UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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

ORAL STATEMENT OF DIANA L. MOSS
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AMERICAN ANTITRUST INSTITUTE
MARCH 8, 2007

Thank you very much for inviting me here today to share the American Antitrust Institute's (AAI's) views at this technical conference on the Commission's merger policy. As you may know, the AAI is a non-profit, Washington D.C.-based education, research, and advocacy organization. Our mission is to increase the role of competition, assure that competition works in the interests of consumers, and challenge abuses of concentrated economic power in the American and world economies.

Merger policy is a key component of broader competition policy because industry consolidation directly affects the competitive landscape of any industry. Merger policy is particularly important in electricity for two major reasons. One is that consolidation in restructuring industries occurs against the backdrop of changing market institutions and dynamics. These factors can alter key strategic competitive variables such as how, where, and when firms invest in transmission and generation infrastructure and how they conduct themselves in the marketplace. Merger review in this environment is a challenge, so it is particularly important to ensure proper scrutiny of a merger's effect on competition in applying the Commission's public interest standard.

A second reason why merger policy is important in electricity is that mergers are subject to multiple review by numerous state and federal regulatory and antitrust agencies. The full force of such multi-agency review will be felt more in an era of mergers such as Exelon/PSEG and Duke/Cinergy that leave a large horizontal and/or vertical footprint. But relatively limited coordination between agencies increases the possibility of different analytical outcomes and remedies--all of which raise uncertainty and costs and detract from the predictability and transparency of governmental decision-making.

My comments on this panel today pertain largely to the interplay between federal antitrust and regulatory merger review of the competitive effects of electricity mergers. I will discuss some of the key issues that multi-agency review raises and what options the Commission might consider to promote harmonization. Before that, though, I would like to give you some quick statistics on the last decade of merger activity in the electricity industry.

From 1992 to 2006, about 100 mergers involving electric utilities were proposed in the U.S. Two-thirds of these deals were electric-electric combinations and one-third were electric-gas combinations. About 80 of these transactions have been subject to the Commission's jurisdiction under Section 203. In 9 percent of mergers that were consummated, the antitrust agencies imposed remedies to address competitive concerns. This percentage is far higher than the average for all industries. The Commission either accepted remedies proposed by applicants or imposed additional remedies in 6 percent of cases.

Let me now focus on a few of the major differences between antitrust and regulatory merger review that I think have important and useful implications for the Commission. First is the fact that while the *Merger Policy Statement (Policy Statement)* officially adopted the Department of Justice/Federal Trade Commission *Horizontal Merger Guidelines (Guidelines)*, Appendix A of the *Policy Statement* focuses primarily on a small part of the *Guidelines* framework. As you know, the *Guidelines* framework includes: (1) relevant product and geographic market definition, (2) evaluation of market concentration, (3) competitive effects or the particular theory(ies) of competitive harm, (2) the ease of entry, and (5) merger-related efficiencies.

Appendix A takes up the first two steps—defining relevant markets and determining if a merger exceeds the thresholds for increases in market concentration. If it does, applicants are encouraged to propose remedies, the implication being that the Commission gives great weight to market definition and concentration, but relatively less weight to theories of competitive harm, entry, and efficiencies. This is not all bad—defining the product and geographic boundaries of relevant markets is perhaps the most difficult and controversial aspect of electricity merger analysis. But market concentration is really just a screen. The full story of a merger's effect on competition (good or bad) is told by the totality of the *Guidelines* factors.

For example, theories of competitive harm, or the "market power story," can include unilateral effects, such as a dominant firm withholding capacity to drive up price. They also include coordinated effects, such as rivals in tight oligopoly markets tacitly colluding on price and/or quantity. The role of entry—either generation or transmission—in electricity markets affected by a merger bears materially on whether potential postmerger price increases will be disciplined by new entrants. Merger-related and cognizable efficiencies such as scale, scope, and coordination economies are also important to consider in the balance of the other *Guidelines* factors.

Much of the Commission's focus on market definition is driven by the requirement that an applicant's analysis rely on publicly available data. And while publicly available data is "serviceable" for this purpose, it provides little or no support for developing theories of harm or examining entry and efficiencies. The antitrust agencies, which obtain confidential data and information from numerous market participants under a Civil Investigative Demand are better able to address all of the *Guidelines* factors. Not giving due consideration to all the *Guidelines* factors increases the possibility of incomplete analysis, outcomes that differ from those that might emerge from an antitrust review, and less transparent and predictable Commission decision-making.

While there are no quick fixes for resolving the source of this tension between antitrust and regulatory merger review, the Commission might want to consider two things. One is to promote more frequent periodic inter-agency meetings between FERC, DOJ, the FTC, and other agencies in order to discuss these issues. A second is that the Commission can issue supplemental data requests to collect additional information that would allow it to better consider all the *Guidelines* factors, particularly in complex and controversial cases.

A second major issue that emerges from differences between antitrust and regulatory merger review is how economic analysis is handled. The antitrust agencies perform their own independent, in-house analysis of a merger's effect on competition while the Commission relies on applicant-filed analysis. This lack of internal analytical corroboration at the Commission introduces at least one significant problem.

For example, as part of a study I recently completed for the AAI, I examined applicant-filed analyses from merger filings over the period 1997 to 2004 and found that in a number of merger cases, several of the same relevant product and geographic markets were analyzed. However, the level of concentration in any given market differed widely from filing to filing, sometimes by several orders of magnitude. This type of variation is not easily explained by legitimate changes in market conditions, generation entry, or even expanding market boundaries due to RTOs. It can only be explained by variations in modeling, data, and assumptions used by the economic experts that performed the competitive analysis on behalf of the merger applicants.

This type of inconsistency in applicant-filed analysis should be of grave concern to the Commission, particularly if it is relying on applicant-filed analysis in rendering its merger decisions. It introduces analytical error into the Commission's decision-making process, which could lead to erroneous outcomes. It also decreases the predictability and consistency of decision-making and provides no objective metric for assessing how the structures of various regional electricity markets are changing over time.

The AAI suggests respectfully that an appropriate fix for this problem is for the Commission to develop its own in-house model for the purposes of corroborating applicants' analyses. Alternatively, it could perform the analysis with its own model using applicant-provided data. This would allow the Commission to detect any bias in the analysis, vet important analytical and data issues, and perform the types of sensitivity analysis that it deems important. Here, the Commission should consider the use of both structural market models and simulation models that may be better suited for evaluating price and output outcomes under different scenarios regarding firm interaction.

Finally, I would briefly like to address a third difference between antitrust and regulatory merger review. The antitrust agencies, as you know, generally favor structural remedies such as divestiture to address competitive problems raises by mergers. Divestiture is a one-time fix and permanently reduces or eliminates either the ability or incentive to adversely affect prices or output through the exercise of market power. The antitrust agencies have devoted significant thought and resources into the structuring of effective merger remedies over the last two decades—enough to justify two policy statements or guidelines--one each from the FTC and the DOJ.

FERC, on the other hand, has traditionally favored conduct-based remedies such as RTO commitments, virtual divestiture, and market monitoring. A conduct-based approach may be inherently more comfortable for the Commission but it requires ongoing monitoring and enforcement for all involved parties. Here, the concern is that under a system of multi-agency merger review, remedies imposed in different jurisdictions can potentially conflict or be duplicative, thus imposing unnecessary, additional costs. As mergers become larger and multi-agency review more pronounced, we would expect this issue to become more pronounced.

The Commission may thus want to consider structural remedies (as opposed to behavioral fixes) for addressing competitive problems. Where the Commission feels it is limited in its ability to impose structural remedies, AAI encourages cooperative efforts with states and the antirust agencies that are in a better position go the structural route.

Developing some informal inter-agency guidelines on coordinating (or minimizing any friction between) merger remedies might also be worthwhile.

In sum, I would like to note that despite the very different standards of review, information gathering procedures, and institutional preferences that surround various aspects of merger review in the complex multi-agency world we live in, much can still be done to promote coordination and harmonization across agencies. These efforts will promote consistency, predictability, and credibility of decision-making and further the goal of promoting competitive electricity markets. Thank you for the opportunity to offer comments today and I look forward to any questions.