

103 FERC ¶ 61, 128
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell.

Ameren Energy Generating Company
and Union Electric Company,
d/b/a AmerenUE

Docket No. EC03-53-000

ORDER SETTING DISPOSITION OF FACILITIES APPLICATION
FOR HEARING

(Issued May 5, 2003)

1. On February 5, 2003, Ameren Energy Generating Company (AEG) and Union Electric Company d/b/a AmerenUE (AmerenUE) (collectively, Applicants) filed an application under Section 203 of the Federal Power Act (FPA)¹ requesting Commission authorization to transfer from AEG to AmerenUE the jurisdictional interconnection facilities associated with certain generating assets that are also to be sold to AmerenUE. The Commission is concerned that the proposed transaction may undermine competition and thus may not be consistent with the public interest. We will, therefore, set the application for hearing, as discussed below.

I. Background

A. Applicants

2. AmerenUE, a subsidiary of the Ameren Corporation (Ameren), provides wholesale and retail electric service and retail gas service to customers in Missouri and Illinois.² AmerenUE owns about 8,500 megawatts (MW) of generating capacity and also

¹16 U.S.C. § 824b (2000).

²AmerenUE serves wholesale electric load (at market-based rates) only in Missouri and most of its retail electric load is located in Missouri, where retail service
(continued...)

purchases power to meet its peak load, which exceeded 8,600 MW in 2002. Central Illinois Public Service Company d/b/a AmerenCIPS (AmerenCIPS), also a subsidiary of Ameren, provides retail electric and gas service to customers in Illinois. AmerenUE has market-based rate authority. Both AmerenUE and AmerenCIPS provide transmission service under the Ameren OATT, and Ameren has received conditional authorization from the Commission to join the Midwest Independent Transmission Operator, Inc. (Midwest ISO) through GridAmerica, an independent transmission company.

3. AEG, another subsidiary of Ameren, has market-based rate authority.³ AEG owns generating resources of approximately 4,600 MW and sells wholesale power to its affiliate, Ameren Energy Marketing Company (AEM), and to non-affiliates.⁴ Among AEG's current resources are the Pinckneyville, Illinois generation facility (Pinckneyville), consisting of eight combustion turbine generator units (CTG) with a total capacity of 316 MW and placed in service in 2000 and 2001, and the Kinmundy, Illinois generation facility (Kinmundy), consisting of two CTG units with a total capacity of 232 MW and placed in service in 2001.

B. Transaction and Arguments Presented by Applicants

4. Under separate asset transfer agreements, AEG will sell Pinckneyville and Kinmundy, along with certain transmission facilities that interconnect these generating facilities to the Ameren transmission system, to AmerenUE at a net book value of \$161.5 million and \$96.4 million, respectively. As a result, AmerenUE would own an additional 548 MW of generation capacity.

5. According to Applicants, the purpose of the transaction is to enable AmerenUE to meet its peak load requirements, both short-term and long-term, including planning reserve requirements (15 percent for 2003 and 17 percent for 2006) established in the Mid-America Interconnected Network, Inc. (MAIN) regional reliability council. Based on these requirements, Applicants state that AmerenUE's resource needs are 543 MW in 2003, increasing to 991 MW in 2006.

²(...continued)

has not been deregulated. Retail electric service has been deregulated in Illinois.

³AEG does not own a transmission system and does not provide retail service.

⁴Most of AEG's resources were transferred to it from AmerenCIPS in 1999. AEM's purchases from AEG are principally resold to AmerenCIPS for the purpose of serving AmerenCIPS' retail customers.

6. Applicants argue that AmerenUE's decision to meet its needs by buying these plants is a reasonable one that does not reflect affiliate preference. Applicants state that the choice of Pinckneyville and Kinmundy resulted from AmerenUE's resource planning process and is consistent with a Stipulation and Agreement (Missouri Stipulation) approved by the Missouri Public Service Commission (Missouri Commission). They also assert that the proposed price of the facilities is reasonable, in comparison with other recent sales of similar types of generating capacity used for peaking purposes. According to Applicants, AmerenUE analyzed several options in addition to the proposed purchase, such as purchasing power on the market, purchasing existing assets from non-affiliates, and building new capacity, before reaching a decision, as discussed below.

7. In support, Applicants offer an affidavit, based principally on analyses contained in Attachment II to the affidavit, filed confidentially pursuant to § 388.112 of the Commission's regulations.⁵ Applicants contend that disclosure of the information contained in Attachment II could damage their ability to engage in transactions at reasonable prices.

8. In the fall of 2001, AmerenUE issued a Request for Proposal (RFP) for 500 MW of capacity for the period 2002 through 2011. The bids received were evaluated in conjunction with a 25-year analysis of the cost to build peaking capacity. According to Applicants, an Asset Mix Optimization (AMO) Analysis presented to the Missouri Commission staff in January 2002, indicated that the least cost RFP options, coupled with the construction of combustion turbine generators at the end of the contracting period (2011), was comparable in cost to the purchase of generating facilities from AEG. However, Applicants state that during the period when the RFP bids were being evaluated, the Missouri Commission staff expressed a concern with AmerenUE meeting its needs through power purchases and indicated a preference that AmerenUE own hard assets. Applicants claim that as a result of discussions with the Missouri Commission staff, AmerenUE agreed "to focus on building and/or owning generating assets as the long-term least-cost method of meeting AmerenUE's resource needs."⁶ AmerenUE updated the AMO Analysis in 2002, and the analysis showed that the addition of simple

⁵Applicants state that Attachment II contains highly confidential and sensitive information, including (1) marketing analyses, (2) pricing information, (3) information about the operating characteristics of AEG's facilities and (4) commercially sensitive analysis of the value of certain generating facilities owned by unaffiliated entities.

⁶Appendix A to the Application, Affidavit of Richard A.Voytas at 5-6.

cycle and combined cycle combustion turbines would meet AmerenUE's needs on a least cost planning basis.

9. Applicants state that among the alternatives considered by AmerenUE were the purchase of existing generating assets from non-affiliated entities both inside and outside of the Ameren control area. However, AmerenUE rejected the purchase of generators outside of its control area due to the inability of the generators to obtain firm transmission service to the Ameren border, as documented in its evaluation of the responses to the RFP. Although transmission facility upgrades are planned, the timing of the completion of the upgrades is uncertain, making this option unrealistic, in AmerenUE's view. Similarly, Applicants indicate that AmerenUE rejected the purchase of two non-affiliated generators inside of its control area due to concerns about the creditworthiness of the owners of the assets and about transmission constraints associated with the plants.⁷

10. Apart from the Pinckneyville and Kinmundy plants, AmerenUE also evaluated other AEG plants. Applicants state that municipal property tax issues and implications for holding company requirements eliminated one plant from consideration, transmission constraints eliminated another, and high net book value caused still another to be infeasible. According to Applicants, none of these concerns were present for Pinckneyville and Kinmundy.

11. In addition, AmerenUE evaluated the option of constructing new capacity. According to Applicants, although the cost of new combustion turbines is slightly lower in today's environment of surplus capacity than a few years ago, AmerenUE estimated the site acquisition and development costs for new facilities to be higher than the costs incurred by AEG to develop the Pinckneyville and Kinmundy sites. The higher costs are, in part, due to the fact that the most desirable sites for new generation, where existing gas pipelines intersect with transmission lines, have already been taken. Applicants point out that site and development costs increase as plants are located farther from either a gas pipeline or a transmission system.

12. Further, Applicants claim, the net book value AmerenUE will pay for Pinckneyville and Kinmundy is within the range of prices at which other facilities comparable in terms of operational flexibility and reliability that have recently been sold. A comparison with five other plant sales shows that the price to be paid for Kinmundy is

⁷According to Applicants, these concerns involve commercially sensitive issues, the disclosure of which could harm the owners of the assets.

lower than for all of the other sales except one. The price to be paid for Pinckneyville, although greater than that of four of the plants, is 20 percent less than the highest priced plant recently sold.

13. Finally, Applicants claim that their decision is consistent with the Missouri Stipulation between Ameren UE and the Missouri Commission staff, which was approved by the Missouri Commission on July 25, 2002. The Missouri Stipulation requires AmerenUE to acquire 700 MW of new "regulated" generating capacity by June 30, 2006,⁸ and specifically states that this requirement may be met by the purchase of generation plant from an Ameren affiliate at net book value. The Missouri Stipulation also requires that AmerenUE construct new transmission lines and transmission upgrades that will increase transmission import capability by 1,300 MW.⁹

C. Notice and Responsive Filings

14. Notice of Applicants' filing was published in the Federal Register, 68 Fed. Reg. 7,995 (2003) with motions to intervene and protests due on or before February 26, 2003. Timely motions protesting the application were filed by Midwest Independent Power Suppliers, Inc. (MWIPS), The Electric Power Supply Association (EPSA) and Calpine Corporation (Calpine).¹⁰ Timely motions to intervene without protest were filed by the PSEG Companies,¹¹ the NRG Companies (NRG) and Exelon Corporation. An untimely motion to intervene without protest was filed by National Energy Marketers Association (NEM). On March 13, 2003, Applicants filed an answer (Applicants' Answer) to the protests.

15. On March 18, 2003, the Missouri Commission submitted a letter to the Commission in response to Applicants' request that the Missouri Commission ask the

⁸"Regulated" capacity is not defined, but presumably refers to generating capacity that will be subject to cost-based regulation and will be used to meet Missouri retail load.

⁹In addition, the Missouri Stipulation provides that retail rates will remain frozen, except for certain specified rate decreases, through June 30, 2006.

¹⁰Calpine endorses EPSA's protest without offering separate comments. Calpine requests that it be permitted to supplement its filing to provide more detailed comments, if necessary.

¹¹Although not filing a protest, the PSEG Companies state that they generally support the filings by EPSA and Midwest Suppliers.

Commission to expeditiously approve the application. The Missouri Commission requests that the Commission timely consider the application and states that it does not object to approval of the application, but further states that it is not seeking to comment in any manner on the protests that have been filed in the proceeding. As explained in its letter, the Missouri Commission does not pre-approve acquisitions such as this one. Rather, it reviews the prudence of the acquisition when AmerenUE files to pass through the costs of the acquisition to retail customers.

16. On March 28, 2003, NRG, which had not filed a protest, filed a motion for leave to file an answer to AmerenUE's Answer. On April 14, 2003, Applicants filed a response to NRG's Answer. Finally, on April 25, 2003, Calpine filed a motion to lodge recent relevant information regarding a pending Illinois Commerce Commission proceeding involving the facilities at issue in this proceeding.

II. Discussion

A. Procedural Matters

17. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.214 (2002)), the timely motions to intervene make the movants parties to these proceedings. In addition, the Commission will grant NEM's untimely motion to intervene, as it was filed at an early stage of the proceeding and will not unduly delay the proceeding. Answers to protests are prohibited by Rule 213(a)(2) (18 C.F.R. § 385.213(a)(2)) unless otherwise ordered by the decisional authority. We will accept Applicants' Answer since it assists the Commission in understanding several issues. However, we will not accept NRG's Answer and Applicants' April 14 response to NRG's Answer because they do not add anything to the Commission's understanding of the issues in this case. We will accept Calpine's motion to lodge because it aids in the Commission's understanding of the issues in this case.

B. Analysis

18. Section 203(a) of the FPA provides that:

No public utility shall sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission, or any part thereof of a value in excess of \$50,000, or by any means whatsoever, directly or indirectly, merge or consolidate such facilities or any part thereof with those of any other person, or

purchase, acquire, or take any security of any other public utility, without first having secured an order of the Commission authorizing it to do so.¹²

19. In 1996, the Commission issued the Merger Policy Statement setting forth procedures, criteria and policies applicable to public utility mergers and other dispositions of jurisdictional facilities.¹³ The Merger Policy Statement and Order No. 642,¹⁴ which sets forth the Commission's filing requirements for Section 203 applications, provide that the Commission will take account of three factors in its Section 203 analysis: (a) the effect on competition; (b) the effect on rates; and (c) the effect on regulation. For the reasons discussed below, we will set the proposed transaction for hearing on the effect on competition.

1. Effect on Competition

a. Arguments in Application

20. Applicants state that Order No. 642 does not require a competitive screen analysis for intra-company transfers, as is the case here.¹⁵ They point out that such transfers do not change concentration in generation markets and state that the Commission has recognized that such transfers do not present competitive concerns, citing Order No. 642,¹⁶ GenHoldings I, L.L.C.,¹⁷ and PP&L Resources, Inc.¹⁸ Thus, Applicants claim that the proposed transaction will not adversely affect competition.

¹²16 U.S.C. § 824b(a) (2000).

¹³See 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. ¶ 31,044 at 30,117-18 (1996), order on reconsideration, Order No. 592-A, 62 Fed. Reg. 33,341 (1997), 79 FERC ¶ 61,321 (1997) (Merger Policy Statement).

¹⁴Revised Filing Requirements Under Part 33 of the Commission's Regulations, FERC Stats. & Regs., Regs. Preambles 1996-2000 ¶ 31,111 (2000) (Order No. 642).

¹⁵Order No. 642 at 31,902.

¹⁶Id.

¹⁷96 FERC ¶ 61,140 at 61,602 (2001).

¹⁸90 FERC ¶ 61,203 at 61,649 (2000).

b. Intervenors' Arguments

21. Protestors distinguish the precedent cited by Applicants in support of the transaction, noting that the cited cases involved intra-company transfers that separate generation activity from other lines of business in order to facilitate competition. To the contrary here, Protestors note, the proposed transfer of merchant generation to a franchised utility's regulated rate base to meet retail needs reverses the process and removes demand from the wholesale market that would otherwise be subject to competitive forces. Protestors contend that, at the least, this transfer should be considered a change in status that the Commission must consider in determining whether to permit AmerenUE and AEG to retain market-based rate authority. If the Commission approves the transfer, they urge that it be conditioned on AmerenUE agreeing to not make any off-system sales at market-based rates, including sales to any Ameren affiliate. According to Protestors, this requirement would be consistent with DTE East China, LLC,¹⁹ where the Commission allowed a merchant affiliate of the operating public utility to sell power in the public utility's region at negotiated rates subject to a cost-based rate cap.

22. Protestors express concerns about the possible effects on the competitive process resulting from the type of affiliate transaction proposed here. They note that the success of facilities constructed as merchant plants, such as Pinckneyville and Kinmundy, depends on market conditions and efficiency of plant operations. They argue that AEG and Ameren (and their investors) were able both to avoid obligations placed on traditional utilities in building the plants and to obtain the benefit of opportunities to sell in the market at market-based rates. Thus, AEG and Ameren should have to accept the risk of possible non-recovery of costs in a depressed market, the same risk accepted by non-affiliated generators. Protestors contend that permitting this risk to be transferred will protect the merchant from losses due to power sales at marginal cost in a soft market and thus destroy a level playing field. Also, with a greater likelihood of cost recovery than is the case for non-affiliated suppliers, affiliated generators that are more costly than non-affiliated generators may capture sales that would be otherwise gained by less costly alternatives. In addition, Protestors suggest that a company not affiliated with a traditional utility in whose shadow it is able to build may be deterred from making generation investments if it perceives that affiliated merchant generators will be allowed to move generation in and out of rate base in response to changing market conditions and that the output of such plants can be sold at less than marginal cost.

¹⁹99 FERC ¶ 61,315 (2002).

23. Protestors further regard the type of transaction proposed here to be inconsistent with the concepts underlying RTO initiatives and the Standard Market Design (SMD) NOPR.²⁰ They state that the Commission has emphasized the importance of long-term bilateral contracts in conjunction with short-term spot markets as necessary to achieve competitive market outcomes. According to Protestors, transactions such as this undermine the opportunity to compete for load through bilateral contracts.

24. Protestors, particularly EPSA, assert that the transfer of merchant generation to an affiliated franchised utility should be permitted only upon a showing that the transfer is superior to a "market" alternative. Because the proposed transaction is equivalent to a life-of-unit power purchase and sale contract between affiliates, the Commission should evaluate the transaction in the same manner as it does affiliate purchase contracts. EPSA would have the Commission use the standards first developed in Boston Edison Company Re: Edgar Electric Company (Edgar)²¹ for judging power sales between affiliates. Specifically, EPSA believes that Applicants should be required to either conduct a transparent competitive solicitation or provide benchmark evidence. Only with such evidence can Applicants show that their proposal is more reliable, efficient and economical than other competitive options and that AmerenUE has not unduly favored its affiliate.

25. Based on Edgar, EPSA identifies three forms of evidence for demonstrating lack of affiliate abuse: (1) evidence of direct head-to-head competition between the affiliated seller and unaffiliated suppliers in either a formal solicitation or an informal negotiation process; (2) evidence of the prices that non-affiliated buyers were willing to pay the affiliated sellers for similar services; or (3) benchmark evidence of market value, based on both price and non-price terms and conditions, of contemporaneous sales made by non-affiliated sellers for similar services in the relevant market. EPSA notes that since Edgar, the Commission has approved affiliate contracts based on review of the RFP process used by the purchasing utility (in Aquila Energy Marketing Corp.²² and Southern

²⁰Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design, 67 Fed. Reg. 55,451 (Aug. 29, 2002); IV FERC Stats. & Regs. ¶ 32,563 (July 31, 2002).

²¹55 FERC ¶ 61,382 (1991).

²²87 FERC ¶ 61,217 (1999)

Power Co.²³), thus indicating that affiliate contracts that result from a fair, contemporaneous RFP process are acceptable. In addition, EPSA points out, the Commission has approved a contract based solely on "benchmark" testimony (in Ocean State Power II²⁴, which explained that several factors, such as the relevant market, the contemporaneousness of the benchmark evidence, comparability and non-price terms must be evaluated in the benchmark analysis).

26. EPSA regards Applicants' evidence as inadequate with respect to either the first or third Edgar test.²⁵ First, according to EPSA, Applicants have not relied on a competitive solicitation, as their sole purpose was to avoid direct competition. Second, Applicants have not provided evidence of valid competitive benchmarks. EPSA argues that the two-year-old RFP can hardly be viewed as yielding bids comparable to the proposed transfer, given that market conditions have changed in the interim. Also, the analysis of the RFP results may be faulty, since it may be based on unreliable market price projections after 2011. Further, intervenors note that they are prevented from evaluating the reasonableness of an analysis that has been filed confidentially.

27. Thus, Protestors argue that before the Commission acts on this application, Applicants should be required to either conduct a new, updated and transparent solicitation or submit some other form of market evidence that the requested transfer is equivalent or superior to any "market" alternative. Absent this showing, Protestors urge that the Commission deny the application, or, in the alternative, set the matter for a trial-type evidentiary hearing, similar to that the Commission has required for its review of other types of affiliate transactions.

c. Applicants' Response

28. Applicants acknowledge that the Commission has announced its intention, in light of "generic concerns" raised by affiliate plant sales, to modify its approach to analyzing

²³97 FERC ¶ 61,279 (2001).

²⁴59 FERC ¶ 61,360 at 62,332 (1992), order denying reh'g and granting clarification, 69 FERC ¶ 61,146 (1994).

²⁵EPSA states that to date, no utility has attempted to justify a contract on the basis of evidence required under the second Edgar test.

the competitive effects of such transactions "in the future."²⁶ However, because the Commission has not yet enunciated new standards or criteria, they contend that the Commission should not apply new standards to this transaction; the transaction meets current standards, and the capacity at issue is needed to meet reserve margin requirements for summer 2003. In addition, Applicants note that the sale is consistent with the Missouri Stipulation, which was entered into in summer 2002, long before Cinergy was issued. Applicants state that no evidence has been submitted to show that the sale of the plants is intended to provide AEG a "safety net" or to shield AEG from competition. Rather, AmerenUE is simply seeking to meet its needs on a least cost basis consistent with the Missouri Stipulation while taking into account the Missouri Commission staff's preference that AmerenUE own hard assets. Applicants disagree that AmerenUE is guaranteed recovery of the costs associated with the transaction, since such a claim assumes that state regulators will not act responsibly to protect retail customers.

29. Applicants argue that Protestors, rather than offering relevant evidence or studies, have made only vague or speculative claims that the purchase of the plants is not prudent or reasonable. They suggest that Protestors are more concerned with protecting their interests as competitors, as opposed to protecting competition. Creating an artificial preference for the purchase of power from non-affiliates is no more conducive to the competitive process than is an unjustified preference for an affiliate.

30. In this instance, Applicants argue, power purchases would be inconsistent with the Missouri Stipulation. The purchase of comparable units from non-affiliated entities was not viable for meeting summer 2003 needs, due to uncertainty and potential delay arising out of transmission availability and creditworthiness. Applicants contend that the Voytas affidavit explains why these alternatives are not viable and also shows that the price to be paid for the plants is less than or comparable to the prices paid in arms-length transactions between non-affiliates for similar facilities. While Applicants recognize that the proposed sale would "remove" demand from the wholesale market, they note that any long-term contract has the same consequence. The fact that some other supplier or other plant owner offering less favorable terms was not chosen does not mean that competition did not occur.

31. Applicants disagree that the standards of Edgar should be applied to the proposed transaction. A heightened standard of review for affiliate transactions under Section 205

²⁶See Cinergy Services, Inc., et al., 102 FERC ¶ 62,128 at 61,345 (Cinergy) (2003).

is unnecessary where, as here, all customers are protected by retail rate freezes, retail customer choice or fixed rate contracts. Even when such protections end, Applicants claim, approval of the transaction by the Commission would not prevent the Missouri Commission from reviewing any AmerenUE filing to recover the costs in cost-based rates. Applicants point out that, in contrast, the Missouri Commission would not have similar review authority over costs arising from a Commission-approved contract involving power purchases in the market.

32. Applicants claim that, in any case, they have adequately demonstrated that no affiliate preference has occurred. First, they refer to the prices paid in similar transactions between non-affiliates and conclude that the prices to be paid for Pinckneyville and Kinmundy are comparable. Second, they note that the Voytas affidavit contains a comparative analysis of non-price factors, such as deliverability and creditworthiness. Third, they reiterate the Missouri Commission staff's preference that AmerenUE own hard assets. Fourth, with respect to the timing of the analyses, Applicants note that AmerenUE relied on data on plant sales that closed as late as December of 2002 and an updated AMO Analysis in 2002. Fifth, Applicants state that EPSA has provided no evidence to show that AmerenUE's long-term energy projections are inaccurate.

33. Applicants also contend that Protestors have not provided any legitimate basis to condition AmerenUE's market-based rate authority, noting that the transaction does not alter the amount of company-owned generating capacity and that no evidence of market power abuse has been submitted. Applicants also argue that Protestors' reference to DTE East China is not on point, since the affiliate in that case had not requested market-based rate authority in the first instance.

34. Finally, Applicants dispute that the proposed transaction is inconsistent with SMD. According to Applicants, SMD emphasizes the need for utilities to avoid overuse of spot-market purchases and, instead, rely on a variety of long-term resources, including self-supply as well as bilateral contracts, to achieve resource adequacy. Applicants state that AmerenUE expects to continue to use a mix of resources, including self-owned generation, long-term purchases and spot market purchases and that members of the groups protesting this application will be able to compete for sales to meet AmerenUE's needs. They also challenge the assertion that the proposed transaction is contrary to the Commission's RTO policies, as no competitor alleges that Ameren has denied access to its transmission system.

d. Commission Determination

35. Applicants have not shown that the proposed transaction will not adversely affect competition. We will order a trial-type hearing to be held to examine possible effects of the proposed transaction on competition before we make any determination as to whether the proposed transaction is consistent with the public interest.

36. Heretofore, as we stated in Order No. 642, the Commission's experience has been "that anticompetitive effects are unlikely to arise with regard to internal corporate reorganizations or transactions."²⁷ However, this pronouncement was made in the context of the types of intra-corporate transactions that the Commission had been confronted with at that time. Such transactions had been of two general types. Usually, in a transfer of jurisdictional facilities occurring as a consequence of the creation of a holding company or a reorganization of interests or entities holding the facilities, no change would occur in the way the associated generating facilities were operated or the way output from the generation facilities was marketed or sold, regardless of whether the generation facilities were used for cost-based sales or market-based sales. On other occasions, sometimes as the result of state restructuring initiatives, separate generating subsidiaries had been established. In both types of Section 203 transactions, the Commission found that competitive concerns generally do not arise.

37. In contrast, the filing here marks the second occasion within a very short period that a franchised utility has sought our approval to acquire jurisdictional facilities associated with generating facilities initially developed and marketed as merchant generation by a power marketer affiliate. We indicated in Cinergy our 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."²⁸ We noted that "the ability of a franchised utility to assume its affiliated merchant's generation when market demand declines gives the affiliated merchant a "safety net" that merchant generators not affiliated with a franchised utility lack."²⁹ We expressed concern that "the existence of a safety net may affect the incentive of new merchant generators to invest in new facilities," erecting a barrier to entry that harms the competitive process and raises

²⁷Order No. 642 at 31,902. This statement was made in a discussion of the type of Section 203 applications that could make abbreviated filings.

²⁸102 FERC at 61,345.

²⁹Id.

prices to customers in the long run "because affiliated merchant generation with a safety net option will not be subject to the price discipline of a competitive market."³⁰

38. While the Commission did not withhold approval of the transaction in Cinergy (referring to the Indiana Utility Regulatory Commission's specific review and approval of the generation acquisition and also the need of the franchised utility to acquire secure supplies), we also stated that "in light of the generic concerns raised by this case, the Commission will in the future modify its approach to analyzing competitive effects of intra-corporate transactions of this nature."³¹ The case at hand presents these types of competitive concerns; the transaction proposed by Applicants would change the competitive landscape by means that do not reflect the exercise of competitive forces in the market, i.e., the interaction of independent sellers with an independent buyer. Unlike Cinergy, the only state regulatory commission with pre-approval authority here, the Illinois Commerce Commission (Illinois Commission), has not acted and its staff has recommended that the transaction not be approved. As this Commission has previously noted:

if the Commission is to fulfill its statutory responsibilities, it must determine what is consistent with the public interest in light of conditions in the electric industry in general as well as the specific circumstances presented by a proposed merger. In an era of traditional, cost-of-service based regulation, the Commission defined its public interest responsibilities consistent with that structure. Today, we believe that the public interest requires policies that do not impede the development of vibrant, competitive generation markets.³²

39. Under Edgar, the reasonableness of a franchised utility's wholesale purchases from an affiliate is evaluated to ensure that affiliate abuse has not occurred. However, we have no similar established standards to evaluate Section 203 transactions between affiliates that effectively accomplish the same end. In the Commission's view, however, the two situations are similar. Just as our Section 205 review of affiliate transactions under Edgar is intended to prevent affiliate abuse and to ensure prices that would be consistent with competitive outcomes, a franchised utility should be required to

³⁰Id.

³¹Id.

³²Merger Policy Statement at 30,115.

demonstrate that its purchase of an affiliate's plant is on terms similar to any other competitive alternatives available.

40. In defending AmerenUE's decision to acquire two affiliate plants, Applicants rely on the results of the RFP issued in August 2001,³³ an updated assessment of the viability of non-affiliated generators located both outside and inside the Ameren control area and an updated AMO Analysis completed in mid-2002. Applicants also provide a comparability analysis of recent non-affiliated plant sales.

41. We have concerns regarding the adequacy of the evidence offered by Applicants. Initially, we note that AmerenUE did not issue an RFP. The application gives some indication that generating facilities were offered for sale in response to the RFP issued in August 2001. Market conditions may have pushed down the price of generating assets since then.

42. Applicants' evaluation process rejected a number of alternatives due to the claimed lack of necessary transmission availability, alleged specific transmission constraints associated with particular plants, and creditworthiness concerns about the owners of certain plants. A fair and reasonable evaluation of the transmission system is vital to ensuring that all generation resources are given a fair opportunity to compete. As discussed below, a hearing on the application is necessary to determine whether Applicants' evaluation of transmission service factors adequately considered competing

³³We note that the Missouri Commission has required AmerenUE to conduct a competitive bidding process before entering into a power purchase contract with AEG or a marketing affiliate of AEG. Motion to Intervene and Comments in Support of Union Electric Company at 5, Docket No. ER02-1451-000, April 11, 2002. Because the potential bidders to supply AmerenUE's needs for power for the period 2002-2011 included its affiliates, AmerenUE issued the 2001 RFP. AmerenUE also employed an independent consultant to help evaluate the responses. The Missouri Commission staff then recommended that the RFP proposal be modified to reflect a one-year term. AmerenUE obtained revised bids and ultimately chose a combination of three, including an AEM bid, to supply its 2002 needs. After the AEM contract was filed with this Commission and set for hearing, the case was settled. Among other terms, the settlement provides that whenever an RFP is issued for capacity and energy in the future and purchases from an affiliate are a possible result, AmerenUE will use an independent consultant and ensure that the consultant has all of the information necessary for it to make a fair and independent analysis of the bids. Article III, Offer of Settlement filed in Docket No. ER02-1451-001, December 6, 2002.

alternatives. In the hearing, the parties are not limited to presenting evidence regarding the concerns raised here, but also may present other evidence bearing on whether Applicants' analysis fairly addressed competing alternatives, such as whether Applicants properly took account of changing market conditions or creditworthiness concerns in investigating alternatives.

43. The Commission is unable to determine from the analysis submitted with the application whether the costs of solutions to the lack of transmission availability, such as incremental transmission investments or redispatch opportunities to relieve constraints, were properly considered and evaluated. We also note that Applicants refer to the transmission evaluation conducted for the 2001 RFP and to uncertainty associated with the timing of planned facility upgrades within the control area. However, it is unclear from the application whether Applicants updated the 2001 assessment of transmission availability before concluding that transmission service necessary to deliver power from plants outside of the Ameren control area was inadequate.

44. In addition, we note as a condition of the Commission's approval of Ameren's acquisition of Central Illinois Light Company, Ameren agreed to make certain transmission upgrades, some of which were to be completed within six months of consummation of the acquisition.³⁴ It is also anticipated that Ameren will join the MISO. While these potentially beneficial actions would not add transmission capability to facilitate power deliveries to meet summer 2003 needs, they would improve transmission availability in later periods and could expand the range of power supply options. It is unclear whether the option of purchasing power by contract for 2003 in conjunction with buying power plants in 2004 or later years was considered or fairly evaluated.

45. Further, the Commission must note that the use of an independent consultant to analyze the alternatives considered in the application would have provided greater assurance that an affiliate did not receive undue preference in the evaluation process and that the necessary transmission upgrades and potential redispatch were properly considered in the evaluation of each alternative.

46. Based on all of above considerations, the Commission finds it necessary to set this matter for hearing. We need to be certain that the purchase of the Pinckneyville and Kinmundy plants at net book value is consistent with results that would be obtained through a competitive process reflecting the interplay between AmerenUE and independent sellers and has not resulted in undue preference being shown to

³⁴See Ameren Services Co., et al., 101 FERC ¶ 61,202 (2002).

AmerenUE's affiliate, AEG. We are mindful that a hearing process may force AmerenUE to seek other means of satisfying summer 2003 peak requirements.³⁵ Nonetheless, we believe it vital to fully address before the fact the potential effects of changes in the competitive landscape that could be caused by the transaction, changes that would be long-lasting.

47. We emphasize that our determination to set the merits of the proposed transaction for hearing is not inconsistent with any ruling by the Missouri Commission or any position that may have been taken by the staff of the Missouri Commission regarding the acquisition of generating assets versus power purchase contracts as a solution to either AmerenUE's short-term or long-term needs. The Missouri Commission staff's apparent preference that AmerenUE own hard generation assets, instead of relying on power purchase contracts, was expressed in the context of AmerenUE's evaluation of RFP bids to meet power needs over the period 2002-2011, that is, as a means of meeting long-term power needs. Just as AmerenUE acted to meet its needs for Summer 2003 with power purchase contracts, there is no indication that the Missouri Commission staff sought to preclude AmerenUE from considering short-term power purchases for 2003.³⁶ The Missouri Stipulation itself does not preclude power purchases in the near term, given that AmerenUE has until 2006 to satisfy its commitment to add 700 MW of regulated generation capacity.

48. Finally, the Illinois Commission, which does have review authority over the proposed asset transfers,³⁷ has initiated a proceeding to address AmerenUE's proposed acquisitions. In that proceeding, the staff of the Illinois Commission has filed testimony

³⁵Applicants bear some responsibility for these circumstances. The need for additional power supplies for 2003 was long evident and the Missouri Stipulation, which noted the option of buying an affiliate plant at net book value, was approved in July, 2002. In addition, the updated AMO analysis, which considered the possibility of buying the Pinckneyville plant, was presented to the Missouri Commission staff in August 2002. None of the information disclosed in the application suggests any reason why this application could not have been filed earlier than February 5, 2003.

³⁶It was also apparent early in 2002, long before AmerenUE submitted its application in this proceeding, that the problem of obtaining sufficient power supplies would be present in 2003 as well as beyond.

³⁷The Illinois Commission also has prudence review authority if and when AmerenUE seeks to recover the costs of the acquisition in its Illinois retail rates, which are currently frozen.

urging the Illinois Commission to disallow the proposed asset transfer. In its testimony, the Illinois Commission staff concludes, among other things, that AmerenUE has not shown that the proposed asset transfer is the least-cost means to meet its customers' needs.

2. Effect on Rates

a. Applicants' Position

49. Applicants state that the proposed transaction will not adversely affect rates. They note that all of AmerenUE's wholesale customers are served under contracts that have fixed rates or other pricing provisions that will not be affected by any costs associated with this transfer. The wholesale customers will be able to purchase power from other suppliers when their contracts expire. Applicants contend that the Commission has found that wholesale customers are adequately protected in such circumstances, citing Cinergy Services, Inc.³⁸ and Potomac Electric Power Co.³⁹ At the retail level in Missouri, Applicants note that retail rates are frozen through 2006, a protection previously found by the Commission to be sufficient, citing First Energy Corp.⁴⁰

50. Applicants state that none of AmerenCIPS' customers will be affected, noting that AmerenCIPS has no wholesale customers. They also point out that the AEG capacity being sold is not needed to support power sales by AmerenCIPS to its bundled retail load, which also occur at rates frozen at current levels through 2006.

b. Protests

51. Protestors note that the assets to be transferred would become part of regulated utility facilities, with their costs presumably to be rolled into AmerenUE's regulated rate base. While retail rate settlements and rate freezes may protect retail consumers in the near-term from cost- and risk-shifting, Protestors claim that the costs and risks associated with the facilities will remain for decades.

c. Applicants' Response

³⁸98 FERC ¶ 61,306 at 62,307 (2002).

³⁹96 FERC ¶ 61,323 (2001).

⁴⁰94 FERC ¶ 61,179 at 61,620 (2001).

52. Applicants dispute Protestors' assertion that the transfer would improperly shift risks from the AEG merchant operations to AmerenUE. They point out that no customer, customer group, or state regulatory commission has opposed the transfer. Applicants also reiterate that AmerenUE's wholesale customers take service under contracts with fixed rate provisions, with most of the contracts extending several years into the future, and that the customers will be able to buy power from other suppliers when the contracts expire. They also point out that if AmerenUE seeks in the future to sell wholesale power at cost-based rates, the Commission will be able to review and judge the reasonableness of any cost-based rate levels. At the retail level, while Applicants acknowledge that Missouri retail customers may not have a choice of supplier when the rate freeze expires in 2006, they stress that AmerenUE will still need to obtain the Missouri Commission's approval before any of the costs associated with the transfer may be recovered from retail ratepayers.

d. Commission Determination

53. The Commission finds that the proposed transfer will not adversely affect rates. All of the municipal wholesale customers are served at fixed rates under AmerenUE's market-based tariff, with most contracts extending to the end of 2008. Although three of the wholesale contracts terminate at the end of 2003, those customers will be able to seek other sources of supply. The ability of wholesale customers to seek other sources of supply is dependent on the competitiveness of the market. We are setting for hearing the effects of this disposition on competition. Moreover, no issue has been raised by any customer as to the need for ratepayer protection.⁴¹

54. In addition, the Commission notes that the Missouri Commission has approved the Missouri Stipulation, which provides that AmerenUE will institute three periodic retail rate decreases through 2006. The Missouri Stipulation also specifically permits any of the signatories to raise issues concerning the prudence and reasonableness of the infrastructure investment decisions made by AmerenUE regarding generation and transmission projects contemplated by the Missouri Stipulation. Thus, retail customers are protected.

3. Effect on Regulation

a. Applicants' Arguments

⁴¹Merger Policy Statement at 30,123-24. In fact, no wholesale customer has sought to intervene in the proceeding.

55. Applicants assert the proposed transfer will not undermine the Commission's regulation. They state that while Ameren is a registered public utility holding company under the Public Utility Holding Company Act of 1935, Ameren has previously committed to abide by the Commission's policies with respect to intra-company and affiliate transactions and will continue to do so.⁴² Also, the Commission will continue to have authority over any wholesale power sales from the generating facilities being sold, as well as all wholesale power sales by AmerenUE and AEG.

56. At the state level, Applicants point out that the Illinois Commerce Commission (Illinois Commission) must approve the transaction and that the Missouri Commission, while lacking similar approval authority over the transaction, has the authority to require AmerenUE to comply with its resource planning regulations and has done so here. Applicants further note that both state commissions will continue to have jurisdiction over all retail sales of power and all bundled transactions currently subject to their jurisdiction.

b. Protests

57. MWIPS claims that the Commission will not have jurisdiction to prohibit and regulate affiliate transactions once the facilities become part of AmerenUE's regulated rate base. It points out that after the plant transfers the Commission will not have jurisdiction over sales to the extent that the output of the plants is sold at retail and not at wholesale. MWIPS asserts that as a result, the Commission would lose its ability to prevent affiliate abuse associated with cross-subsidization by captive AmerenUE customers. MWIPS believes that the Commission should not give up its ability to regulate such affiliate transactions without first assuring itself that the transfer of the plants is not a new form of abusive affiliate practice.

c. Applicants' Response

58. Applicants disagree with MWIPS' assertions. They point out that to the extent that AmerenUE continues to sell power from the plants at wholesale, the Commission will maintain review authority over cost-based transactions and oversight of market-based sales. They also note that in Cinergy, the Commission found that a reduction in the amount of sales subject to its jurisdiction does not imply that its regulation will be impaired.

d. Commission Determination

⁴²Application at 18.

59. The Commission finds that its regulation will not be adversely affected by the proposed transaction. As we stated in Cinergy, if the generating units that are the subject of the proposed transfer are used to make wholesale sales, whether market-based or cost-based, the Commission will continue to review transactions under its Section 205 authority. Even if the output from the plants will be used principally for retail needs, thus potentially reducing the amount of possible wholesale sales from the plant, a reduction in the amount of sales subject to our regulation does not mean that the effectiveness of our regulation will be impaired. In addition, Applicants have reiterated their commitment to abide by the Commission's policies with respect to intra-company and affiliate transactions.⁴³

60. The Commission is mainly concerned with the effect of a Section 203 transaction on state regulation where the affected state regulatory commission lacks approval authority over the transaction. Here, Applicants are required to seek the approval of the Illinois Commission, which is currently conducting a proceeding on the transaction. Approval by the Missouri Commission is not specifically required. However, as stated previously, under the Missouri Stipulation approved by the Missouri Commission, AmerenUE may satisfy its commitment to add 700 MW of regulated capacity by purchase of generation plant from an affiliate at net book value and issues relating to prudence and reasonableness of such an infrastructure investment decision may be brought before the Missouri Commission. We note further that the Missouri Commission has not intervened in this proceeding. Therefore, the Commission finds that the proposed transfer will not adversely affect state regulation.

4. Accounting

61. The asset transfer agreements provide for AmerenUE to acquire AEG's Pinckneyville and Kinmundy generation and associated transmission facilities at the net book value of \$161.5 million and \$94.6 million, respectively. Section 33.5, Proposed Accounting Entries, of the Commission's Regulations requires that Applicants present proposed accounting entries with sufficient detail showing the effect of the transaction.⁴⁴ Applicants have not included the proposed accounting entries and related details in the application and request waiver of Section 33.5 of the Commission's regulations. They state that they will provide this information at a later date if and as required by the Commission.

⁴³Merger Policy Statement at 30,125.

⁴⁴18 CFR § 33.5 (2002).

62. In the Merger Policy Statement,⁴⁵ we indicated that it is important for entities to properly account for transactions under Section 203. The information required in Section 33.5 enables the Commission to evaluate an applicant's accounting for Section 203 transactions and to provide guidance and direction when the accounting is inconsistent with the Commission's Uniform System of Accounts. The recent and widely reported allegations of accounting irregularities by the business community at large and their negative effect on capital markets reinforce our views regarding the importance of proper accounting. Therefore, we will deny Applicants' request for waiver of Section 33.5 of our regulations and will require that Applicants satisfactorily demonstrate that their proposed accounting for the transaction complies with the Commission's Uniform System of Accounts. In addition, Applicants are advised that they must comply with Section 33.5 for any future transaction requiring Commission authorization under Section 203 of the FPA.

The Commission orders:

(A) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by Section 402(a) of the Department of Energy Organization Act and the Federal Power Act, particularly Section 203 thereof, and pursuant to the Commission's Rules of Practice and Procedure and regulations under the Federal Power Act (18 C.F.R. Chapter I), a public hearing shall be held to address the effect of Applicants' proposed disposition of facilities on competition.

(B) Applicants' request for a waiver of the requirement of Section 33.5 of the Commission's regulations is denied. Applicants shall submit their proposed journal entries and related details required by Section 33.5 within 30 days of the date of this Order. The submission must include appropriate narrative explanations of the proposed accounting entries, how the net book value of the assets was calculated and the related income tax consequences.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

⁴⁵Merger Policy Statement at 30,126.