

COMPETITION & ENERGY UPDATE

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Contacts

Washington DC Office

1900 K Street, NW
Washington, DC 20006-1109

William F. Young

(202) 955-1684
byoung@hunton.com

D. Bruce Hoffman

(202) 955-1619
bhoffman@hunton.com

Patrick J. McCormick III

(202) 778-2218
pmccormick@hunton.com

Antitrust Division Obtains Substantial Penalty for Conduct Approved by FERC

On February 23, the Antitrust Division of the U.S. Department of Justice posted documents relating to a significant settlement of antitrust claims against KeySpan Corp. The settlement requires KeySpan to "disgorge" \$12,000,000 of profits that were asserted to be improper because of a financial "swap" arrangement relating to the market for "installed capacity" in New York City. Sales of "installed capacity" give the buyer the right to call on specified generation to produce electricity when needed. During the relevant period, KeySpan owed approximately 2,400 MW of electric generating capacity in New York City. The Antitrust Division alleged that the financial "swap" was an anticompetitive agreement in violation of the Sherman Act.

The settlement is significant because:

- It is based on an unusual remedy of "disgorgement" of profits from an antitrust violation;
- It acknowledges that a private damages suit against KeySpan would likely fail because of the "filed rate doctrine," meaning that a court would find that KeySpan was charging rates for installed capacity that were approved by the Federal Energy Regulatory Commission ("FERC"); and

- The same conduct was found by FERC not to involve collusion, not to violate the applicable tariff and not to have adversely affected the relevant market.

The swap involved an agreement between KeySpan and an unnamed financial services company, and a further agreement between the financial services company and another entity owning installed generating capacity in New York City. Under the first agreement, if the price for installed capacity in New York City went above \$7.57 per kilowatt (kW)-month, the financial services company would pay KeySpan the difference between the market price and \$7.57 times 1800 MW, with payment in the opposite direction if the market price went below that level. Contemporaneously, the financial services company entered into a second agreement with another entity with significant generating capacity in New York City. Under that agreement, if the price for capacity went above \$7.07 per kW-month, the other generator would pay the financial services company the difference times 1800 MW, and vice versa.

The Antitrust Division asserted that these agreements effectively eliminated KeySpan's incentive to compete for sales of installed capacity, with the result that

but for the swap, installed capacity would likely have been sold at a lower price in New York City. According to the Competitive Impact Statement (“CIS”) accompanying the settlement, the settlement “requires KeySpan to disgorge profits gained as result of its unlawful agreement restraining trade.” The CIS states that the Antitrust Division has not previously sought disgorgement as a remedy under the Sherman Act, but believes that it can do so because courts have the authority to order such equitable relief.

The Antitrust Division took action against KeySpan notwithstanding the fact that FERC, which has regulatory authority over installed capacity

markets, investigated KeySpan and the swap and in a report issued on February 28, 2008, found that: (a) KeySpan’s offering behavior was not affected by the swap, (b) KeySpan did not engage in collusion to impair the functioning of the installed capacity market in New York City and (c) KeySpan’s behavior did not violate the applicable tariff of the New York Independent System Operator, Inc., the entity that administers the installed capacity markets in New York. That tariff, which had been approved by FERC, includes bid caps as a remedy against possible withholding of capacity by entities with market power in the New York City installed capacity market.

The settlement is a powerful reminder to participants in electricity or other regulated or partially regulated markets that compliance with applicable tariffs and agency rules may not provide immunity from antitrust scrutiny. The new “disgorgement” remedy also appears indicative of a commitment to an innovative approach to enforcement at the Antitrust Division under the leadership of Assistant Attorney General Christine Varney.

If you have questions about the settlement or its potential impact on electricity or other markets, please contact William Young, Bruce Hoffman or Patrick McCormick.