

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Implementation of Amended)
Section 203(a)(1)(B) of the) Docket No. RM19-4-000
Federal Power Act)

**COMMENTS OF
THE AMERICAN ANTITRUST INSTITUTE**

The American Antitrust Institute (AAI) submits these comments in response to the Notice of Proposed Rulemaking (NOPR) issued by the Federal Energy Regulatory Commission (Commission or FERC) on November 15, 2018 in the above-captioned docket.¹ The NOPR proposes to amend the Commission’s regulations to implement *An Act to Amend Section 203 of the Federal Power Act* (Act).² The Act makes three changes to Section 203 of the Federal Power Act (FPA). First, it specifies a \$10 million minimum value threshold for transactions (mergers and acquisitions) that must receive Commission approval under section 203(a)(1)(B). Second, the Act adds new section 203(a)(7) that requires the Commission to implement a notification requirement for transactions if the value of the acquisition is greater than \$1 million and the transaction is not otherwise subject to review under section 203(a)(1)(B).³ And third, it instructs the Commission to submit a report to Congress that assesses the effects of creating the \$10 million threshold.

These comments urge the Commission to expand on its proposed notification requirements under section 203(a)(7) for transactions that fall between \$1-10 million in value. As discussed below, there are a number of reasons why expanded notification requirements for such “small” transactions will facilitate the Commission’s collection of data and information that is necessary for the agency to

¹ *Implementation of Amended Section 203(a)(1)(B) of the Federal Power Act*, 165 FERC ¶ 61,091 (2015), 83 Fed. Reg. 61,338 (Nov. 29, 2018) (“NOPR” or “Proposed Rule”).

² Pub. L. 115-247, 132 Stat. 3152, enacted by Congress on September 28, 2018.

³ Such transactions are defined by the Act as those in which a public utility “is seeking to merge or consolidate, directly or indirectly, its facilities subject to the jurisdiction of the Commission, or any part thereof, with those of any other person,” *See* Act at § 2 (adding 16 U.S.C. § 824b(a)(7)(A)).

monitor and evaluate changes in wholesale power markets that may result from small transactions that are exempt from its review. The AAI also suggests that a number of pending Commission rulemakings that address various key aspects of competition in wholesale power markets be given particularly careful attention.

I. INTEREST OF THE AMERICAN ANTITRUST INSTITUTE

The AAI is an independent, nonprofit organization. The AAI's mission is to promote competition that protects consumers, businesses, and society. We serve the public through education, research, and advocacy on the benefits of competition and the use of antitrust enforcement as a vital component of competition policy. The AAI has provided legal and economic analysis, commentary, and testimony on mergers, market design, energy policy, and competition policy involving the energy industries since the organization's founding in 1998.

II. PROPOSED NOTIFICATION REQUIREMENTS FOR TRANSACTIONS BETWEEN \$1-10 MILLION IN VALUE

The NOPR proposes to add section 33.12 to the Commission's regulations to implement the notification requirement mandated by section 203(a)(7) of the FPA. For transactions subject to the new requirement, the notification requirement would include:

(1) The exact name of the public utility and its principal business address; and (2) a narrative description of the transaction, including the identity of all parties involved in the transaction and all jurisdictional facilities associated with or affected by the transaction, the location of such jurisdictional facilities involved in the transaction, the date on which the transaction was consummated, the consideration for the transaction, and the effect of the transaction on the ownership and control of such jurisdictional facilities.⁴

III. COMMENTS

The Commission's proposed requirements provide a basic framework for collecting data and information that is vital for monitoring changes in wholesale electricity markets resulting from small transactions valued between \$1-10 million that are exempt from review. The AAI's comments draw

⁴ NOPR at 5 and proposed 18 C.F.R. § 33.12(b).

attention to the fact that even small transactions that fall under the \$10 million minimum reporting threshold can raise a number of concerns, as discussed below. These can have material effects on and implications for competition and consumers in wholesale electricity markets. Given the Commission's statutory obligation to protect competition and consumers, and the requirement that it prepare a report to Congress that addresses the effects of excluding such transactions from Commission review, the agency should be collecting information to assess the potential adverse competitive effects of such transactions.

A. A Succession of Small Horizontal or Vertical Acquisitions Can Result in the Accretion of Market Power Over Time (“Accretive” Transactions)

A series of exempt small acquisitions by a single company can, over time, result in a seller or buyer with significant market power. Entities that engage in serial small acquisitions to strategically build portfolios of assets can increase their market power in wholesale markets and enhance their ability and incentive to exercise it. Broader economy-wide concerns about declining competition and high concentration raise a number of questions. One is the role of antitrust enforcers (U.S. Department of Justice and Federal Trade Commission) in allowing series of successive, smaller mergers and acquisitions in key markets such as telecommunications, pharmaceuticals, energy, and agriculture).⁵ Over time, serial transactions created significantly larger entities, higher market concentration, and even evidence of consumer harm.⁶

In wholesale electricity markets, serial small transactions include horizontal combinations of electricity generation assets. They also include vertical combinations of generation and fuel (e.g., natural gas) transportation, and generation and transmission assets. As the Commission knows, the

⁵ See, e.g., American Antitrust Institute, *A National Competition Policy: Unpacking the Problem of Declining Competition and Setting Priorities Moving Forward*, Sept. 28, 2016, <https://www.antitrustinstitute.org/work-product/national-competition-policy/>. See also Council of Economic Advisers, *Benefits of Competition and Indicators of Market Power*, THE WHITE HOUSE at 4 (Apr. 2016), https://www.whitehouse.gov/sites/default/files/page/files/20160414_cea_competition_issue_brief.pdf.

⁶ See, e.g., John Kwoka, *The Structural Presumption and the Safe Harbor in Merger Review: False Positives or Unwarranted Concerns*, 81 ANTITRUST L.J. 837 (2017), at 875-865.

exercise of market power through the ability to control price or to exclude rivals – by firms acting unilaterally (i.e., alone) or in coordination with others (i.e., collusively) – is highly detrimental to competition and consumers.

For example, a utility that serially acquires smaller generation assets to build a larger portfolio over time may enhance its ability and incentive to engage in unilateral economic or physical capacity withholding. As has occurred on numerous occasions in U.S. wholesale electricity markets, such schemes result in harmful, supra-competitive wholesale and retail electricity prices and potentially jeopardize the reliability of the electricity grid.⁷ Likewise, a vertically integrated generator may enhance its ability and/or incentive through successive small transactions to strategically operate its transmission or fuel transportation assets to frustrate rivals' access to or foreclose them entirely from wholesale markets.

Successive small transactions that create larger horizontal and vertical portfolios of assets over time -- and the associated accretion of horizontal or vertical market power -- should be monitored carefully by the Commission. The AAI urges the Commission to give particular scrutiny to acquisitions of small assets by market participants with large market shares. The accretion of market power by such “dominant” firms can significantly exacerbate competitive problems and deserves careful monitoring by the Commission. The notification requirements proposed in the NOPR are a critical mechanism for collecting data and information and performing analysis of how small transactions affect shares, concentration, and competitive incentives in wholesale electricity markets over time.

⁷ See e.g., American Antitrust Institute Letter to U.S. Department of Justice, Antitrust Division, Assistant Attorney General William Baer and Federal Trade Commission Chairwoman Edith Ramirez, *Antitrust Tools for Challenging Capacity Withholding in Wholesale Electricity Markets*, Jul. 22, 2014, https://www.antitrustinstitute.org/wp-content/uploads/2014/07/AAI-on-Capacity-Withholding_final.pdf.

B. Acquisitions of Small Partial Ownership Shares in Strategic Assets Can Raise Competitive Concerns Due to Common and Cross-Ownership Issues (“Partial Ownership” Transactions)

The acquisition of a partial ownership interest in an asset may result in anticompetitive effects even when the acquisition would be exempt from Commission review under the new threshold. Cross-ownership involves rivals who have partial ownership shares *in each* other, while common ownership involves rivals who have shareholders or investors *in common*.⁸ These types of arrangements raise a host of competitive issues when assets compete in the same markets and when owners may have strong incentives to strategically affect competition.

Competitive issues associated with cross- and common ownership has been the subject of intensifying scrutiny by the U.S. antitrust agencies and the Commission.⁹ Indeed, the Commission’s 2010 rulemaking *Control and Affiliation for Purposes of the Commission’s Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act* (Docket. No. PL09-3-000) addressed these issues in the energy industries.¹⁰ Partial ownership of competing assets by investors such as private equity firms can adversely affect competition through unilateral and coordinated effects, as explain by the AAI in its comments to the Commission in PL09-3-000.¹¹

⁸ See, e.g., Jose Azar, Martin Schmalz, and Isabel Tecu, *Anticompetitive Effects of Common Ownership*, JOURNAL OF FINANCE, 73(4) (2018), <https://ssrn.com/abstract=2427345>. See also Einer Elhauge, *Horizontal Shareholding*, 129 HARVARD L.R. 1267 (2016), and Steven C. Salop and Daniel P. O’Brien, *Competitive Effects of Partial Ownership: Financial Interest and Corporate Control*, 67 Antitrust L.J. 559-614 (2000).

⁹ See e.g., Federal Trade Commission, In the Matter of TC Group, LLC, Riverstone Holdings LLC, Carlyle/Riverstone Global Energy and Power Fund II, LP, and Carlyle/Riverstone Global Energy and Power Fund III, LP (Complaint), Docket No. C-4183 (Jan. 24, 2007) and (Decision and Order) (Jan. 25, 2007). Available <http://www.ftc.gov/os/caselist/0610197/complaint.pdf>. See also United States v. Dairy Farmers of America, Competitive Impact Statement, Civil Action No.: 6:03-206-KSF (E.D. Ky. October 2, 2006). Available <http://www.usdoj.gov/atr/cases/f221700/221713.htm>. See also United States v. Dairy Farmers of Am., Inc., 426 F.3d 850 (6th Cir. 2005).

¹⁰ *Control and Affiliation for Purposes of Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act*, 130 FERC ¶ 61,046 (2010).

¹¹ Comments of the American Antitrust Institute in *Control and Affiliation for Purposes of Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act*, 130 FERC ¶ 61,046 (2010), Jan. 16, 2009, https://www.antitrustinstitute.org/wp-content/uploads/2018/08/aaicrossownershipcomments_012020091152.pdf.

For example, under some circumstances a private equity firm can control or influence managerial decision-making, even with a partial and minority ownership share in an asset. Such control or influence may be obtained with an investment of less of \$10 million. For example, a \$9 million investment in a partial ownership share of a \$27 million asset constitutes a substantial share (30%) of the total value of the asset but *would not* be reviewable by the Commission. A \$100 million investment in a partial ownership share of a \$300 million asset also comprises a 30% share but *would* be reviewable by the Commission. This comparison reveals the difficulty inherent in the selection of dollar “thresholds” for purposes of the Commission’s authority to review transactions under Section 203.

Cross ownership that results in rivals’ ownership of each other can facilitate the anticompetitive exchange of information that could have deleterious effects on competition and consumers. And common-ownership of rivals can dampen incentives to compete because more vigorous competition is less profitable than “cooperation” for investors with partial shares in each of those rivals.¹² Such anticompetitive cross- and common ownership problems could be induced by transactions below the \$10 million threshold.

Private equity investors are active in electricity markets. As early as the mid 1990s, private equity investors purchased small, partial shares of electric utilities with FERC jurisdictional assets.¹³ In the mid-2000s, there was a surge of private equity investment in regulated electric utilities.¹⁴ And as recently as 2016, private equity investors have been described as the “go to” buyers for power plants.¹⁵ There are now over 60 private equity firms that are active in the U.S. electricity industry.¹⁶

¹² Elhauge, *supra* note 8.

¹³ Joseph Diamond and Jon D. Edwards, *Mergers, Acquisitions and Market Power in the Electric Power Industry* (Apr. 4, 1997), <https://www.energy.ca.gov/papers/CEC-999-1996-005.PDF>, at 4.

¹⁴ *Private Equity Firms Discover Electricity — and Lead the Charge for Energy Investment* (Apr. 26, 2007), <http://knowledge.wharton.upenn.edu/article/private-equity-firms-discover-electricity-and-lead-the-charge-for-energy-investment/>.

¹⁵ Peter Maloney, *With AEP deal, private equity continues gobbling up utility plants* (Sep. 20, 2016), <https://www.utilitydive.com/news/with-aep-deal-private-equity-continues-gobbling-up-utility-plants/426486/>.

Small partial ownership shares of FERC jurisdictional assets can result in complex ownership structures and create the ability and incentive to exercise market power in wholesale electricity markets. The Commission should therefore monitor them carefully.

C. The Unique Nature of Electricity Markets Can Make Even Small Acquisitions Strategically Advantageous (“Strategic Acquisitions”)

Electricity markets are particularly susceptible to the exercise of market power, including capacity withholding as a strategy to drive up price.¹⁷ Electricity markets are conducive to withholding for a number of reasons. One is the relative inelasticity of demand for electricity. The more insensitive consumption is to changes in price, the greater is the price increase if a seller withholds capacity. A lack of demand-side bidding in some organized wholesale markets limits the ability of demand to discipline price increases. In addition, some retail rate structures mask the effects of high electricity prices, reducing consumers’ incentives to cut back on consumption at times when wholesale prices are high.

Another key factor that makes wholesale electricity markets susceptible to the exercise of market power is supply inelasticity during times when capacity is constrained. This contributes to supra-competitive prices that result from withholding, since higher-cost resources must be dispatched if marginal or infra-marginal resources are withheld. When supply is tight, a seller can therefore produce a significant price increase by withdrawing just a small amount of capacity and profit from it if it owns even a small amount of infra-marginal generation.

A firm’s incentive to withhold output may not require a large share of the market or a large asset. An effective withholding strategy could involve a relatively small market share or generator

¹⁶ Axial, Middle Market Review: Electric Utilities Private Equity Firms, <https://www.axial.net/forum/companies/electric-utilities-private-equity-firms/1/>.

¹⁷ *Supra* note 7. See also Diana L. Moss, *Electricity and Market Power: Current Issues for Restructuring Markets (A Survey)*, 1 ENVTL. & ENERGY L. & POLY J. 11 (2006). See also John Kwoka and Vladlena Sabodash, *Price Spikes in Energy Markets: “Business by Usual Methods” or Strategic Withholding?*, 38 REV. IND. ORGAN. 285 (2011).

that, if withheld in a geographic/product market, could produce a significant price increase.¹⁸ Thus, even relatively small transactions involving strategic generation assets can create competitive concerns. The same is true of using strategic transmission assets to congest transmission networks in order to foreclose rivals and raise prices. Even a relatively small transmission facility could have strategic value to vertically integrated utility. In light of the foregoing, acquisitions of small but strategic generation and transmission assets should be monitored carefully by the Commission.

IV. FERC SHOULD EXPAND ON PROPOSED NOTIFICATION REQUIREMENTS TO ENSURE THAT UNREVIEWABLE, SMALL TRANSACTIONS DO NOT CREATE OR EXACERBATE COMPETITIVE PROBLEMS, CONVENE A TECHNICAL CONFERENCE, AND REVISIT KEY RULEMAKINGS

The AAI's comments describe three major areas of competitive concern associated with small transactions that are now not reviewable under the Commission's Section 203 authority. For those transactions falling between \$1-10 million in value, the Commission has proposed notification requirements, as described in Section III above. Those requirements include: (1) a description of the transaction, (2) identity of all parties involved, (3) identity of all jurisdictional facilities associated with or affected by the transaction, (4) location of jurisdictional facilities associated with or affected by the transaction, (5) date of consummation of the transaction, and (6) the effect of the transaction on the ownership and control of such jurisdictional facilities.¹⁹

The AAI agrees that the foregoing is important information to collect under the new 18 C.F.R. § 33.12(b)(2) regulations. However, we suggest that additional notification requirements are necessary for Commission to be able to assess and analyze the changes in market shares, market concentration, firm organizational structures, and asset ownership and control that bear materially on competitive incentives and outcomes in wholesale electricity markets. Such expanded notification requirements would allow the Commission to assess whether small transactions raise the

¹⁸ Moss and AAI, *supra* note 18.

¹⁹ NOPR at P 5 & proposed 18 C.F.R. § 33.12(b).

competitive concerns described in Section III above.

The AAI suggests that three additional notification requirements are important to include in the Commission's regulations under 18 C.F.R. § 33.12(b)(2).

- (1) identity of the wholesale markets in which the jurisdictional facilities associated with or affected by the transaction participate, including all applicable RTO markets and identifiable markets outside RTOs.
- (2) A current, 10-year history of changes in ownership involving the jurisdictional facilities associated with the transaction.
- (3) The identity of all energy affiliates and energy subsidiaries owned by the acquirer of the jurisdictional facilities that are the subject of the transaction.

The AAI also encourages the Commission to undertake a technical conference to explore the types of analysis the Commission will perform, utilizing the data and information provided in the new notification requirements, to effectively monitor changes in wholesale electricity markets resulting from small, unreviewable transactions. The report that the Commission is required to produce within two years "that assesses the effects of the amendment" to FPA section 203(a)(1)(B)²⁰ should set forth this methodology and the results of the Commission's analyses for wholesale electricity markets across the United States.

The implications of the Act and proposed new Commission regulations to comply with the statutory change cannot be understated. Because certain transactions will no longer be reviewable by the Commission, it will be vital for the agency to monitor such transactions and seek to ensure that small accretive, partial ownership, and strategic transactions do not impair competition in wholesale power markets and harm consumers. In addition to the expanded notification requirements proposed above, the AAI also suggests that the Commission give careful attention to a number of

²⁰ Act at § 4.

outstanding rulemakings and consider the effects of the revised regulations for small transactions on the questions posed in those NOPRs.

For example, the Commission recently issued the NOPR *Refinements to Horizontal Market Power Analysis for Sellers in Certain Regional Transmission Organization and Independent System Operator Markets* (RM19-2-000).²¹ The exclusion of small transactions from section 203(a)(1)(B) militates in favor of the Commission maintaining close oversight of the workings of RTO markets and not relieving sellers with market based rate authority of their obligation to file competitive analysis with the Commission. The AAI also notes that the Commission's NOPR *Certification of New Interstate Natural Gas Facilities* (PL18-1-000) addresses certification of natural gas transportation facilities.²² As the AAI explained in its comments, the granting of a certificate on the basis of affiliate precedent contracts poses potentially serious competitive concerns. Such transactions could be exempt under the new rules.²³

Finally, the AAI notes that the Commission has not yet acted on two critical rulemakings: *Data Collection for Analytics and Surveillance and Market-Based Rate Purposes* (RM16-17-000) and *Modifications to Commission Requirements for Review of Transactions under Section 203 of the Federal Power Act and Market-Based Rate Applications under Section 205 of the Federal Power Act* (RM16-21-000).²⁴ Both of these NOPRs address key issues relating to the effects of the Act and associated Commission regulations.²⁵ The AAI encourages the Commission to make these rulemakings high priority and to

²¹ *Refinements to Horizontal Market Power Analysis for Sellers in Certain Regional Transmission Organization and Independent System Operator Markets*, 165 FERC ¶ 61,268 (2018).

²² *Certification of New Interstate Natural Gas Facilities*, 163 FERC ¶ 61,042 (2018).

²³ Comments of the American Antitrust Institute in *Certification of New Interstate Natural Gas Facilities*, 163 FERC ¶ 61,042 (2018), Jul. 25, 2018, https://www.antitrustinstitute.org/wp-content/uploads/2018/09/FERC_NOI-Natural-Gas-Certification_AAI-Comments_7.25.18.pdf

²⁴ *Modifications to Commission Requirements for Review of Transactions under Section 203 of the Federal Power Act and Market-Based Rate Applications under Section 205 of the Federal Power Act*, 156 FERC ¶ 61,214 (2016).

²⁵ See Comments of the American Antitrust Institute, *Modifications to Commission Requirements for Review of Transactions under Section 203 of the Federal Power Act and Market-Based Rate Applications under Section 205 of the Federal Power Act*, 156 FERC ¶ 61,214 (2016), Nov. 28, 2016, <https://www.antitrustinstitute.org/work-product/aai-comments-on-the-fercs-notice-of-inquiry-on-competition-analysis-for-electricity-mergers-and-market-based-rate-authority/>.

consider how the issues and questions posed therein relate fundamentally to the competitive issues posed by small transactions that are now exempt from Commission scrutiny. These NOPRs provide a unique opportunity for the Commission to use its other authorities pertaining to promoting competition in wholesale power markets as a backstop for lost Section 203 review authority.

V. CONCLUSION

AAI respectfully asks that the Commission consider and incorporate the suggestions contained herein in the reporting requirements under FPA section 203(a)(7).

Respectfully submitted,

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