redbud Agreement gives Redbud the right to review and approve all transactions, propose transactions, and terminate the agreement if dissatisfied with Westar Energy's performance.¹⁰⁴

69. Applicants also discount OMPA's argument regarding Westar Energy's profit incentives; OMPA has not shown that Westar Energy can raise prices above competitive levels. Redbud's ability to market the power itself undermines Westar Energy's ability to engage in an economic withholding strategy, thus diminishing Westar Energy's ability to increase prices.¹⁰⁵ Applicants also challenge OMPA's contention that Redbud will benefit if Westar Energy withholds output to maximize profits from the Redbud facility. Even if this is the case, it is the case now, before Westar Energy's purchase of the Spring Creek facility, so the transaction would not affect competition. Moreover, OMPA has not offered any evidence that Redbud owns any other generating facilities that would benefit from a withholding strategy. Applicants contend that absent such ownership, OMPA's argument is speculative, as it is based on Redbud foregoing profits (by withholding output) "in the uncertain hope that it may recoup the short-term losses through higher profits in the future."¹⁰⁶

70. Applicants also refute OMPA's claim that Westar Energy has an incentive to raise prices for power sold in its control area. Applicants state that Westar Energy cannot artificially raise wholesale prices in its control area, since sales in its control area are subject to cost-based mitigation in Westar Energy's triennial market-based rate proceeding.¹⁰⁷ Lastly, Applicants address OMPA's allegation that Westar Energy is actually reserving 300 MWs of import capability into its home control area, not 225 MWs. According to Applicants, Westar Energy has requested 225 MWs of import capability through May 2016 and requests 300 MWs of import capability beginning in June 2016, after OMPA's ONEOK contract will have expired.¹⁰⁸

¹⁰⁴ *Id.* at 2, citing *Reporting Requirement for Changes in Status for Public Utilities with Market-Based Rate Authority*, Order No. 652, 111 FERC ¶ 61,413 at P 17 (probably should be P 18) (2005).

¹⁰⁵ *Id.* at 3.

¹⁰⁶ *Id.* at 3-4.

¹⁰⁷ *Id.* at 4, citing *Westar Energy, Inc. and Kansas Gas and Electric Company*, 110 FERC ¶ 61,316 at P 12 (does not appear to be the relevant paragraph) (2005).

¹⁰⁸ *Id.* at 4.

viii. Commission Determination

71. We find that Applicants have failed to show that the acquisition, with their proposed mitigation, will not adversely affect competition in any relevant market. If the Spring Creek Facility does not become a network resource, the transaction passes the Competitive Analysis Screen. As discussed below, if the Facility is a network resource, additional transmission upgrades will be necessary to mitigate any adverse effect on competition.

72. Applicants' analysis indicates that without mitigation, the transaction would adversely affect competition if the Facility is a network resource. We do agree with Applicants that AEC is more relevant than EC in this case. However, this case differs from *Nevada Power* in several respects that cause us to be concerned about the effect on competition even based on AEC. Applicants point out that in *Nevada Power*, the Commission found that AEC should be given more weight than EC because of Nevada Power's significant native load obligation and lack of prospect of that obligation being lifted. In *Nevada Power*, however, the screen failure for AEC was in the Spring Peak season in the Nevada Power market, where the post-acquisition market was only moderately concentrated and Nevada Power's market share was approximately 21 percent. We stated that, in that case, the single screen failure for AEC did not indicate an adverse effect on competition, but we would have been concerned with systematic screen failures in the Nevada Power market if the market was highly concentrated and Nevada Power had a more significant market share. We agree with Applicants that AEC is the more relevant measure in this case. However, the market conditions also differ in this case. While we recognize that one screen failure in the four peak seasons analyzed by Applicants is arguably not "systematic," in this case both the level and the increase in market concentration are much greater than in *Nevada Power*. Specifically, in the Winter Super Peak period, Westar Energy has a 42 percent market share, the market is highly concentrated, and the transaction increases market concentration by 381 HHI. In addition, the unit is a peaking facility, and wholesale customers have protested on grounds of harm to competition in the relevant market – super peak energy in the Westar Energy control area, representing 25 percent of the hours in the study period.¹⁰⁹ Therefore, on balance, we find that the analysis does show harm to competition after integration, and will require mitigation.

73. We reject OMPA's arguments regarding Westar Energy's motives in seeking to buy the Spring Creek Facility and whether Westar Energy will, in fact, seek to designate it as a network resource. Under section 203 of the FPA, Westar Energy does not need to justify its motives; rather it needs to show that the transaction is consistent with the

¹⁰⁹ The Winter Super Peak period is the top 10 percent of peak load hours for December, January and February. Application Exhibit W-1 at 20.

public interest. Moreover, Applicants analyze the effect on competition if Spring Creek is not designated a network facility and show that the transaction does pass the Competitive Analysis Screen.

74. We reject OMPA's claim that Westar Energy's native load obligation should be calculated using the lowest seasonal peak load. Applicants' analysis examined load levels during the top ten percent of load hours during summer, winter and shoulder periods. This is consistent with the Commission Appendix A methodology for the delivered price test; the native load deduction should match the period being studied. OMPA is apparently confusing the native load deduction with the one used in the initial screening analysis for market-based rate applications. In the delivered price test, the relevant product--energy at multiple seasons and load levels--is more narrowly defined than in the initial screens for market-based rate applications, and the native load deduction corresponds to the appropriate season and load level.

75. OMPA argues that Applicants' use of a \$125 per MWh price during periods other than the extreme summer super peak (instead of OMPA's proposed \$150 per MWh price) excludes 264 MWs of Westar Energy's capacity, understating Westar Energy's market share thus understating the competitive effect of the transaction. OMPA further states that, although Applicants ran an analysis using \$250 per MWh for the extreme summer super peak, that analysis brings other capacity into the market, diluting Westar Energy's market share, thus reducing market concentration. We are aware that the assumed market price can significantly affect the results of the delivered price test, and therefore encourage all applicants to provide sensitivity tests in their analysis. OMPA's expert correctly points out that Westar Energy owns a number of peaking facilities with running costs between \$125 per MWh and \$150 per MWh. However, Applicants' expert based the market price in the delivered price test on reported prices for 2005 with escalations for increased natural gas prices in 2006, with maximum prices of \$110 per MWh, \$103 per MWh, and \$117 per MWh for the peak winter, shoulder and summer periods, respectively.¹¹⁰ Based on those prices, the \$125 per MWh price is more accurate than OMPA's proposed \$150 per MWh. It is a conservative estimate in that it is high enough to make Spring Creek an economic resource in all peak periods, even though the Facility is only expected to run in the summer peak.¹¹¹ Finally, we note that a number of Westar

¹¹⁰ Exhibit W-1, Workpapers of Ms. Julie Solomon, SPP-N and HHub Prices.xls.

¹¹¹ The estimated running cost for Spring Creek used in the delivered price test is \$107.40 per MWh. Exhibit W-1 at 22.

Energy's generating units with running costs between \$125 per MWh and \$150 per MWh are the ones that OMPA argues are not economically comparable to the Spring Creek unit because of their high heat rates.¹¹²

76. OMPA raises a number of issues regarding Westar Energy's role as Energy Manager for the Redbud facility. It argues that Westar Energy has operational control of the facility and therefore that the capacity of the facility should be assigned to Westar Energy in the delivered price test. In response, Applicants cite numerous contractual provisions that limit Westar Energy's authority in its role as marketing agent for the Redbud facility. Redbud retains the sole right and responsibility to, among other things: (1) establish all marketing plans for Power, Fuel or Ancillary Services and approve or disapprove of any deviations from such Marketing Plans that may be recommended by the Energy Manager (Westar Energy) from time to time; (2) establish short-term and long-term fuel and energy trading strategies; (3) establish Risk Management Policies and Strategies; (4) approve all short- and long-term fuel and power transactions; (5) determine the amount of otherwise non-contracted power available from the facility at any time; and (6) determine the amount of fuel to be supplied to the facility.¹¹³ Moreover, the Commission has determined that Redbud Operating Company, LLC, is the operator of that facility.¹¹⁴ Therefore, we find that Westar Energy does not control the Redbud facility and that the 1,200 MWs of generating capacity of the Redbud facility should not be attributed to Westar Energy in the delivered price test.

77. We are not convinced by OMPA's argument that a strategic bidding analysis should be considered in assessing of the effect of the acquisition on competition. As we stated in *Exelon*, the Commission's analysis focuses on a merger's effect on competitive conditions in the market.¹¹⁵ In this case, the harm to competition results from the elimination of a competitor, and the mitigation will give access to additional competing supply in the Westar Energy control area.

78. On the issue of mitigation, OMPA argues that 300 MWs is the correct measure of the available economic capacity that should be assigned to Westar Energy as a result of the Spring Creek acquisition, and that, therefore, additional mitigation is required. However, the screen failure for AEC will only occur if Spring Creek is a network resource, and Westar Energy states that it will only seek to have 225 MWs designated as

¹¹² Four of the five proposed units--Hutchinson 1, Hutchinson 2, Hutchinson 3, and Murray Gill 1--have running costs between \$125 per MWh and \$150 per MWh. OMPA Protest, affidavit of Ms. Julie Frayer at 83.

¹¹³ Applicants' answer at 20.

¹¹⁴ *Redbud Energy LP*, 111 FERC ¶ 61,397 (2005).

¹¹⁵ *Exelon*, 113 FERC ¶ 61,299 at P 131.

a network resource regardless of whether the 75 MW contract is assigned, so 75 MWs will stay in the OG&E control area either way. Even if Westar Energy did retain control of the other 75 MWs of Spring Creek, those 75 MWs would be competing for scarce transmission for imports into the Westar Energy control area, and a pro rata allocation of transmission would result in only about 10 MWs of additional available economic capacity.¹¹⁶ Therefore, we find that OMPA's argument is not relevant to our determination of the appropriate mitigation in this case.

79. However, as noted by OMPA, Westar Energy may seek to designate the additional 75 MWs of Spring Creek as a network resource upon expiration of the 75 MW contract in 2016. Given the uncertainty regarding market conditions ten years from now, we will not require mitigation at this time. However, we note that under section 203(b) of the FPA, we can impose additional conditions in the future to ensure that the transaction is consistent with the public interest.

80. OMPA argues that because, under the Redbud Agreement, Westar Energy's compensation is tied to Redbud's revenues, Westar Energy would have the incentive to raise prices in the OG&E control area by withholding Spring Creek output. We reject OMPA's argument because the mitigation ensures that competing suppliers would be able to get transmission to defeat any attempted price increase by Westar Energy. Therefore, the proposed transaction, as mitigated, would not increase Westar Energy's ability or incentive to engage in the withholding strategy posited by OMPA.

81. Applicants state that Westar Energy likely will have to provide transmission upgrades in order to get the Facility treated as a network resource and that if 225 MWs of upgrades are necessary to designate 225 MWs of the Facility's capacity as a Westar Energy network resource, the upgrades will preserve the current competitive balance."¹¹⁷ We disagree. We recognize that in OG&E we stated that a transmission upgrade that creates additional ATC offsetting the loss of competing capacity will mitigate the harm to competition resulting from a generation acquisition.¹¹⁸ However, in this case, Spring Creek has not been a significant competitor in the Westar Energy market because of transmission limitations. Thus, the harm to competition here results not from the elimination of a competitor, but from the increased size of Westar Energy, which has a 42 percent market share, and the associated 381 HHI increase in a highly-concentrated market. As OMPA points out, in this case a simple "MW-for-MW" transmission

¹¹⁶ Based on ONEOK Energy Service's pre-transaction allocation of 39 MWs for import into the Westar Energy control area from the 300 MW Spring Creek Facility in Exhibit W-6, 75 MWs of available economic capacity would receive one fourth of that amount, or approximately 9.75 MWs.

¹¹⁷ Application at 9.

¹¹⁸ *OG&E*, 108 FERC ¶ 61,004 at P32.

increase is not sufficient mitigation for any harm to competition related to the transaction. Therefore, we find that in order to mitigate the harm to competition, Westar Energy must increase transfer capability into the Westar Energy market by an amount that will bring the market concentration within screening tolerances (100 HHI for a moderately concentrated market) of the pre-transaction level.¹¹⁹ Based on Applicants' analysis, a total of approximately 325 MWs of increased transfer capacity will be required to bring market concentration within those tolerances.¹²⁰ Accordingly, Westar Energy shall make a compliance filing to the Commission within 30 days after SPP issues its order on any Westar Energy application to have 225 MWs from the Spring Creek Facility designated as a network resource. Such filing shall demonstrate that any transmission upgrades required by the SPP as a condition of the designation as a network resource will provide sufficient additional ATC with the Westar Energy load as the designated point of delivery, using the SPP planning model under winter conditions, to restore market concentration in the Winter Super Peak period to within 100 HHI of the pre-transaction

¹¹⁹ See *Exelon Corporation and Public Service Enterprise Corporation, Inc.*, 112 FERC ¶ 61,011, *reh'g denied*, 113 FERC ¶ 61,299 (2005). The *Merger Policy Statement* (at fn 33) addresses three ranges of market concentration as described in the FTC/DOJ Horizontal Merger Guidelines: (1) an unconcentrated post-merger market--if the post-merger HHI is below 1000, regardless of the change in HHI the merger is unlikely to have adverse competitive effects; (2) a moderately concentrated post-merger market--if the post-merger HHI ranges from 1000 to 1800 and the change in HHI is greater than 100, the merger potentially raises significant competitive concerns; and (3) a highly concentrated post-merger market--if the post-merger HHI exceeds 1800 and the change in the HHI exceeds 50, the merger potentially raises significant competitive concerns; if the change in HHI exceeds 100, it is presumed that the merger is likely to create or enhance market power.

¹²⁰ For the Winter Super Peak period, without transmission upgrades, the HHI increases from 1,653 to 2,035, with Westar Energy's market share increasing from 37 percent to 40 percent. According to Applicants' witness's work papers, the Simultaneous Import Limit (SIL) into the Westar Energy market was 2,650 MWs in the Winter Peak, but without any upgrades would drop by as much as 225 MWs to 2,425 MWs, due to the designation of Spring Creek as a network resource. Based on those values, an increase in the SIL of 325 MWs bringing the total to 2,750 MWs would bring the HHI to within screening tolerances (less than 1,753 HHI, which would be a transaction-related increase of less than 100 HHI in a moderately concentrated market).

level.¹²¹ The additional ATC created by the upgrades can provide increased access to competitive suppliers in many season and load conditions, which will benefit competition in those periods.

82. Because Spring Creek will not be a network resource until the necessary transmission upgrades are complete, it is likely that no interim mitigation will be necessary, since the transaction cannot harm competition before the Facility becomes a network resource. However, if Spring Creek is designated a network resource with less than the required MWs of increased ATC, there would be a need for interim mitigation. In that case, the interim period would be the time between the date Spring Creek is designated a network resource and the date Westar Energy completes the necessary transmission upgrades. If interim mitigation is necessary, we will rely on Applicants' proposal to offer peaking energy and/or capacity at incremental cost plus 10 percent for energy sales, or at an embedded "up to" rate reflecting Spring Creek's costs for capacity and energy sales, because the requirement to offer at a price based on marginal cost eliminates Westar's ability to exercise market power through either economic or physical withholding.¹²² We recognize that transmission upgrades can take a long time to complete and have imposed interim mitigation in cases such as *OG&E* to ensure that competition is not harmed.¹²³

83. We reject Applicants' proposal that they have the option of generation divestiture instead of transmission upgrades. We agree with OMPA that the Gill and Hutchinson units that Applicants have offered to divest are not economically comparable to the Spring Creek facility. Divestiture of those units, which Applicants acknowledge are likely to be retired, would not adequately mitigate the harm to competition resulting from the Spring Creek acquisition.

84. Finally, Applicants have shown that the proposed transaction will not have adverse competitive effects related to vertical market power. Westar Energy's transmission facilities are under the functional control of the SPP, so Westar Energy cannot use its transmission assets to harm competition in wholesale electricity markets. In addition, Westar Energy does not own or control any inputs to generation; therefore it cannot harm competition by raising rivals' costs or erecting entry barriers.

¹²¹ The Competitive Analysis Screen failure for AEC was in the winter peak period. The requirement that Applicants make such a showing is consistent with the Commission's approach in *Exelon Corporation and Public Service Enterprise Corporation, Inc.*, 112 FERC ¶ 61,011, *reh'g denied*, 113 FERC ¶ 61,299.

¹²² Application, Exhibit W-1 at 8-9.

¹²³ *OG&E*, 108 FERC ¶ 61,004 at PP 33-34.

2. Effect on Rates

a. Applicants' Analysis

85. Applicants state that the proposed transaction will have no adverse impact on rates. Westar Energy does not propose to change the rates it charges any captive wholesale customer as a result of the proposed transaction. It does not propose to change the rate OMPA is paying under the ONEOK Energy Services Power Purchase Agreement when the contract is transferred to Westar Energy. Westar Energy states that it may sell the remaining output of the Facility at negotiated, market-based rates in control areas where it is authorized to make such sales, and may sell output as authorized by the Commission in the pending triennial market-based rate review proceeding¹²⁴ in other control areas.

b. Protests

86. OMPA states that the proposed transaction would adversely affect rates. The fact that its rates may not rise does not mean it will not lose in the transaction. According to OMPA, it selected ONEOK Energy Services because of the company's solid reputation and credit rating and because ONEOK Energy Services was its own gas supplier to the Spring Creek facility.¹²⁵ OMPA claims that Westar Energy lacks ONEOK Energy Services' gas contracts and market acumen, and that OMPA would not have voluntarily contracted with Westar Energy; OMPA has a greater concern with non-performance with Westar Energy than it did with ONEOK Energy Services. OMPA also says that its right to decline to consent to contract assignment may be diminished by the ONEOK Energy Services-Westar Energy Asset Purchase Agreement.¹²⁶ OMPA states that it has been unable to find a supplier willing to take on a replacement long-term 75 MW contract, and that OG&E has told it that OG&E lacks capacity to sell on those terms. Without viable alternatives, OMPA will be unable to protect itself from Westar Energy's negotiating and market power, thus adversely affecting its rates.¹²⁷

87. OMPA requests that the Commission require Westar Energy and ONEOK Energy Services to indemnify and hold it harmless from any increased costs associated with Westar Energy's acquisition of the Spring Creek plant, including court costs associated with legal action OMPA may take to enforce its rights under the contract.¹²⁸

¹²⁴ *Westar Energy, Inc.*, 110 FERC ¶ 61,316 (2005).

¹²⁵ OMPA protest at 43.

¹²⁶ *Id.* at 44.

¹²⁷ *Id.* at 44-45.

¹²⁸ *Id.* at 48.

c. Applicants' Response to Protests

88. According to Applicants, OMPA does not specify how any of its concerns will affect rates. Applicants encourage the Commission to deny OMPA's request to modify the contract. OMPA has asked for contractual indemnification rights and for removal of scheduling restrictions it agreed to a few years ago. According to Applicants, OMPA has not met the *Mobile-Sierra*¹²⁹ standard for modification of fixed rate contracts.

d. Protestor's Reply

89. OMPA continues to argue that Westar Energy's inferior credit rating will impair Westar Energy's ability to perform its contract obligations to OMPA, adversely affecting rates, terms and conditions of the contract. OMPA refers to a 1999 contract under which OMPA pre-paid Westar Energy for capacity. That contract required that Westar Energy fund an escrow account in case its credit dropped, which it did, triggering the funding obligation, which is still in effect. OMPA states that while it has no detailed knowledge of ONEOK Energy Services' credit arrangements, Westar Energy's credit is clearly inferior to that of ONEOK Energy Services, making the assignment a bad deal for OMPA.

e. Commission's Determination

90. Applicants have shown that the proposed transaction will not adversely affect rates. The proposed transaction will not result in Westar Energy changing the rates it charges any captive wholesale customer. OMPA argues that because Westar Energy lacks the business acumen and creditworthiness of ONEOK Energy Services, OMPA will pay higher rates under its 75 MW Power Purchase Agreement with ONEOK Energy Services, which will be transferred to Westar Energy. However, the ONEOK contract runs until 2016 at a fixed rate, and Westar Energy commits not to attempt to change that rate. We are not persuaded by OMPA's argument that its rates may be affected because, unlike ONEOK Energy Services, Westar Energy does not have its own natural gas supply. There is a competitive natural gas market in Oklahoma from which Westar Energy can procure the natural gas for the Spring Creek plant. Again, Westar Energy's commitment not to attempt to change the contract rate protects OMPA. Finally, OMPA can refuse to consent to assignment of the Power Purchase Agreement to Westar Energy.

¹²⁹ *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 345 (1956) (*Mobile*); and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) (*Sierra*).

3. Effect on Regulation

a. Applicants' Analysis

91. Applicants claim that there will be no adverse effect on this Commission's regulation because of the repeal of the Public Utility Holding Company Act of 1935. Additionally, the transaction does not require state commission approval.

b. Commission Determination

92. We find that the transaction will not have an effect on Commission regulation.¹³⁰ In addition, the transaction will not impair any state's ability to regulate either Westar Energy or ONEOK Energy Services. We note that no state commission intervened in the proceeding.

4. Cross-Subsidization

a. Applicants' Analysis

93. Applicants state that the proposed transaction does not involve a non-utility associate company of Westar Energy, and 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. As required by Order No. 669, Applicants verify that the proposed transaction does not result in, at the time of the transaction or in the future: (1) transfers of facilities between a traditional utility associate company with wholesale or retail customers served under cost-based regulation and an associate company; (2) new issuances of securities by traditional utility associate companies with wholesale or retail customers served under cost-based regulation for the benefit of an associate company; (3) new pledges or encumbrances or assets of a traditional utility associate company with wholesale or retail customers served under cost-based regulation for the benefit of an associate company; (4) new affiliate contracts between non-utility associate companies and traditional utility associate companies with wholesale or retail customers served under cost-based regulation, other than non-power goods and services agreements subject to review under sections 205 and 206 of the FPA.

b. Commission Determination

94. As demonstrated by the verifications above, the proposed transaction does not raise any concern with respect to cross-subsidization.¹³¹

¹³⁰ Order No. 669 at P 10.

¹³¹ *Id.* at PP 164-171.

The Commission orders:

(A) The proposed transaction is authorized, subject to Commission acceptance of the Applicants' compliance filings as discussed in the body of this order.

(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 new pending or which may come before this Commission.

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

(D) 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;

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

(F) Westar Energy shall make a compliance filing to the Commission within 30 days after SPP issues its order on any Westar Energy application to have 225 MWs from the Spring Creek Facility designated as a network resource. Such filing shall demonstrate that any transmission upgrades required by the SPP as a condition of the designation as a network resource will provide sufficient additional ATC with the Westar Energy load as the designated point of delivery, using the SPP planning model under winter conditions, to restore market concentration in the Winter Super Peak period to within 100 HHI of the pre-transaction level.

(G) If Spring Creek is designated as a network resource with insufficient increased ATC to restore market concentration in the Winter Super Peak period to within 100 HHI of the pre-transaction level, Westar Energy must pay for additional transmission upgrades to provide sufficient additional ATC with the Westar Energy load as the designated point of delivery to restore market concentration in the Winter Super Peak period to within 100 HHI of the pre-transactional level. If the Spring Creek Facility is designated a network resource before the permanent mitigation is in place, then interim mitigation will be necessary, and Applicants' proposal to offer peaking energy and/or capacity at incremental cost plus 10 percent for energy sales, or at an embedded "up to" rate reflecting Spring Creek's costs for capacity and energy sales, will provide such mitigation.

(H) Westar Energy, Inc. shall account for the acquisition of the facilities in accordance with Electric Plant Instruction No. 5 and Account 102, Electric Plant Purchased or Sold, of the Uniform System of Accounts. Westar Energy must submit its proposed accounting within six months of the date that the transfer is consummated. In addition, the accounting submission must provide all accounting entries related to the acquisition that were made to the books and records, along with appropriate narrative explanations describing the basis for the entries.

(I) Applicants shall notify the Commission within 10 days of the date of the disposition and acquisition of jurisdictional facilities has been consummated.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.