

122 FERC ¶ 61,157
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Sudeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

FPA Section 203 Supplemental Policy Statement

Docket No. PL07-1-001

ORDER ON CLARIFICATION AND RECONSIDERATION

(Issued February 21, 2008)

1. On July 20, 2007, the Commission issued a Supplemental Policy Statement¹ as a supplement to the Commission's rulemakings issued in 2006 to implement provisions of the Energy Policy Act of 2005 (EPA 2005)² and also as a supplement to its 1996 Merger Policy Statement.³ Motions for clarification and/or additional comments were filed by Entegra Power Group LLC (Entegra) and the American Antitrust Institute

¹ *FPA Section 203 Supplemental Policy Statement*, 72 Fed. Reg. 42,277 (Aug. 2, 2007), FERC Stats. & Regs. ¶ 31,253 (2007) (Supplemental Policy Statement).

² 16 U.S.C. § 824b (2000 & Supp. V 2005); *see Transactions Subject to FPA Section 203*, Order No. 669, 71 Fed. Reg. 1,348 (Jan. 6, 2006), FERC Stats. & Regs. ¶ 31,200 (2005), *order on reh'g*, Order No. 669-A, 71 Fed. Reg. 28,422 (May 16, 2006), FERC Stats. & Regs. ¶ 31,214, *order on reh'g*, Order No. 669-B, 71 Fed. Reg. 42,579 (July 27, 2006), FERC Stats. & Regs. ¶ 31,225 (2006); *Repeal of the Public Utility Holding Company Act of 1935 and Enactment of the Public Utility Holding Company Act of 2005*, Order No. 667, 70 Fed. Reg. 75,592 (Dec. 20, 2005), FERC Stats. & Regs. ¶ 31,197 (2005), *order on reh'g*, Order No. 667-A, 71 Fed. Reg. 28,446 (May 16, 2006), FERC Stats. & Regs. ¶ 31,213, *order on reh'g*, Order No. 667-B, 71 Fed. Reg. 42,750 (July 28, 2006), FERC Stats. & Regs. ¶ 31,224 (2006), *order on reh'g*, Order No. 667-C, 72 Fed. Reg. 8,277 (Feb. 26, 2007), 118 FERC ¶ 61,133 (2007).

³ *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), FERC Stats. & Regs. ¶ 31,044 (1996) (1996 Merger Policy Statement), *reconsideration denied*, Order No. 592-A, 62 Fed. Reg. 33,341 (June 19, 1997), 79 FERC ¶ 61,321 (1997).

(AAI).⁴ This order denies these requests for clarification and reconsideration of the Supplemental Policy Statement.⁵

I. Background

2. The Supplemental Policy Statement provided guidance regarding the Commission's future implementation of section 203. In particular, the Commission provided certain clarifications and guidance concerning: (1) the information that must be filed as part of section 203 applications for transactions that do not raise cross-subsidization concerns; (2) the types of applicant commitments and ring-fencing measures that, if offered, might address cross-subsidization concerns; (3) the scope of the blanket authorizations under sections 203(a)(1) and section 203(a)(2); (4) what constitutes a disposition of control of jurisdictional facilities for purposes of section 203; and (5) the Commission's Appendix A analysis, an analytical framework for assessing a merger's effect on competition in wholesale electric markets.

II. Discussion

A. Secondary Market Transactions

3. In the Supplemental Policy Statement the Commission clarified that under certain circumstances neither public utilities nor public utility holding companies have an obligation to seek approval under section 203(a)(1)(A) for a "disposition" of public utility jurisdictional facilities in transactions for the purchase or sale of the securities of a public

⁴ The American Public Power Association, National Rural Electric Cooperative Association and Transmission Access Policy Study Group filed comments in support of AAI's comments.

⁵ Policy statements are not subject to rehearing. *See, e.g., Transmission Agency of N. Cal. v. FERC*, Case No. 05-1400, 2006 U.S. App. LEXIS 6177 (D.C. Cir. Mar. 13, 2006) (unpublished opinion) (finding no injury-in-fact to warrant administrative review of a policy statement that has not yet been applied to petitioners); *Am. Gas Ass'n v. FERC*, 888 F.2d 136, 151-52 (D.C. Cir. 1989) (policies are not ripe until applied specific cases); *Inquiry Regarding Income Tax Allowance*, 112 FERC ¶ 61,203, at P 4 (2005) ("The Commission's normal practice is to dismiss requests for rehearing of policy statements and reserve any further discussions of the issues contained therein for specific proceedings in which the policy is applied."). However, we may, at our discretion, clarify policy statements or entertain reconsideration. We do so here.

utility or its upstream holding company that are made by third parties (secondary market transactions).⁶ Entegra requests that the Commission clarify that secondary market transactions include “circumstances where: (1) the securities are regularly traded but are not necessarily traded at a volume of thousands of shares per day on a public exchange and (2) the public utility or its holding company may review proposed transactions in advance and play a ministerial role in approving the transactions but is not a party to them.”⁷ We will deny Entegra’s request as unsupported at this time.

4. The Commission’s clarification of FPA section 203(a)(1)(A) in the Supplemental Policy Statement was based on Mirant Corporation’s (Mirant) description of circumstances in which: (1) common stock is publicly traded; (2) huge volumes may change ownership every day between third-party investors in arm’s-length transactions; (3) neither the holding company nor its public utility subsidiaries are parties to the transactions; (4) neither the holding company nor its public utility subsidiaries have any control over transfers of the common stock; and (5) neither the holding company nor its public utility subsidiaries are required to be given prior notice of these transactions.⁸ Under these circumstances Mirant argued that, if the Commission did not grant its requested clarification, “the Commission would create an obligation that would be impossible for any public utility to perform if the stock of its holding company is widely-held and publicly-traded (such as Mirant’s).”⁹ Mirant also stated that imposition of such an obligation “would likely decrease the liquidity of Mirant common stock and exert downward pressure on share prices.”¹⁰

5. In contrast, Entegra asks us to find that section 203(a)(1)(A) does not apply to secondary market transactions involving a public utility or public utility holding company whose securities are not publicly traded. Entegra does not claim that, without the requested clarification, a public utility would be put in an impossible position of having to seek authorization for transactions it knew nothing about. Rather, unlike the situation addressed in the Supplemental Policy Statement, Entegra describes a situation in which a public utility has notice of the proposed transactions before they are consummated and

⁶ Supplemental Policy Statement, FERC Stats. & Regs. ¶ 31,253 at P 36.

⁷ Entegra Comments at 1.

⁸ Mirant January 26, 2007 Comments, Docket No. AD07-2-000, at 6.

⁹ *Id.* (emphasis in the original).

¹⁰ *Id.* at 7.

even has a role in approving such transactions despite the fact that it is not a party to them.¹¹

6. We note further that the Commission has granted Entegra and a number of other similarly situated public utilities blanket authorizations under section 203 for secondary market trading of their securities.¹² In these cases, particularly where the Commission authorized acquisitions and holdings of up to 20 percent of the public utility, the Commission conditioned the authorizations to address case-specific concerns over changes in control and potential adverse effects on competition. Among these conditions is a requirement that the acquiring party must be a financial-type entity and not primarily engaged in an energy-related business. The Commission has also restricted the acquiring party from holding more than five percent of another jurisdictional asset within the same market area. To interpret section 203(a)(1)(A) not to require a public utility to seek approval of what may be an indirect disposition of control of jurisdictional facilities in circumstances in which the public utility knows of and has a role in such transactions would generically eliminate these conditions which we have found, on a case-by-case basis, to be necessary to address our concerns under section 203. We note that Entegra does not claim that the conditions on its blanket authorizations impede the trading of public utility or public utility holding company securities. Therefore, we deny Entegra's request for clarification.

B. Appendix A Analysis

7. In the Supplemental Policy Statement, the Commission reviewed concerns about whether the Commission's Appendix A analysis is sufficient to identify market power concerns. The Supplemental Policy Statement explained that the Commission will continue to use the analytical screens adopted by the Commission in the 1996 Merger Policy Statement to help identify mergers that have the potential to harm competition, but that the Commission's review goes beyond those screens and looks at all relevant factors regarding the effect on competition. The Commission stated that it will continue to

¹¹ We note that in its applications requesting blanket authorizations under section 203, Entegra identifies the proposed investors or represents that only certain types of investors with limited interests in the energy industry would be eligible to acquire interests in Entegra's jurisdictional facilities. *See* Entegra Power Group LLC October 24, 2005 Application, Docket No. EC06-15-000, at 7-15; Entegra Power Group LLC February 10, 2006 Application, Docket No. EC06-78-000, at 1-2.

¹² *See Entegra Power Group LLC*, 119 FERC ¶ 62,218 (2007) (order amending blanket authorizations provided for in: *Entegra Power Group LLC*, 113 FERC ¶ 62,185 (2005); *Entegra Power Group LLC*, 115 FERC ¶ 62,038 (2006); *Entegra Power Group LLC*, 117 FERC ¶ 61,085 (2006); *Entegra Power Group LLC*, 118 FERC ¶ 61,181 (2007)).

analyze both horizontal and vertical mergers by focusing on the merger's effect on a company's ability and incentive to exercise market power. In particular, the Commission clarified that in horizontal mergers, if an applicant fails the Competitive Analysis Screen (one piece of the Appendix A analysis), the Commission's analysis focuses on the merger's effect on the merged firm's ability and incentive to withhold output in order to drive up the market price. The Commission stated that the ability to withhold output depends on the amount of marginal capacity controlled by the merged firm, and the incentive to do so depends on the amount of infra-marginal capacity that could benefit from higher prices.¹³

8. AAI argues that the Supplemental Policy Statement rejects, without adequate justification, concerns raised at the March 8, 2007 technical conference regarding the Commission's Appendix A analysis. AAI files comments on two specific areas in which it believes the Supplemental Policy Statement falls short of providing a justification for maintaining the status quo approach.

9. First, AAI argues that evidence demonstrates that the Commission's merger analysis does not always go sufficiently beyond concentration statistics to render sound decisions. AAI maintains that the Commission should go beyond section 1 of the Horizontal Merger Guidelines (defining markets and evaluating market concerns) and address section 2 as well (analysis of potential adverse competitive effects). AAI argues that the Commission erred in finding that competitive effects play a relatively minor role in the Commission's merger analysis. AAI argues that the cases cited in the Supplemental Policy Statement are not relevant to the competitive effects analysis and/or are old. AAI maintains that the Commission's more recent cases highlight the importance of having an appropriate and relevant analysis of likely merger-related harms.¹⁴

10. Second, AAI argues that the Commission errs in relying on Applicant-performed analyses as a fail-safe method for screening mergers. AAI argues that for exclusive reliance on Applicant-performed analyses to be even remotely fail-safe, it has to be obtained at the expense of limiting the scope and flexibility of what analysis can be performed. AAI also argues that there are inconsistencies in Applicant-performed analyses across merger cases, and the Commission's internal use of economic models to corroborate findings could reduce the possibility of errors.

11. We find that AAI has not provided any additional information that would warrant reconsideration of the findings in the Supplemental Policy Statement. AAI essentially repeats its argument that the Commission is overly concerned with the Herfindahl-

¹³ Supplemental Policy Statement, FERC Stats. & Regs. ¶ 31,253 at P 60.

¹⁴ AAI Comments at 4 (citing *Exelon Corp.*, 112 FERC ¶ 61,011 (2005)).

Hirschman Index (HHI)¹⁵ and should instead focus on the potential competitive harm resulting from a merger. The Commission addressed this argument in the Supplemental Policy Statement: “the Commission does look beyond the change in HHI in its analysis of the effect on competition in both horizontal and vertical mergers. The change in HHI serves as a screen to identify those transactions that could potentially harm competition.”¹⁶ The Commission also explained that it typically considers a case-specific theory of competitive harm, which includes, but is not limited to, an analysis of the merged firm’s ability and incentive to withhold output in order to drive up prices.

12. Furthermore, in the merger orders issued since the issuance of the Supplemental Policy Statement, the Commission has articulated its theory of competitive harm. For example, in *Energy East Corporation*,¹⁷ the Commission stated that in mergers combining electric generation assets with inputs to generating power (such as natural gas, transmission or fuel), competition can be harmed if a merger increases the merged firm’s ability or incentive to exercise vertical market power in wholesale electricity markets. The Commission stated that by denying rival firms access to inputs or by raising their input costs, a merged firm could impede entry of new competitors or inhibit existing competitors’ ability to undercut an attempted price increase in the downstream wholesale electricity market. The Commission found that the applicants had shown that the proposed transaction did not raise any of these concerns because: (1) they did not have operational control over transmission facilities so they lacked the ability to impede access to competition; and (2) they lacked both the ability and the incentive to use control of natural gas transportation to harm competition in any relevant market.

13. Articulating a theory of competitive harm and explaining why a merger applicant has shown that a merger will not adversely affect competition, or why mitigation will be necessary to address the harm to competition, will provide additional guidance to both applicants and intervening parties. We will continue this practice and, as we stated in the Supplemental Policy Statement, expect both applicants and interveners to frame their arguments regarding a merger’s effect on competition in terms of a theory of merger-

¹⁵ As part of the screen analysis, applicants must define the relevant products sold by the merging entities, identify the customers and potential suppliers in the geographic markets that are likely to be affected by the proposed transaction, and measure the concentration in those markets. Using the Delivered Price Test to identify alternative competing suppliers, the concentration of potential suppliers included in the defined market is then measured by the HHI and used as a screen to determine which transactions clearly do not raise market power concerns. 1996 Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,119-20.

¹⁶ Supplemental Policy Statement, FERC Stats. & Regs. ¶ 31,253 at P 65.

¹⁷ 121 FERC ¶ 61,236, at P 23 (2007).

related harm to competition. The HHI screen serves as a useful tool in identifying those mergers that may harm competition in a relevant wholesale electricity market, but the extent of our analysis goes beyond the screen.

14. AAI's argument that the Commission relies on Applicant-performed analyses as a fail-safe method for screening mergers is incorrect. As we explained in the Supplemental Policy Statement, an applicant's Appendix A analysis is the first step in the Commission's review process. The Appendix A analysis, which includes an economic model (the Delivered Price Test (DPT)), was developed by the Commission and provides a consistent framework for the analysis of a merger's effect on competition. Once it is filed by the applicant, the Appendix A analysis is available for review and comment by all interested parties, including state commissions and customers, and, importantly, can be replicated by them in the limited time period available for public comment.¹⁸ Moreover, the Commission makes its decision in each case based on evidence that is available to all parties to the proceeding. If the analysis as submitted by the applicant is not adequate, the Commission can, and does, direct the applicant to submit additional record evidence. Such evidence, like the original application, would be reviewed by and subject to challenge by all interested parties. On this basis, neither the Commission nor interveners are disadvantaged by the Commission's policy of requiring Applicant-performed analyses.

15. AAI requests that the Commission essentially adopt the review process of the antitrust agencies, without regard to the fundamental differences between the Commission's process and that of the antitrust agencies. The Commission's review process is public and parties can intervene and submit comments, while the review process at the antitrust agencies is nonpublic and closed. As noted above, the Commission's merger decision is based on a factual record shaped not only by the applicant, but by intervenors and subject to analysis by Commission staff. The merger decisions by antitrust agencies are based on information submitted by the applicant, non-public information gathered by the agency staff, as well as the economic analysis performed by agency staff. The argument that our merger decision is based solely on the applicants' analyses ignores the participation of other parties, and Commission staff's review of the factual record. We believe our approach is sound.

16. Finally, in response to AAI's argument that there are inconsistencies in Applicant-performed analyses across merger cases, if the results of the DPT in one proceeding are significantly inconsistent with those in another case, the Commission and interveners can challenge those results and applicants would have the opportunity to explain any relevant

¹⁸ See Supplemental Policy Statement FERC Stats. & Regs. ¶ 31,253 at P 69, 71.

differences.¹⁹ The Commission is not bound to follow the analysis of the applicants. Rather, the Commission analyzes the entire record and determines what result is appropriate based on the entire record, and the Commission provides its analysis of the record in the public order that it issues.

17. Accordingly, we deny AAI's request for clarification.

The Commission orders:

The requests for clarification and reconsideration are hereby denied as set forth in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

¹⁹ See, e.g., *Ameren Corp.*, 108 FERC ¶ 61,094 (2004), *order on reh'g*, 111 FERC ¶ 61,055 (2005). In that case, intervenors challenged the applicants' inclusion of over 4,000 megawatts of competing generation in the DPT, which Ameren had not included in a previous proceeding. The applicants responded with an explanation that relevant products were different in the two cases (firm network resources vs. energy). The Commission agreed, stating that it would not expect all resources modeled in the DPT to be suitable for a long-term capacity purchase such as the one in the previous case.