

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Elizabeth Anne Moler, Chair;
Vicky A. Bailey, James J. Hoecker,
William L. Massey, and Donald F. Santa, Jr.

H.Q. Energy Services (U.S.) Inc.) Docket No. ER97-851-000

ORDER DIRECTING FURTHER INFORMATION AND ANALYSIS AND
DEFERRING ACTION ON MARKET-BASED RATES

(Issued May 9, 1997)

In this proceeding H.Q. Energy Services (U.S.) Inc. (H.Q. Energy), a wholly-owned subsidiary of Hydro-Quebec, applied to the Commission for market-based rate authority. As discussed below, the Commission does not have sufficient information to complete its analysis of H.Q. Energy's request. We find that H.Q. Energy has satisfied all but one of the Commission's requirements for market-based rates. However, we are unable to conclude at this time that H.Q. Energy has demonstrated that Hydro-Quebec, its Canadian utility affiliate, lacks generation market power. Accordingly, we will defer action on H.Q. Energy's request for market-based rates and direct H.Q. Energy to provide further information and analysis concerning generation market power consistent with the Commission's guidance in New York State Electric & Gas Corporation, 78 FERC ¶ 61,309 (1997) (NYSEG), which was issued after H.Q. Energy completed its application.

Background

On December 18, 1996, as amended on December 19, H.Q. Energy filed an application (December Application) to sell power at market-based rates. On March 11, 1997, H.Q. Energy filed a supplemental petition (March Supplement), which substantially amends its December Application in response to the Commission's decision in British Columbia Power Exchange Corporation, 78 FERC ¶ 61,024 (1997) (Powerex).

According to its application, H.Q. Energy is a wholly-owned subsidiary, incorporated in the State of Delaware, of Hydro-Quebec, the utility for the Canadian province of Quebec. After Commission approval of its application for market-based rates, H.Q. Energy intends to engage in various wholesale power marketing activities in the United States. H.Q. Energy does not own any electric generation or transmission facilities, and none of its affiliates owns any generation or transmission facilities that are located in the United States. H.Q. Energy's application includes a proposed code of conduct that H.Q. Energy suggests is

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consistent with the standards established by the Commission in the OASIS Rule. 1/

H.Q. Energy's March Supplement includes revised transmission tariffs for Hydro-Quebec and its affiliate Cedar Rapids Transmission Company Ltd. (Cedar Rapids). 2/ H.Q. Energy also discusses changes in the Quebec regulatory regime. In legislation entitled "An Act respecting the Regie de l'energie" (Regie Act), the Province of Quebec created a new regulatory body, the Regie, with functions, powers and procedures similar to those of this Commission.

Other salient aspects of H.Q. Energy's application, including the transmission tariffs proposed for its transmission-owning utility affiliate, its generation market power study and its proposed code of conduct, are described in further detail below.

Notices of H.Q. Energy's filings were published in the Federal Register, 3/ with comments, protests and motions to intervene due on or before March 27, 1997.

In response to H.Q. Energy's December Application, Enron Power Marketing, Inc. (Enron) filed a timely motion to intervene and protest on January 3, 1997, raising no substantive issues. On January 15, 1997, the following entities timely filed the following pleadings: Niagara Mohawk Power Company (Niagara

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- 1/ Open Access Same-Time Information System (formerly Real-Time Information Networks) and Standards of Conduct, Order No. 889, 61 Fed. Reg. 21,737 (1996), FERC Stats. & Regs. ¶ 31,035 (1996), order on reh'g, Order No. 889-A, 62 Fed. Reg. 12,484 (1997), FERC Stats. & Regs. ¶ 31,049 (1997), reh'g pending (OASIS Rule).
 - 2/ H.Q. Energy explains that Cedar Rapids owns and operates transmission facilities in Quebec and in the Province of Ontario. For convenience of reference, we generally will refer to Cedar Rapids and Hydro-Quebec collectively as Hydro-Quebec when discussing the transmission tariffs and transmission market power issues.
 - 3/ 62 Fed. Reg. 1112, 62 Fed. Reg. 13,605 (1997). Comments, protests and motions to intervene in response to H.Q. Energy's December Application were due January 15, 1997. As noted below, several intervenors filed pleadings after that date but before March 27, 1997, the deadline for responses to the March Supplement. As a result, all such pleadings are timely filed.

Mohawk), motion to intervene and protest; Plum Street Energy Marketing, Inc. (Plum Street), motion to intervene; New York State Electric & Gas Corporation (NYSEG), motion to intervene; Newfoundland and Labrador Hydro (Newfoundland Hydro), motion to intervene; Electric Clearinghouse, Inc., motion to intervene and protest; and Enron, protest. Those interventions of Plum Street, NYSEG and Newfoundland Hydro raise no substantive issues.

Also in response to the December Application, the following entities filed the following pleadings on the specified dates: 4/ the Grand Council of Crees and the New England Coalition for Energy Efficiency and the Environment (collectively, the Crees), motion for extension of time to file comments and intervention, filed January 21, 1997; Vermont Public Power Supply Authority (Vermont Public Power), motion to intervene, filed January 22, 1997; TransCanada Energy Limited, motion to intervene, filed January 24, 1997; Indeck Capital, Inc. and Indeck Energy Services, Inc. (collectively, Indeck), motion to intervene, filed January 30, 1997; Central Vermont Public Service Corporation (Central Vermont), motion to intervene, filed January 31, 1997; and The Utility-Trade Corp. (Utility-Trade), motion to intervene, 5/ filed February 4, 1997. Those interventions of Indeck, Central Vermont and Utility-Trade raise no substantive issues. 6/

Some of the issues raised by intervenors in their responses to the December Application were rendered moot by modifications included in the March Supplement. We will not address such issues or further describe intervenors' arguments in connection therewith.

4/ See supra note 2 regarding the timeliness of these pleadings.

5/ Utility-Trade styled its pleading a notice of intervention. Under the Commission's Rules of Practice and Procedure, however, only the Secretary of Energy and state commissions are permitted to file notices of intervention to achieve intervenor status. See 18 C.F.R. § 385.214(a) (1996). Accordingly, we will regard Utility-Trade's pleading as a motion to intervene.

6/ In a letter filed January 17, 1997, H.Q. Energy requested that the Commission defer action on the December Application, pending the anticipated legislative action in the Province of Quebec and possible amendment of the application. In addition to the above-listed pleadings, the Crees filed, on February 24, 1997, a motion to delay filing additional pleadings until H.Q. Energy amended the December Application. The new comment period established after the March Supplement renders the Crees' motion moot.

In response to H.Q. Energy's March Supplement, the following entities timely filed the following pleadings on the specified dates: the Crees, motion to file additional pleadings and comments, filed March 21, 1997; Mouvement Au Courant, motion to intervene, filed March 26, 1997; Niagara Mohawk, supplemental protest, filed March 27, 1997; Newfoundland Hydro, extension of time to file protest, 7/ filed March 27, 1997; Burlington Electric Department, motion to intervene, filed March 27, 1997; and Indeck, motion to intervene, raising no substantive issues, filed March 27, 1997.

Also in response to the March Supplement, the following entities filed the following pleadings on the specified dates: the Crees, comments and intervention, filed March 28, 1997, as corrected April 1, 1997; CNG Energy Services Corporation (CNG Energy), motion to intervene out of time, raising no substantive issues, filed April 9, 1997; Newfoundland Hydro, comments, filed April 10, 1997; Consolidated Edison Company of New York (ConEd), motion to intervene out of time in support of H.Q. Energy's application, raising no substantive issues, filed April 17, 1997; and Mouvement Au Courant, supplement to motion to intervene, filed April 30, 1997.

On April 11, 1997, H.Q. Energy filed a response to various motions to intervene and protests. In addition to addressing substantive issues raised by intervenors, H.Q. Energy opposes the motions to intervene of the Crees and of Mouvement Au Courant, on the alleged grounds that their interests relate exclusively to matters of Quebec policy and law. On April 28, 1997, H.Q. Energy filed a response to Newfoundland Hydro's comments.

To the extent that intervenors or H.Q. Energy's responses raises issues that require resolution in this order, their arguments are described below.

Discussion

A. Procedural Matters

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 8/ the timely, unopposed motions to intervene serve to make the movants parties to this proceeding. Additionally, given the early stage of this proceeding and the absence of undue prejudice or delay, we will grant the unopposed motions for late intervention of CNG Energy and ConEd. We also

7/ We will treat Newfoundland Hydro's pleading as a motion to file out of time.

8/ 18 C.F.R. § 385.214 (1996).

will accept the late-filed comments of Newfoundland Hydro, the filing of which H.Q. Energy does not oppose. Moreover, notwithstanding the opposition of H.Q. Energy, we will grant intervenor status to the Crees and to Mouvement Au Courant and will accept their respective late-filed pleadings, as we find that their interests may not be adequately represented by other parties to this proceeding. We will also accept H.Q. Energy's responses. Given the unusual nature and complexity of the case, involving Canadian affiliates, and the evolving regulatory regime in Quebec, these pleadings have aided us in understanding the issues.

B. Market-Based Rates

We generally have allowed power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. In order to demonstrate the absence or mitigation of market power, a transmission-owning public utility must have on file with the Commission an open-access transmission tariff for the provision of comparable services. The Commission also considers whether there is evidence of affiliate abuse or reciprocal dealing. ^{2/}

As we discuss below, we find that H.Q. Energy meets all but one of the criteria for granting market-based rates. Because, however, H.Q. Energy in preparing its generation market power analysis did not have the benefit of the guidance set forth in NYSEG, we cannot conclude on the basis of the information and analysis before us that H.Q. Energy has demonstrated that its affiliate Hydro-Quebec lacks generation market power in United States markets. Accordingly, we will direct H.Q. Energy to submit additional information and analysis, consistent with NYSEG, on generation market power. In the meantime, we will defer action on H.Q. Energy's request for market-based rates, pending receipt of such additional information and analysis.

1. Transmission Market Power

In the case of a power marketer that is affiliated with a transmission-owning United States utility, mitigating transmission market power requires the transmission-owning utility affiliate to have on file with the Commission an open access transmission tariff that conforms to the pro forma tariff

^{2/} E.g., Progress Power Marketing, Inc., 76 FERC ¶ 61,155 at 61,919 (1996); Northwest Power Marketing Company, L.L.C., 75 FERC ¶ 61,281 at 61,889 (1996). Accord, Heartland Energy Services, Inc., 68 FERC ¶ 61,223 at 62,060-63 (1994) (Heartland).

contained in the Open Access Rule (as modified on rehearing). ^{10/} In this case, the transmission-owning utility affiliate is Canadian.

In prior market-based rate cases involving power marketer affiliates of Canadian utilities, the Commission has applied the same general standards that we use for reviewing requests for market-based rates by power marketers affiliated with United States utilities. ^{11/} In Energy Alliance, for example, we stated that the marketer must be able to show that its transmission-owning utility affiliate offers non-discriminatory access to its transmission system that can be used by competitors of the power marketer to reach the United States. We added, however, that we would consider a variety of approaches when dealing with the market power of foreign utility affiliates of United States marketers. ^{12/} In Powerex, although we rejected the marketer's application for failure to demonstrate mitigation of transmission market power, we emphasized that the Commission, while wishing to assure reciprocal service into and out of Canada when Canadian entities seek access to United States markets, does not intend to open intra-Canadian electric markets by imposing open access tariffs for transactions wholly within Canada. Moreover, the Commission stated that it would determine on a case-by-case basis what tariffs, other than the Open Access Rule pro forma tariff, would satisfy our concerns, i.e., be consistent with our comparability principles. ^{13/}

In this case, H.Q. Energy has submitted proposed transmission tariffs under which Hydro-Quebec will provide transmission service that are virtually identical to the Open

^{10/} See Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 Fed. Reg. 21,540 (1996), FERC Stats. & Regs. ¶ 31,036 (1996), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Stats. & Regs. ¶ 31,048 (1997), reh'g pending (Open Access Rule).

^{11/} The cases include: Energy Alliance Partnership, 73 FERC ¶ 61,019 (1995) (Energy Alliance); TransAlta Enterprises Corporation, 75 FERC ¶ 61,268 (1996) (TransAlta); Powerex; and Ontario Hydro Interconnected Markets Inc., 78 FERC ¶ 61,369 (1997), reh'g pending (Ontario Hydro).

^{12/} 73 FERC at 61,030-31. Accord, TransAlta, 75 FERC at 61,875-76.

^{13/} See Powerex, 78 FERC at 61,100.

Access Rule pro forma tariff. The main difference is that while the pro forma tariff refers to the Commission as the applicable regulatory agency, these tariffs refer to the Regie. 14/ Similarly, the proposed tariffs substitute Canadian law for United States law -- e.g., Canadian commercial law in lieu of the Uniform Commercial Code. H.Q. Energy states that the transmission rates were developed using the Commission's standard average cost, rolled-in methods. While there are separate tariffs and charges for Hydro-Quebec and Cedar Rapids, customers using both services will pay only the Hydro-Quebec transmission charge.

The Crees argue that the proposed transmission tariffs are not equivalent to the Commission's pro forma tariff because they will be subject to the regulatory oversight of the Regie rather than this Commission. They complain that the Regie is not an adequate substitute for the Commission because it is appointed by the same government that owns Hydro-Quebec and because its decisions are not subject to judicial review. We disagree with the Crees' assumption that a foreign entity must submit to the Commission's jurisdiction for transmission services provided in foreign countries. The Commission's jurisdiction in this proceeding extends only to H.Q. Energy's jurisdictional power sales in the United States. As a condition of approving those sales, the Commission simply evaluates the transmission arrangements that are available in Canada (under the jurisdiction of Canadian governments and regulatory agencies) against the standards that the Commission requires for open access transmission services under our jurisdiction. Here, the terms and conditions of transmission service are identical to the Commission's pro forma tariff in all material respects.

The Crees also object to the use of a postage stamp rate in the proposed transmission tariffs. They argue that a postage stamp rate is discriminatory when the transmission grid extends over a large area. The Crees suggest that lower rates for shorter distances, or rates reflecting a zonal approach, would be more appropriate. The Crees also argue that use of the firm rate as the ceiling for the nonfirm rate is unreasonable. We disagree. The rates at issue here reflect rate designs previously approved by the Commission for jurisdictional transmission services, including in the Open Access Rule pro

14/ The Regie Act provides that the Regie will operate as an independent commission to regulate transmission rates on a traditional cost of service basis, establish terms and conditions of service and address service complaints.

forma tariffs. ^{15/} Moreover, Hydro-Quebec and Cedar Rapids will obtain transmission service for their own wholesale power sales under the proposed tariffs.

We conclude, therefore, notwithstanding the Crees' arguments, that Hydro-Quebec has mitigated its transmission market power adequately to support authorization of market-based rates for H.Q. Energy's United States wholesale sales.

2. Generation Market Power

The Commission's generation dominance analysis assumes that the seller, and its affiliates owning, operating or controlling transmission facilities, have satisfactory open access transmission available. As discussed above, H.Q. Energy has demonstrated compliance with that requirement. We find, however, as discussed below, that it has not provided sufficient information to demonstrate that its utility affiliate lacks generation market power.

While H.Q. Energy in its generation market analysis defines the relevant markets as those utilities with which Hydro-Quebec and Cedar Rapids are directly interconnected, it does not compute generation market shares using the Commission's hub-and-spoke method, which is the method that the Commission usually employs in market-based rate cases. ^{16/} Instead, H.Q. Energy analyzes the amount of customer load that could be served by each interconnected utility (including Hydro-Quebec), using the size of each customer's interconnections with potential suppliers as a proxy for load. H.Q. Energy contends that its analysis shows market shares below 20 percent, which do not exceed levels that the Commission previously has found acceptable. ^{17/}

As noted above, H.Q. Energy completed its application prior to the issuance of NYSEG. Thus H.Q. Energy prepared its generation market power analysis without the benefit of our discussion in NYSEG of why a similar approach to analyzing generation market power is insufficient for purposes of our market-based rate requirements. We explained in NYSEG that an analysis designed around the single factor of interconnection

^{15/} See Open Access Rule, FERC Stats. & Regs. ¶ 31,036 at 31,650, 31,668.

^{16/} See NYSEG, 78 FERC at 62,237-38 & n.5.

^{17/} See, e.g., Southwestern Public Service Company, 72 FERC ¶ 61,208 at 61,966-67 (1995), reh'g pending; Louisville Gas and Electric Company, 62 FERC ¶ 61,016 at 61,146 (1993) (Louisville).

capacity is so selective and incomplete as to provide no basis upon which to draw conclusions about market power. ^{18/} The Commission also stated that interconnection capacity is not irrelevant to market power issues and it is one of the factors that will be considered in the market screen analysis now being used for mergers. The Commission directed that any proposed substitute to the traditional hub-and-spoke analysis must "fully address all the competition factors considered under the market power analysis in the [Commission's] merger policy statement." ^{19/}

Accordingly, we will defer action on H.Q. Energy's market-based rate application until such time as H.Q. Energy provides further information and analysis concerning generation market power consistent with the discussion above and with our discussion in NYSEG. ^{20/}

3. Other Barriers to Entry/Reciprocal Dealing

Intervenors raise a number of issues regarding barriers to entry and affiliate abuse. Even though we are deferring action on H.Q. Energy's market-based rate application at this time, we nonetheless will address these matters here in order to give guidance to the parties in the event that H.Q. Energy supplements its application with a revised generation market power analysis, as this order permits.

With regard to potential barriers to entry and reciprocal dealing concerns, we note that Hydro-Quebec wholly owns Green Mountain Energy Partners, an energy service company that intends to sell electricity and natural gas at retail to United States customers. Additionally, Hydro-Quebec holds a substantial interest in Noverco, Inc., which in turn holds interests in the main natural gas distributor in the Province of Quebec and in a natural gas distributor in Vermont.

Were we to accept H.Q. Energy's application for market-based rates after submission of the additional generation market

^{18/} See 78 FERC at 62,328-29.

^{19/} *Id.* at 62,329 n.7. See Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act, Order No 592, 61 Fed. Reg. 68,595 (1996), FERC Stats. & Regs. ¶ 31,044 (1996). H.Q. Energy must address both physical and economic limitations on the definitions of the relevant product and geographic markets.

^{20/} We will provide notice and an opportunity for comments on the supplement.

concern. The code of conduct will be included as part of H.Q. Energy's rate schedule on file with this Commission, and any violations of the code can be reported to the Commission. Also, the code of conduct applies to all affiliates of Hydro-Quebec, without limitation. It does not exclude affiliates doing business in the United States, as the Crees mistakenly allege.

Finally, while the proposed code of conduct, as noted above, does not prohibit sharing market information beyond the OASIS Rule requirements, H.Q. Energy, in response to Niagara Mohawk's protest, agreed to revise the code of conduct in that regard. With this modification, which should be submitted along with the previously-discussed additional generation market power information, H.Q. Energy's code of conduct meets the Commission's requirements. In these circumstances, we are satisfied that there are no concerns of affiliate abuse here.

C. Waivers and Authorizations

H.Q. Energy, in its application, requests the same waivers and blanket authorizations as those afforded to other power marketers. Because we are deferring action on H.Q. Energy's application for market-based rates, there is no need to address the requested waivers and authorizations at this time.

D. Other Issues

The Crees complain that, while the Regie Act recognizes, for the first time, a market for wholesale energy competition in Quebec, Canadian wholesale purchasers must seek government approval prior to making purchases from suppliers other than Hydro-Quebec, and the Regie Act does not expressly recognize the authority of any utility other than Hydro-Quebec to act as a power marketer in Quebec. The Crees are concerned, therefore, that the Regie Act in practice may not lead to a competitive market. The Crees ask the Commission to condition approval of H.Q. Energy's application on amendments to Canadian laws to remove the requirement for Canadian government approval to obtain new suppliers and to recognize power marketers within Quebec on terms similar to those imposed by the Commission. To the extent the Crees seek our interference with trade that takes place wholly within Canada, we cannot do so. The market for power sales that take place wholly within Canada is beyond the scope both of this proceeding and of our jurisdiction.

We note that in Ontario Hydro, 78 FERC at 62,529, the Commission stated that it "seeks to assure reciprocal service into and out of Canada when Canadian entities seek access to United States markets." We believe that United States sellers should be able to sell to wholesale purchasers within Canada.

However, we also believe the Crees' concerns are premature at this time.

Conclusion

We note that with the exception of generation market power, H.Q. Energy has satisfied all our requirements for market-based rates. While we express no opinion on the ultimate resolution of the generation market power issue, we note that H.Q. Energy, and, for that matter, Hydro-Quebec, can utilize the open access tariffs of United States public utilities since the reciprocity condition is at this point fully satisfied. Thus, assuming an adequate showing can be made in its supplemental filing on generation market power, H.Q. Energy will be able to sell at market-based rates. Until that time, it would be able to transact at cost-based rates for the resale of power purchased either from Hydro-Quebec or from non-affiliates.

The Commission orders:

(A) The motions for late intervention of CNG Energy and ConEd are hereby granted.

(B) The late-filed comments of Newfoundland Hydro are hereby accepted.

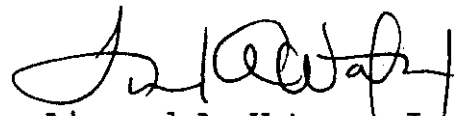
(C) The motions to intervene of the Crees and Mouvement Au Courant are hereby granted, and their respective late-filed pleadings are hereby accepted.

(D) H.Q. Energy's responses are hereby accepted.

(E) Action on H.Q. Energy's application for market-based rates, and related waivers and authorizations, is hereby deferred, and H.Q. Energy is hereby directed to provide additional information and analysis concerning generation market power and to amend its proposed code of conduct, as discussed in the body of this order.

By the Commission. Commissioners Bailey and Santa concurred with separate statements to be issued later.

(S E A L)


Linwood A. Watson, Jr.,
Acting Secretary.