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FERC Decides to Retain Existing Merger Review Policies

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On February 16, 2012, FERC issued an order (***February 16 Order***) reaffirming its existing merger review policies under Section 203 of the Federal Power Act (FPA) and its current framework for analyzing requests for market-based rate authority under section 205 of the FPA. In March of last year, FERC had sought comment in a ***Notice of Inquiry*** (NOI) on whether it should amend its existing policies in these two areas in light of new ***Horizontal Merger Guidelines*** (2010 HMG) issued jointly by the Federal Trade Commission (FTC) and Department of Justice (DOJ) on August 19, 2010. The NOI explained that the 2010 HMG deemphasize market definition as a starting point for merger analysis and depart from the sequential analysis found in the prior 1992 version of the Horizontal Merger Guidelines (1992 HMG), and instead support the use of a fact-specific inquiry and greater analytical flexibility. Section 203 of the FPA requires parties to public utility mergers and acquisitions involving jurisdictional facilities to seek FERC authorization before closing. Section 203(a) provides that FERC should approve such transactions if they are consistent with the public interest. As part of that determination, FERC must consider the proposed transaction's effect on competition in the relevant market(s). FERC currently uses a five-step framework that was adopted from the 1992 HMG, as well as a Competitive Analysis Screen (CAS) which focuses on the first step of the analysis: whether the proposed transaction would significantly increase concentration and result in a concentrated market. One component of the CAS includes an analysis of market concentration using the Herfindahl-Hirschman Index (HHI). Under Section 205 of the FPA, parties that can demonstrate they do not have, or have adequately mitigated, their horizontal and vertical market power are granted authority to make sales of electric energy, capacity and ancillary services at market-based rates. FERC's analysis under Section 205 includes the use of two indicative screens that rely on market share as well as market concentration as measured by HHI. In its February 16 Order, FERC declined to follow the 2010 HMG's approach as the framework for the Commission's analysis of horizontal market power. The Commission explained that it would retain its five-step framework, including the CAS as part of its first step, as the CAS provides a useful conservative check to allow parties to quickly identify mergers unlikely to present competitive problems at a relatively low cost. The Commission stated that its current approach, which provides analytical and procedural certainty, is also flexible enough to incorporate theories outlined in the 2010 HMG, and that it has previously, and will continue to, look beyond the HHI screens in its review process when warranted. The Commission also declined to adopt the revised, higher HHI thresholds presented in the 2010 HMG for use in its CAS. Noting its extensive experience with electrical markets and their distinct characteristics, as well as its intent to use the CAS to identify proposed transactions that clearly would have no adverse effect on competition, FERC stated that its current HHI thresholds are appropriate. The Commission also declined to initiate a more formal coordination process with the FTC and DOJ, as requested by one commenter. FERC stated that it will continue to coordinate with the federal antitrust agencies as appropriate, on a case-by-case basis. Regarding its electric market-based rate program, FERC decided not to modify the current market power analysis and declined to alter the HHI threshold used in that screening process, noting that its current HHI threshold is already consistent with the 2010 HMG approach. With regard to the existing market share screen, FERC explained that, due to the physical and economic characteristics of electricity markets, including low elasticity of demand, market power is more likely to be present at lower market shares. Thus, FERC concluded that the current indicative screens used in its market-based rate analysis provide an appropriate balance between a "conservative but realistic screen" and imposing undue burdens on applicants. FERC also noted that its current analysis provides adequate flexibility to consider additional evidence when raised by an applicant or an intervenor.