

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Cinergy Services, Inc.

Docket No. EC02-113-001

On behalf of

PSI Energy, Inc.
CinCap Madison, LLC
CinCap VII, LLC

ORDER DENYING REQUEST FOR REHEARING

(Issued September 17, 2004)

1. This order denies a request for rehearing filed by the Midwest Independent Power Suppliers, Inc. NFP (Midwest Suppliers). This order benefits customers because it reaffirms our prior decision that allowed PSI Energy, Inc. (PSI)¹ to acquire needed generation supply.

BACKGROUND

2. On February 4, 2003, the Commission approved an application filed under section 203 of the Federal Power Act (FPA)² by Cinergy Services, Inc. (Cinergy Services), on behalf of PSI, CinCap Madison, LLC (CinCap Madison), and CinCap VII, LLC (CinCap VII)³ (collectively, Applicants) and authorized the transfer of jurisdictional

¹ PSI, a public utility and a wholly-owned subsidiary of Cinergy Corp. (Cinergy), provides wholesale service at cost-based rates and is authorized to sell wholesale power at market-based rates. PSI also provides retail electric service in the State of Indiana, subject to regulation by the Indiana Utility Regulatory Commission (Indiana Commission).

² 16 U.S.C. 824b (1994).

³ CinCap Madison and CinCap VII (jointly, CinCap) are indirect, wholly-owned subsidiaries of Cinergy. They own and operate generating stations that are interconnected with the transmission system of Cinergy's public utility subsidiaries, and

interconnection facilities associated with the sale of certain generating assets owned by CinCap Madison and CinCap VII to PSI.⁴

3. In reviewing the application, the Commission stated that under the Merger Policy Statement and Order No. 642,⁵ the Commission takes into account three factors in its section 203 analysis: (1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation. February Order at P 10.

4. With respect to the effect on competition, the Commission noted that because the Transfer involved facilities of affiliated parties, Applicants did not submit a horizontal screen analysis, since an intra-corporate transaction by its nature would not result in increased market concentration levels in any relevant market. Therefore, the Commission found that the Transfer would not affect competition under the standards we applied at that time to determine whether a proposed transaction would have an adverse effect on competition. However, the Commission stated that it had general concerns about the possible implications of affiliate transactions of the type proposed here for the competitive process in general and for the region's wholesale competition.⁶ February Order at P 23.

they are authorized to sell power at market-based rates.

⁴ See *Cinergy Services, Inc., et al.*, 102 FERC ¶ 61,128 (2003) (February Order). We note that on February 12, 2003, Applicants advised the Commission that the disposition of jurisdictional facilities was consummated on February 5, 2003.

⁵ See *Inquiry Concerning the Commission's Merger Policy under the Federal Power Act: Policy Statement*, Order No. 592, 61 Fed. Reg. 68,595 (1995), 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); *Revised Filing Requirements Under Part 33 of the Commission's Regulations*, FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,111 (2000) (Order No. 642), *order on reh'g*, Order No. 642-A, 66 Fed. Reg. 16,121 (2001), 94 FERC ¶ 61,289 (2001).

⁶ Specifically, the Commission stated that the ability of a franchised utility to assume its affiliated merchant's generation when market demand declines gave the affiliated merchant a "safety net" that merchant generators not affiliated with a franchised utility lacked. The Commission concluded that the safety net could be a barrier to entry that could harm the competitive process in general and could raise prices to customers in the long run because affiliated merchant generation with a safety net option would not be subject to the price discipline of a competitive market. February Order at P 23.

5. The Commission also noted that the Indiana Commission had approved the proposed transaction, since the transaction would affect matters within the Indiana Commission's jurisdiction.⁷ Recognizing PSI's need to acquire secure supplies, the Commission stated that it would not withhold approval of this transaction on competitive grounds. However, in light of the generic concerns, the Commission added that it would in the future modify its approach to analyzing the possible competitive effects of intra-corporate transactions of this nature. February Order at P 24.

6. With regard to the effect on rates, the Commission noted that the approach of the Merger Policy Statement is to assess the extent of ratepayer protection offered by applicants and to encourage applicants and ratepayers to negotiate adequate ratepayer protection. The Commission noted that although Applicants here did not offer any protection beyond that already available from the wholesale rate freeze through May 2003, wholesale ratepayers did not complain. Therefore, the Commission found that there would be no effect on current wholesale rates, and that the consequences for wholesale ratepayers of adding CinCap plants and associated jurisdictional faculties to rate base would be addressed in the next section 205 wholesale rate case filed by PSI. February Order at P 33.

7. With respect to the effect on regulation, the Commission found that the Transfer would not adversely affect the Commission's regulation. The Commission explained that the fact that the transaction would result in a change in the form of the Commission's regulation of sales from the units and in the magnitude of sales subject to our regulation did not imply that the effectiveness of our regulation would be impaired. The Commission noted that to the extent that the units were used by PSI to make market-based wholesale spot sales, the Commission would continue to be able to review transactions under the market-based authority granted to PSI; and to the extent that units were included in wholesale rate base, sales from the units at cost-based wholesale rates would be subject to the Commission's regulation. February Order at P 36.

⁷ The Commission also noted that the Indiana Commission, with one Commissioner dissenting, had issued certificates of public convenience and necessity for PSI to purchase CinCap's generating assets, and further noted that the proposed purchase price was the result of a settlement agreement between PSI (and CinCap) and the Indiana Commission staff that was also approved by the Indiana Commission. February Order at P 4.

REQUEST FOR REHEARING

8. On March 6, 2003, the Midwest Suppliers filed a request for rehearing of the February Order arguing that Applicants failed to demonstrate that the Transfer satisfies the public interest standard under section 203 of the FPA.

9. First, Midwest Suppliers argue that despite the Commission's concerns about the effect of the proposed transaction on competition, the Commission deferred to the Indiana Commission and thus violated the Commission's duty to review independently applications subject to its exclusive jurisdiction. They also contend that the Commission failed to provide a rational basis for its decision to take action only in a future case. Midwest Suppliers assert that the Commission should have identified the interests that it would balance, or at least explain the circumstances under which it would eventually address these problems.

10. Second, Midwest Suppliers argue that the sale of the generating plants at the proposed price has the same economic effect as a sale to PSI of the power produced from the plants at above-market sales under a life-of-plant power contract. They claim that the proposed transfers violate the Commission's standards for affiliate transactions, which prohibit the sale of non-power goods or services at rates that exceed market value.

11. Third, Midwest Suppliers argue that the the transaction may undermine the Commission's ability to regulate because PSI will not be subject to the Commission's jurisdiction with respect to the generating facilities if PSI is permitted to implement its plan to supply retail load from the two facilities. They maintain that the Commission should acknowledge that the "change in form" of regulation as well as the magnitude of sales subject to its jurisdiction will diminish its ability to regulate in the public interest.

DISCUSSION

12. We disagree with Midwest Suppliers' first argument that we improperly deferred to the Indiana Commission. While we took into consideration the Indiana Commission's views, we made our own decision to authorize the transaction. In fact, in the February Order we found that the Transfer would not affect competition under our standards at the time. Thus, our finding was consistent with our precedent.⁸ Moreover, in response to Midwest Suppliers' argument that the Commission failed to explain why it would modify its approach to affiliate transactions under section 203 only in future cases, we note that

⁸ See *Hatch v. FERC*, 654 F.2d 825, 835 (D.C. Cir. 1981) (normally an agency must adhere to its precedent in deciding cases).

judicial precedent clearly holds that a new policy (as opposed to a binding rule) need not be applied retroactively to the parties in a pending case, as long as the agency gives a reasoned explanation for not applying the policy retroactively.⁹ Because this application had focused our attention for the first time on a possible new threat to competition from affiliate transactions of this type, it was within our discretion to modify our approach to analyzing competitive effects of intra-corporate transactions of this nature in the future. This approach was reasonable and equitable,¹⁰ given the generic nature of our concerns and the fact that the Transfer was consistent with then-existing standards.

13. In addition, the February Order fully addressed Midwest Suppliers' second argument (that the sale of the generating plants at the proposed price violates the Commission's standards of conduct for affiliate transactions). In the February Order, in response to Midwest Suppliers' assertion that this transaction required a heightened standard of review, the Commission applied the approach of the Merger Policy Statement, which is to assess the extent of ratepayer protection offered and to encourage applicants and ratepayers to negotiate adequate ratepayer protection. In this case, Applicants had already agreed to a wholesale rate freeze through May 2003, and wholesale ratepayers had not complained.¹¹ We also noted that the Applicants had not proposed to raise wholesale rates. Thus, we found that there would be no effect on wholesale rates. Furthermore, in the February Order we added that the consequences for wholesale ratepayers of adding the CinCap plants and associated jurisdictional facilities to rate base would be addressed in the next section 205 wholesale rate case filed by PSI. Midwest Suppliers have not provided us with any more information or arguments that would persuade us to change our position on this issue.

⁹ See *Consolidated Edison Company of New York, Inc., et al. v. FERC, et al.*, 315 F.3d 316, 323-324 (D.C. Cir. 2003). Cf. *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074, 1081 (D.C. Cir. 1987); *Retail, Wholesale & Dep't Store Union v. NLRB*, 466 F.2d 380, 390 (D.C. Cir. 1972) (a new binding *rule* is presumed to apply retroactively to parties in an ongoing adjudication, so long as the parties before the agency are given notice and an opportunity to offer evidence bearing on the new standard, and the affected parties have not detrimentally relied on the established legal regime).

¹⁰ *The Power Co. of America, L.P. v. FERC*, 245 F.3d 839 (D.C. Cir. 2001) (focusing on equitable considerations such as degree of burden retroactivity would impose on the party).

¹¹ In this regard, we note that Midwest Suppliers are independent power suppliers and are not wholesale customers of PSI.

14. We also have already addressed Midwest Suppliers' third argument (that PSI will not be subject to the Commission's jurisdiction with respect to the generating facilities if PSI is permitted to implement its plan to supply retail load from the two facilities). In the February Order, in response that argument, we stated that the Transfer would not adversely affect the Commission's regulation. We stated that the fact that the transaction would result in a change in the form of the Commission's regulation of sales from the units and in the magnitude of sales subject to our regulation does not mean that the effectiveness of our regulation would be impaired. The Commission noted that to the extent that the units are used by PSI to make market-based wholesale spot sales, we will continue to review transactions under the market-based authority granted to PSI; and to the extent that units are included in wholesale rates, sales would be subject to the Commission's regulation. Midwest Suppliers have not provided us with any more information or arguments that would persuade us to change our findings on this issue.

The Commission orders:

Midwest Suppliers' request for rehearing is hereby denied, as discussed in the body of this order.

By the Commission. Commissioner Kelliher dissenting in part with a separate statement attached.

(S E A L)

Magalie R. Salas,
Secretary.

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Joseph T. KELLIHER, Commissioner *dissenting in part*:

With one exception, I agree with the Commission's order that rehearing should be denied. I write separately to express my views regarding the inadequacy of the Commission's determination in the February 4, 2003 order (February 4 order) regarding the effect of the proposed transaction on competition.

In my view, the February 4 order did not make a clear finding with respect to the effect of the proposed transaction on competition. Although the February 4 order initially indicated that the transaction would not affect competition under the then-applicable standards, that determination was subsequently undercut by the Commission's concerns that the "safety net" created by this type of affiliate transaction could "be a barrier to entry that harms the competitive process."¹ The effect on competition was further called into question when the Commission declared that it would "not withhold approval of the transaction on competitive grounds" given PSI Energy, Inc.'s need to acquire secure supplies.² There would be no question of withholding approval of the transaction had there been no effect, or a positive one, on competition.

In addition, I believe that the Commission improperly deferred or delegated its authority in some measure to the Indiana Utility Regulatory Commission (Indiana

¹ Cinergy Services, Inc., *et al.*, 102 FERC ¶ 61,128 at P23 (2003).

² *Id.* at P24.

Commission) to the extent it relied on the Indiana Commission's approval of the transaction in order to acquire needed supplies. In my view, the Commission relied upon the Indiana Commission's approval of the transaction and acquisition process and determination of need as reasons for not withholding approval of the transaction on competitive grounds.³ I do not believe the need for electricity supply can overcome an effect on competition under the three-part test applied by the Commission in these cases.

I would have granted rehearing for the Commission to make a determination on the effect on competition independent of the Indiana Commission's determinations.

Joseph T. Kelliher

³ *Id.* at P24.