



FERC Issues NOPR to Address Control and Affiliation Concerns

On January 21, 2010, the Federal Energy Regulatory Commission issued a Notice of Proposed Rulemaking to address what constitutes “control” or an “affiliate” when investors seek to acquire an interest in a public utility.

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On January 21, 2010, the Federal Energy Regulatory Commission (“the Commission”) issued a Notice of Proposed Rulemaking^[1] (“NOPR”) to address what constitutes “control” or an “affiliate” when investors seek to acquire an interest in a public utility. The NOPR responds to uncertainty over whether certain investments in public utilities may create affiliation with a public utility or create perceived market power. Industry concerns had been expressed that such uncertainty may discourage needed investment in energy infrastructure and cause compliance problems for competitive power suppliers in market-based rate contexts. The NOPR proposes amendments to the Commission’s regulations regarding the amount of stock ownership that results in “control” of a company and amends the definition of corporate “affiliate.” The NOPR presents proposed amendments to the Commission’s regulations pursuant to sections 203 and 205 of the Federal Power Act (“FPA”).^[2]

BACKGROUND

The Commission has implemented rules under Section 203 of the FPA to prevent market participants from accumulating horizontal or vertical market power. Section 203 requires Commission authorization for mergers, dispositions, and acquisitions involving electric generation and transmission companies and their holding companies. The market power rules under Section 203 work in concert with the market-based rate program rules the Commission has implemented under Section 205 of the FPA to prevent the exercise of market power in wholesale energy and capacity markets.

Currently, the Commission grants blanket authorizations under Section 203 for transactions falling within certain parameters which the Commission has determined to be within the public interest and outside the realm of “inappropriate cross-subsidization.”^[3] However, a market-based rate seller acquiring or disposing of public utility securities under a Section 203 blanket authorization is still subject to the Commission’s market-based rate program rules under Section 205. Specifically, under the Section 205 market-based rate program rules, a market-based rate seller must be able to demonstrate to the Commission that it – and its affiliates – do not have market power in the relevant geographic market.^[4] In this context, for purposes of the Commission’s market power analysis under Section 205, it is important to understand whether an investor’s energy assets should be attributed to a public utility whose securities are acquired by that investor under a Section 203 blanket authorization. The Commission’s proposed amendments to its regulations under Section 203 and 205 are a response to confusion regarding issues of control and affiliation in transactions in which investors acquire public utility securities.

EPSA’S PETITION FOR GUIDANCE AND OTHER INDUSTRY COMMENTS

The Commission's actions were initially motivated by a petition for guidance filed by the Electric Power Supply Association ("EPSA") on September 2, 2008. EPSA asked for guidance regarding "when investments in publicly-held companies will be deemed to convey 'control' or result in 'affiliation' for purposes" of the Commission's rules and regulations under Sections 203 and 205 of the FPA. In its petition, EPSA asserted that uncertainty existed over whether certain investments would result in affiliation with a public utility and create perceived market power. EPSA indicated that this uncertainty threatened to discourage investment in energy infrastructure and also created potential compliance problems for competitive power supply companies with market-based rates.

EPSA requested that the Commission provide a blanket ruling that certain investor acquisitions of public utility securities would not result in affiliation with the public utility for purposes of the Commission's market power analysis under Section 205 and would not be deemed a disposition of the public utility's jurisdictional facilities under Section 203. EPSA asked the Commission for three basic findings. First, EPSA asked the Commission to determine that in situations in which an investor holds less than 20 percent of a public utility's securities and files a Schedule 13G statement of beneficial ownership with the Securities and Exchange Commission ("SEC"),^[5] no control over, or affiliation with, the public utility exists for Section 203 or Section 205 purposes. Second, EPSA asked the Commission to state that in the situations described above: 1) the public utility does not have to make a change in status filing with the Commission in instances where it has market-based rate authorization; 2) the public utility does not need to include generation and inputs owned or controlled by other entities in which the investor holds an interest in any subsequent market power analyses conducted pursuant to Section 203 applications or market-based rate authorizations under Section 205; and 3) affiliate sales restrictions will not apply to transactions between publicly-held companies with market-based rate authorization (and their subsidiaries) and other entities in which the investor holds interests and/or voting securities. Building on these three main requests, EPSA also proposed additional safeguards against the exercise of market power and recommended that the Commission rely on SEC sanctions associated with Schedule 13G filings.

The Commission staff held a workshop on December 3, 2008, to address the issues raised in EPSA's petition. A number of other parties weighed in on the control and affiliation issues by submitting comments and participating in the workshop. Some commenters generally agreed with the propositions in EPSA's petition.^[6] Others argued that a control relationship should not be supposed simply from the absence of a Schedule 13G filing with the SEC, and discussed the different scope of the term "control" as defined by the Commission and the SEC.^[7] Other commenters opposed reliance on a Schedule 13G filing and recommended that the Commission develop its own form to evaluate whether an investor gains control over a public utility through its investment.^[8] Finally, some parties expressed concerns about diminished competition resulting from an investor acquiring a partial interest in competing generating assets, and asserted that the Commission should consider issues of

“cross-ownership,” similar to the attention given to these issues by Department of Justice and the Federal Trade Commission.[9]

After review of EPSA’s petition and the comments of the various other parties, the Commission determined that although EPSA’s petition only sought guidance on the issues, the issues involved called for more formal treatment. The Commission issued the NOPR to fully address those issues.

THE NOTICE OF PROPOSED RULEMAKING

To address the concerns about control, the Commission proposes a new blanket authorization under section 203(a)(2) of Part 33 of its regulations to allow a holding company to acquire voting securities from a public utility or a holding company. The proposed blanket authorization allows a holding company to acquire 10 percent, but less than 20 percent, of a utility’s or another holding company’s voting securities if the investor files an Affirmation with the Commission on newly-developed Form 519-C within 10 days following the acquisition. The Commission found that SEC Schedule 13G did not provide enough information for it to monitor markets and protect the public interest, so it developed its own form designed for those specific purposes. The Affirmation, which creates a rebuttable presumption that the investor does not control the public utility, requires detailed information from the acquiring holding company and must be certified by a corporate officer of the company. An investor that is also a public utility holding company, seeking to acquire 20 percent or more of a public utility’s voting securities, must file a stand-alone application under Section 203(a)(2) – unless that investor qualifies for one of the other blanket authorizations contemplated in the Commission’s regulations.

The Commission also proposes to amend the definition of “affiliate” of a specified company in section 35.36(a)(9) of its market-based rate program regulations to mean “any person that controls, is controlled by or is under common control with, such specified company.” The current regulation creates a rebuttable presumption that a person owning less than 10 percent of the outstanding voting securities of a public utility lacks control of that utility. The amended regulation would provide that if an investor owns 10 percent, but less than 20 percent of the outstanding voting securities of a public utility, certain Commission regulations would not apply to the investor or public utility. Market-based rate filing requirements would not be triggered, and the public utility would be exempt from certain restrictions applicable to affiliates if the acquiring person has filed an Affirmation and continues to comply with all of the other conditions and reporting obligations. The Commission proposes to use the Affirmation as a monitoring tool and to sanction entities that violate the conditions and reporting obligations set forth in the Affirmation.

COMMENT PROCEDURE

Comments should be filed electronically with the Commission by March 29, 2010 (60 days after the NOPR was published in the Federal Register on January 28, 2010).[10] This proceeding is docketed at the Commission as Docket No. RM09-16-000.

[1] *Control and Affiliation for Purposes of Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act*, 130 FERC ¶ 61,046 (2010), 75 Fed. Reg. 4498 (January 28, 2010) (the "NOPR").

[2] 16 U.S.C. §§ 824b and 824d (2006).

[3] NOPR at P 3.

[4] *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, 119 FERC ¶ 61,295 (2007) at PP 320-338.

[5] NOPR at P 4.

[6] Calpine Corporation and Tenaska Energy, Inc., Mirant Corporation, and the Edison Electric Institute supported EPSA's proposals. NOPR at P15.

[7] *Id.* at P15.

[8] *Id.* at P16.

[9] *Id.* at P 17.

[10]75 Fed. Reg. 4498 (January 28, 2010).

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