UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Technical Conference on Public Utility Holding Company Act of 2005 and Federal Power Act Section 203 Issues	Docket No. AD07-2-001

OPENING REMARKS OF MARK S. HEGEDUS[*]
ON BEHALF OF
TRANSMISSION ACCESS POLICY STUDY GROUP

On behalf of the Transmission Access Policy Study Group ("TAPS"), I want to thank the Commission for organizing this technical conference and inviting TAPS to participate. Like APPA, TAPS urged the Commission to undertake an examination of the adequacy of its merger review approach in light of changes in the electricity industry in the ten years since the Commission's adoption of its Merger Policy[1] and the industry's growing appreciation that methods of competitive analysis that may suffice for other industries do not suffice for the electricity industry.[2] My remarks today are informed by the experiences of TAPS members who have been intervenors in Commission merger proceedings, as well as by my (1) tenure as an attorney with the Antitrust Division, U.S. Department of Justice, where I investigated electricity industry mergers and acquisitions and (2) understanding of the European Commission's approaches to competitive analysis

---

[*] Partner, Spiegel & McDiarmid, 1333 New Hampshire Avenue, NW, Washington, DC 20036, 202-879-4000, mark.hegedus@spiegelmcd.com.

[1] *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, 61 Fed. Reg. 68,595 (Dec. 30, 1996), [1996-2000 Regs. Preambles] FERC Stat. & Regs. ¶ 31,044 (1996), *reconsideration denied*, Order No. 592-A, 62 Fed. Reg. 33,340 (June 19, 1997), 79 F.E.R.C. ¶ 61,321 (1997).

[2] *See, e.g.*, Severin Borenstein, James Bushnell and Christopher R. Knittel, *Market Power in Electricity Markets: Beyond Concentration Measures*, 20 Energy L. J. 65 (1999).

of the electricity industry, which I gained during the past four years while living in Brussels, Belgium.

In responding to the three sets of questions posed on this afternoon's agenda, TAPS urges the Commission to make the following changes to its merger policy:

1. Incorporate an analysis of competitive effects into merger analysis, including those effects that are not apparent from an assessment of concentration measures.
2. Enlarge the scope and types of information required to be filed by merger applicants, including documents merger applicants already must file under Hart-Scott-Rodino.
3. Consider limited, notice-period discovery so that the Commission has the benefit of a larger body of facts when ruling on a merger.
4. Use the Commission's procedural flexibility to examine controversial mergers more closely via technical conferences and Track One-type hearings.
5. Develop regional models to analyze mergers, taking advantage of development of the proposed regional approach to analyzing market-based rate authorizations and the Office of Enforcement's expanding capabilities.

Should the Commission retain the factors it currently uses in reviewing mergers (effect on competition, rates and regulation)? Are any revisions needed in the focus of the current factors?

TAPS does not propose that the Commission change the factors it uses to assess mergers. It does believe revisions in the focus of those factors are needed, however, particularly regarding the effect on competition factor.

The central problem with Commission's current approach under Appendix A of the Merger Policy Statement is that it does not assess a proposed transaction's effect on competition. Passing or failing an Appendix A screen is not a competitive effect. Examples of competitive effects include higher prices, reduced output and price discrimination, none of which Appendix A requires to be analyzed. While Appendix A

purports to be based upon the antitrust agencies' Merger Guidelines,[3] Commission analysis begins and ends with the first step required by the Guidelines – calculation of market shares and HHIs ("Herfindahl-Hirschman Index") – and ignores the other four steps.[4] Few Commission merger orders, especially of late,[5] include a competitive effects analysis that is based upon a theory of competitive harm. The Commission typically does not express why a particular transaction will or will not lead to higher prices, for example. When intervenors articulate harm theories that are not dependent upon HHIs, such as a strategic bidding theory, the Commission responds by claiming that proposed mitigation addresses intervenor concerns because the mitigation returns HHIs to pre-transaction levels.[6] Such a response, however, does not address competitive effects unrelated to HHIs in the first place.

In this regard, I want to express my support for the comments offered earlier today by Sue Kelly, on behalf APPA, and Professor Darren Bush. As they note, narrow application of Appendix A's concentration measures will cause the Commission to overlook competitive harms including, for example, harms associated with the loss of potential competitors. In addition, this singular focus on concentration measures risks the Commission's giving short-shrift to market-specific facts that do not fit into the

---

[3] United States Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines (1992).

[4] Appendix A characterizes concentration calculations as the "final step" of the competitive analysis and suggests, but does not require, analyzing the Merger Guidelines' other four factors -- competitive effects, entry, efficiency and failing firm – only if the DoJ concentration thresholds are exceeded. Merger Policy Statement, Appendix A, 61 Fed. Reg. 68,608-09.

[5] Compare *Am. Elec. Power Co. & Central & Southwest Corp.*, 85 F.E.R.C. ¶ 61,201, at 61,819 (1998), *reh'g denied*, 87 F.E.R.C. ¶ 61,274 (1999), to *Exelon Corp.*, 112 F.E.R.C. ¶ 61,011 (2005), *reh'g denied*, 113 F.E.R.C. ¶ 61,299 (2005).

[6] *See Exelon*, 112 F.E.R.C. ¶ 61,011 at P 132.

concentration framework, such as a merger that provides the merged firm a combination of infra-marginal and marginal resources that gives it the ability and incentive to raise prices, despite the merger's passing the screens.

Turning to the other factors, the Merger Policy's examination of a merger's effect on rates is generally not problematic, but is affected by Commission decisions in other areas. Concerns can arise to the extent customers' or the Commission's ability to police hold-harmless clauses and the like is impaired by lack of access to relevant information. For this reason, the ongoing inquiry regarding FERC Forms[7] and the Commission's decisions about PUHCA's books, records and reporting requirements[8] bear on the enforceability of these hold-harmless clauses. Similarly, an open season to choose alternative suppliers is of no value if the merging firm's constrained transmission system will not give customers meaningful access to alternatives.

Effect on regulation concerns can arise to the extent the Commission refrains from remedial actions out of concern for potential overlaps with state regulation. Overlaps will not arise where a state lacks authority to review certain kinds of mergers, which is the case under state laws in Florida, Indiana, Michigan, Montana, Nebraska, South Dakota, Massachusetts and Virginia.[9] Indeed, under the Merger Policy, the Commission will review effects on retail competition where a state requests that the

---

[7] *Assessment of Information Requirements for FERC Financial Forms*, Docket No. RM07-9 (2007).

[8] *Repeal of the Public Utility Holding Company Act of 1935 and Enactment of the Public Utility Holding Company Act of 2005*, Docket No RM05-32, Order No. 667, 70 Fed. Reg. 75592 (Dec. 20, 2005), FERC Stats. & Regs. ¶ 31,197 (2005); Order No. 667-A, 71 Fed. Reg. 28446 (May 16, 2006), FERC Stats. & Regs. ¶ 31,213 (2006); Order No. 667-B, 71 Fed. Reg. 42750 (July 28, 2006), FERC Stats. & Regs. ¶ 31,224 (2006); Order No. 667-C, 118 F.E.R.C. ¶ 61,133 (2007).

[9] Robert E. Burns and Michael Murphy, *Repeal of the Public Utility Holding Company Act of 1935: Implications and Options for State Commissions*, 19 ELECTRICITY JOURNAL 32, 39 n.15 (Oct. 2006); MASS. GEN. LAWS ch. 164, § 96; VA. CODE ANN. § 56-88.1.

Commission do so because the state itself lacks authority.[10] Overlap concerns also do not exist where the Commission's jurisdiction is exclusive, such as interstate transmission service and sales to wholesale customers.

> ***At present, and taking into account the Commission's ex parte rule prohibitions regarding pending contested proceedings and the new section 203 requirement that the Commission act on a merger application within 180 days of filing (with one additional 180 days for good cause shown), is the level of coordination appropriate between the Commission and other Federal and state agencies involved in merger review? Is the level of information exchange between the Commission and other agencies adequate?***

The questions posed underscore the need for the Commission to structure merger reviews in ways that accommodate *ex parte* rules and timing requirements yet yield a factual record sufficient to analyze a transaction. The questions suggest that one way to deal with these issues is via information exchanges among agencies, though it is not clear how that can be accomplished consistent with the Commission's *ex parte* rules, the procedural requirements of the Administrative Procedure Act, and other agencies' obligations to maintain the confidentiality of certain kinds of information.

While TAPS believes that inter-agency coordination is beneficial as a means for to learn from each agency's best practices, coordination should not necessarily lead to identical outcomes. The Constitution and our nation's form of government purposefully disperses decision-making. If consistency were paramount, we would have centralized decision-making. This diversity is reflected as well in the statutory provisions applied by various agencies. Under Clayton Act, Section 7, the Antitrust Division assesses mergers

---

[10] *See, e.g., American Electric Power Co. and Central and Southwest Corp.*, 85 F.E.R.C. ¶ 61,201, at 61,819 (1998).

to determine whether they might substantially lessen competition.[11] Under the FPA, the Commission must determine whether a merger is consistent with the public interest,[12] which is a broader standard.

More important is that the Commission understand why its decisions are different from other agencies, such as the Antitrust Division's, and that the reasons for these differences be justifiable. For example, this Commission's failure to consider some kinds of merger harms simply because they do not fit within the Commission's HHI-centered analytical framework would not be a justified difference, given concentration measures' known limitations as a market power metric in the electricity industry. On the other hand, the Commission's requiring a more extensive merger remedy than one mandated by the Antitrust Division would be justifiable to the extent necessary to ensure that a transaction is consistent with the public interest. For example, the Commission might decide that the public interest in wholesale competition and the impairment of such competition resulting from inadequate transmission investment requires a commitment on the part of the merged firm to expand the transmission grid, to offer opportunities for investment, including by transmission dependent utilities, or to divest transmission. The Commission certainly would be empowered to impose such conditions, just as it has previously conditioned merger approvals on the applicants' filing of open access transmission tariffs or joining of RTOs.[13]

---

[11] 15 U.S.C. § 18.

[12] 16 U.S.C. § 824b.

[13] *See, e.g., Utah Power & Light Company, PacifiCorp and PC/UP&L Merging Corporation*, 45 F.E.R.C. ¶ 61,095 at 61,287–89 (1988), *order on reh'g*, 47 F.E.R.C. ¶ 61,209, *order on reh'g*, 48 F.E.R.C. ¶ 61,035 (1989), *remanded in part sub nom. Environmental Action, Inc. v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991), *order on remand* 57 F.E.R.C. ¶ 61,363 (1991); *American Electric Power Co. and Central and Southwest*

To ensure that the Commission has information needed to fully analyze a merger, while respecting both time limits on Commission review and *ex parte* requirements, TAPS has the following suggestions.

First, the Commission can reduce the need for trial-type procedures by requiring that additional, relevant and pre-existing information and data be submitted as part of the initial section 203 application. Applicants should submit the transaction-background information that they must already prepare for the antitrust agencies under the Hart-Scott-Rodino Antitrust Act, including (1) documents about the transaction filed with the Securities and Exchange Commission, (2) annual reports and audits, as well as regularly prepared balance sheets, and (3) studies, surveys, analyses and reports prepared by or for any officers or directors for the purpose of evaluating or analyzing the transaction with respect to market shares, competition, competitors, markets, potential for sales growth or expansion into product or geographic markets.[14] Reviewing such information is an example of an antitrust agency best practice that the Commission should adopt.[15]

Applicants should also submit all data sets examined but not used by them in preparing their Appendix A analysis. Merger applicants will ordinarily have put their economic teams together well in advance of the filings with the Commission, and will have spent months examining various iterations of the potential data available, in order to

---

Corp. 90 F.E.R.C. ¶ 61,242, at 61,786-90 (2000).

[14] 16 C.F.R. pt. 803. This information is frequently referred to as "4(c) documents" and is required to be prepared by all merging parties subject to the HSR Act. Antitrust Improvements Act Notification and Report Form for Certain Mergers and Acquisitions, Instructions, Item 4 (*available at* http://www.ftc.gov/bc/hsr/050407InstructRpt.pdf). It is far less burdensome than the "Second Request" response required in a small number of antitrust agency investigations.

[15] To the extent such information is competitively sensitive, the Commission can limit through protective orders who may be reviewing representatives and use its beefed-up penalty authority and other sanctions for violations of the protective orders.

create a favorable record. The rejected data are clearly relevant to the Commission's assessment of the transaction.

Particularly if the Commission does not expand the kinds of information that it requires applicants to submit, consideration should be given to a limited right to discovery during the initial notice period. Discovery should be available only to parties that have filed a motion to intervene so that applicants can determine whether the requesting party would have a legitimate interest in using the discovery for purposes of the Commission's review of the transaction. Reasonable limitations to prevent discovery from being unduly burdensome could be considered. Discovery requests and responses should also be filed with the Commission so that its staff has access to the information.

Second, the Federal Power Act and Administrative Procedure Act provide the Commission with significant flexibility to structure proceedings to allow the development of the record without resort to time-consuming, trial-type proceedings. Issues such as market definition, competitive harms and adequacy of mitigation are fact-intensive, and it is quite amazing to me, as a former investigative attorney, that one can satisfactorily develop a record upon which to make a decision without posing questions to the parties in possession of the facts underlying the merger. This is especially true as PUHCA's repeal gives rise to mergers presenting novel issues. To comply with statutory requirements that it act within 180 or 360 days, the Commission should rely on on-the-record technical conferences and, where necessary, expedited trial-type hearings, *e.g.* Track One Hearings. Such proceedings would also provide a forum for Federal and state coordination.

What would be the pros and cons of having the Commission use a regional market computer model to analyze mergers? Would there be extensive data inputs that would be needed to run such a model, and what would be the resource commitments and costs associated with the Commission running such a model?

The Commission should not address the question of whether to adopt a regional market model in isolation from its other proceedings where market power questions are relevant. In particular, the Commission's analysis of market power for purposes of market-based rates should not vary greatly from its competition analysis of mergers. TAPS supports the Commission's proposal for regional assessments of market-based rate authority,[16] and we see no reason why the regional analytical models developed in that context cannot be adapted for merger review. The Commission can certainly require submission of data necessary to run such a model as part of a merger application or as a condition of market-based rate authority. Further, there presumably will be coordination within the Commission so that the growing information resources of the Office of Enforcement can aid in the Commission's development and use of such a model.

Further, while EPAct 2005 expanded the subject matter of the Commission's merger review, others continue to advocate that electric merger review, at least at the federal level, be the exclusive domain of the antitrust agencies.[17] If policy makers believe that the Commission adds value to merger review, it is less likely to lose this

---

[16] *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Notice of Proposed Rulemaking, 71 Fed. Reg. 33,102 (June 7, 2006), IV F.E.R.C. Stat. & Regs. ¶ 32,602 (to be codified at 18 C.F.R. pt. 35).

[17] *See, e.g.,* Report on Electric Merger Review by the [American Bar Association] Section of Antitrust Law to the Antitrust Modernization Commission, at 2 (July 2006) (recommending that electric mergers be subject to a single review by DoJ or FTC on grounds, among others, that FERC's "narrower HHI-centered analysis does not adequately probe a merger's likely competitive effects and has led to more wooden enforcement in the electric power sector"), *available at* http://www.amc.gov/public_studies_fr28902/regulated_pdf/060717_ABA_Regulated.pdf.

important authority. The Commission's enhancing its ability and reputation for sound assessment of competition in electricity markets would lend further support to its retaining merger authority in the face of these calls for removal. Nor should the Commission lose this authority.[18] No other agency has the Commission's obligation to protect consumers from exploitation by non-competitive utilities or the Commission's resources for fulfilling this responsibility. At least within electricity industry, the antitrust agencies' responsibilities are not nearly as broad as the Commission's, and those agencies certainly do not have the statutory authority or resources to develop and maintain electric market expertise. The Department of Energy's responsibilities are not particularly focused on economic regulation. And no state is in position to fulfill this function. The responsibility and the opportunity is the Commission's.

Thank you.

March 8, 2007

---

[18] TAPS hopes that the Commission itself wishes to retain this authority.