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THE CHANGING FOCUS OF ELECTRIC UTILITY MERGER PROCEEDINGS

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I. INTRODUCTION

The Federal Energy Regulatory Commission's (FERC or Commission) review of electric utility mergers has undergone a sea of change in recent years. Lengthy hearings on market shares have been replaced by open access transmission tariffs. Cross-examination on operating costs and rates has been replaced by commitments to hold customers harmless. An approval process that in some instances took two years or more can now be completed in eight months.

That is the good news. There remain, however, many repairs to the FERC's section 203 ship that can be made and certain obsolete parts that can be removed. In particular, the FERC's six-prong "*Commonwealth*"¹ test has atrophied so significantly that several of the factors appear to no longer require regular application. Even as to the remaining factors, some closer attention is appropriate. For example, in some cases the FERC has considered the issue of a merger's impact on retail rates, but in others it has specifically declined to do so. The issue implicates important federalism considerations, and the FERC should, at the very least, clarify its policy on this issue. Further, while the issue of a merger's effect on competition is enjoying a well-deserved rest, it will not likely last long, as the industry continues to restructure. A few observations are offered on competitive issues that may provoke controversy in the future.

Another area ripe for examination is the scope of the FERC's jurisdiction under Federal Power Act (FPA) section 203.² For instance, proposed

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1. *Commonwealth Edison Co.*, 36 F.P.C. 927 (1966), *aff'd sub nom.*, *Utility Users League v. FPC*, 394 F.2d 16 (7th Cir. 1968), *cert. denied*, 393 U.S. 953 (1968).

2. 16 U.S.C. § 824j (1988).

acquisitions that are hostile in nature may push the bounds of existing case law and cause the FERC to articulate precisely when a "transfer of control" requiring its prior approval occurs—e.g., whether replacing a utility's board of directors through a proxy contest or purchasing 50 percent or less of a utility's voting securities constitutes a "transfer of control?" Other jurisdictional issues are more heavily traveled, but remain unsettled. For example, many decry the *Missouri Basin*³ "gap" in jurisdiction as eviscerating federal review of important issues. It is argued here, however, that the FERC's residual authority over wholesale rates and transmission access will provide it enough jurisdiction to protect the public interest on an ongoing basis in most cases, even if it lacks jurisdiction over a particular merger.

Finally, there is the FERC's procedural model. In recent years, the FERC has come a long way in rationalizing the process by which it considers a section 203 application, but improvements still can be made. In general, the current model lacks imagination because the choice between summary disposition and a trial-type hearing is too limiting. There are other well-established procedural options (such as "paper" hearings and alternative dispute resolution methods) that may better suit particular section 203 issues.

II. RECENT DEVELOPMENTS

Three recent section 203 proceedings merit brief, but particularized attention.

A. *Northeast Utilities / Public Service Co. of New Hampshire*⁴

Northeast Utilities' (NU) proposed acquisition of Public Service Co. of New Hampshire (PSNH) sought to bring PSNH out of bankruptcy and thereby complete the first major electric utility bankruptcy reorganization since the Great Depression.⁵ While popular in New Hampshire and Connecticut, the proposed merger was opposed by virtually every other constituency within New England.⁶ At the FERC, two issues dwarfed all others.

First, NU and PSNH elected "single participant status" within the New England Power Pool (NEPOOL)⁷ and thereby sought to achieve \$364 mil-

3. *Missouri Basin Mun. Power Agency v. Midwest Energy Co.*, 53 F.E.R.C. ¶ 61,368 (1990), *reh'g denied*, 55 F.E.R.C. ¶ 61,464 (1991).

4. *Northeast Util. Serv. Co. Re Pub. Serv. Co. of N.H. (NU/PSNH)*, 53 F.E.R.C. ¶ 63,020 (1990), 56 F.E.R.C. ¶ 61,269 (1992), *reh'g*, 58 F.E.R.C. ¶ 61,070 (1992), *reh'g*, 59 F.E.R.C. ¶ 61,042 (1992), *on petition for review*, *Northeast Util. Serv. Co. v. FERC*, 993 F.2d 937 (1st Cir. 1993).

5. See *In re Public Serv. Co. of N.H.*, 963 F.2d 469 (1st Cir. 1992), *cert. denied*, *Rochman v. Northeast Util. Serv. Co.*, 113 S. Ct. 304 (1992).

6. The proposed merger was opposed by the state commissions from Massachusetts, Vermont, Rhode Island and Maine and by virtually every investor-owned and public power utility in New England. Certain investor-owned utilities, such as New England Power Co., United Illuminating, Inc., and a group of eighteen Vermont utilities, opposed the merger initially, but later settled with NU.

7. As explained by the FERC, "NEPOOL operates all of its members' electric facilities as a single system and provides for coordinated regional planning of generation and transmission facilities." *NU/PSNH*, 56 F.E.R.C. ¶ 61,269, at 61,985. More specifically, "[t]he New England Power Exchange (NEPEX) uses economic dispatch, operating all of the NEPOOL members' generation and

lion in savings due to combining their “capability responsibility”⁸ and “own load” dispatch within the Pool.⁹ However, because neither NEPOOL’s overall “objective capability,” nor its economic dispatch changed, every dollar “saved” by NU/PSNH was a dollar “shifted” from the rest of the Pool.¹⁰ Despite complaints that this resulted in an unfair and “massive cost shift,”¹¹ the FERC recognized NU and PSNH as single participants within NEPOOL¹² and thereby preserved \$364 million in savings used to finance the PSNH reorganization plan.¹³

The second major issue was the merger’s effect on competition. To its opponents, the merger created a “transmission curtain” around eastern Massachusetts and Rhode Island, separating it from the rest of New England.¹⁴ It was alleged that generation-hungry Boston consumers would have to rely almost exclusively on NU’s surplus capacity.

The FERC essentially agreed and found the merger anticompetitive. As a remedy, the Commission (1) required NU to file an open access transmission tariff;¹⁵ (2) eliminated NU’s proposal to maintain priority use of its

transmission systems to maximize the use of the least expensive resources to meet the demand with the pool, while maintaining appropriate standards of reliability.” *Id.*

8. NU and PSNH had a diverse peak load, PSNH being a winter peaking utility and NU being a summer peaking utility. *Northeast Util.*, 993 F.2d at 948.

9. With respect to energy transactions, “NEPOOL’s actual dispatch of a participant’s resources is compared, after the fact, to a simulated ‘own load’ dispatch of that participant’s system to meet its load as if it were not part of NEPOOL” and the “difference between this actual and simulated dispatch is used to calculate the level of fuels savings from NEPOOL’s centralized dispatch,” with the savings then allocated among the Pool’s members based on contribution of generation resources. *NU/PSNH*, 56 F.E.R.C. at 61,985-86. As to responsibility for generating capacity, NEPOOL calculates a participant’s share of generating resources that it must contribute to NEPOOL’s “Objective Capability” and then “assesses charges (Adjustment and Deficiency Charges) to the participants lacking adequate capacity to meet their Capability Responsibility obligations.” *Id.* at 61,986.

10. The intervenors argued “that these savings for the merged company will effectively come from the pockets of all other NEPOOL members.” *NU/PSNH*, 63 F.E.R.C. ¶ 63,020, at 65,213 (1990). The Court responded, holding “that because the cost shift amounted to a zero-sum transaction, with NU and PSNH benefitting and the other members burdened dollar-for-dollar, the shift could not be counted as a benefit of the merger.” *Northeast Util.*, 993 F.2d at 950.

11. 58 F.E.R.C. at 61,188.

12. The Commission relied principally on the testimony of one of the Agreement’s drafters, who testified that the NEPOOL Agreement’s drafters had contemplated allowing such a cost shift. At the time the NEPOOL Agreement was drafted, a merger of New England Power Co., Boston Edison Co., and Eastern Utilities Associates was under consideration. 58 F.E.R.C. at 61,189.

13. 63 F.E.R.C. at 65,213. These “savings” were a substantial part of the overall package used to finance the acquisition of PSNH and bring PSNH out of bankruptcy with a reasonable rate structure. *Id.*

14. To illustrate this, opposing parties attached a map to their testimony and briefs showing, in darkened colors, the transmission Goliath of NU/PSNH “cutting off” Eastern Massachusetts and Rhode Island from the rest of New England. Even the Presiding Judge attached the map to his initial decision. *See* 53 F.E.R.C. at 65,238.

15. NU proposed a firm and non-firm transmission tariff for short-term transactions (i.e., those not exceeding five years), but to negotiate individually any requests for service for a longer term. *See* 56 F.E.R.C. at 62,033. The FERC required NU to extend the tariff for a term “as long as the duration of the customer’s power supply contract.” *Id.* at 62,034. However, the FERC did not require NU to file the tariff before consummation of the merger, as had been requested by certain intervenors. *Id.* at 61,991.

transmission system to market its surplus generating capacity;¹⁶ (3) rejected NU's proposal that it could reserve capacity on its "New York ties" for economy transactions or otherwise charge for the "lost" opportunities associated with providing transmission service;¹⁷ and (4) established an "immutable constraints" proceeding to "reallocate" existing transmission capacity where new transmission could not be built.¹⁸

These conditions inflamed the States of New Hampshire and Connecticut, which threatened to deny approval of the merger (and send PSNH back into Bankruptcy Court) if the conditions were retained.¹⁹ The FERC itself was divided. Commissioners Trabandt and Terzic favored compensating native load customers for lost opportunity costs²⁰ and then Commissioner Moler, while joining the majority, indicated her ambivalence on this issue.²¹

After permitting oral argument, the Commission reversed itself on rehearing in two critical respects. First, it permitted NU to charge opportunity costs (if properly formulated and verified) in its firm transmission service tariff²² to compensate native load customers for giving up use of the transmission system to third parties. Second, the Commission abandoned the "immutable constraints" proceeding to "reallocate" transmission capacity and decided instead to rely on transmission pricing to provide incentives to encourage new transmission construction.²³

16. *Id.* at 62,017-18.

17. *Id.* at 62,020-21.

18. *Id.* at 62,024.

19. The State of New Hampshire argued on rehearing, that immutable constraints condition "was an attempt by the Commission to force the states to site transmission lines to serve third parties" and would "encourage the very parochialism that the majority intended to discourage by use of the hammer threat in the first place." Request for Rehearing of the State of New Hampshire at 4, 17, No. EC90-10-001 (filed Sept. 29, 1991). The State recommended, as did NU and Connecticut, that this "war of the regulators can be ended" by holding native load customers harmless. *Id.* at 13.

20. Commissioner Terzic wrote "to register my disappointment at staff's and my colleagues' failure to acknowledge" that "opportunity costs are appropriate to compensate native load customers." 56 F.E.R.C. at 62,072 (Terzic, C., concurring). Subsequent to the *NU/PSNH* order, Chairman Allday gave his now famous speech, stating: "It's no longer true that a particular utility's native load customers deserve special treatment, to the detriment of someone else's native load customers. After all, everybody is somebody's native load customer." *Id.* at 62,073.

21. Commissioner Moler stated: "When we adopted Order 364, I expressed my belief, even at the Commission meeting, that we didn't need to deal in that order with the opportunity cost issue. I thought we could defer it to a later case. Upon reviewing the rehearing petitions, I became convinced, particularly because of the rehearing petitions filed by [the] state commissions, that we had to deal with the issue before it would be clear that the merger could be consummated." *See*, Tr. 36-37 (Oral Argument in EC90-10-001)

22. The Commission adopted its tripartite "balancing" test for pricing transmission services. 58 F.E.R.C. at 61,203. The three pricing goals proposed by the Staff, and adopted by the Commission, were that (1) native load customers be "held harmless"; (2) transmission customers should be charged the "lowest reasonable" cost-based rate; and (3) collection of "monopoly rents" should be prevented. *Id.*

23. *Id.* at 61,209. The FERC went on to further state that:

We now believe that convening a technical conference to debate issues of "immutability" and "reallocation" of existing transmission capacity would be of little value and would serve only to divert attention and resources away from the legitimate issue of determining the

*B. Entergy / Gulf States Utilities*²⁴

In *Entergy/GSU*, the Commission broke new ground by summarily disposing of competitive issues for the first time in recent years where a merger integrated two substantial transmission networks. The primary reason was that the applicants had submitted an open access transmission tariff with their application, which the FERC found would “adequately mitigate any increase in market power in the relevant geographic and product markets that may arise from the proposed merger.”²⁵

Aside from disposing of the merger’s effect on competition without a hearing, the FERC’s decision on competitive issues was noteworthy in two other respects. First, the Commission was not disturbed by the merged company’s possession of up to 27 percent of the uncommitted generation in particular markets. The Commission pointed out that each merger must be “functionally viewed in the context of its particular industry.”²⁶ Second, the FERC rejected requests for “network service” that appeared to rest on the premise that the FERC should “even” the competitive playing field when approving a merger—i.e. put the merged company’s competitors on equal footing with the merged company. The FERC held that such a contention proved too much, for under section 203 the FERC has authority only to remedy “specific” anticompetitive harms “directly resulting” from the merger.²⁷

These findings might have startled an electricity lawyer on vacation since *NU/PSNH*. In *NU/PSNH* and other previous cases, merging applicants had argued, rather unsuccessfully, that (1) the FERC should view with skepticism claims that the possession of a significant share of uncommitted generating capacity conveys market power; and (2) only competitive

incremental cost of an expansion to NU’s transmission system that *can* alleviate a particular constraint. *Id.*

24. *Entergy Servs., Inc. and Gulf States Util. Co. (Entergy/GSU)*, 62 F.E.R.C. ¶ 61,073 (1993), *on reh’g*, 64 F.E.R.C. ¶ 61,001 (1993), 64 F.E.R.C. ¶ 63,026 (1993), 65 F.E.R.C. ¶ 61,332 (1993).

25. *Entergy/GSU*, 62 F.E.R.C. at 61,374. The FERC’s phraseology—that the open access tariff would “adequately mitigate any *increase* in market power” (emphasis added)—is noteworthy. It implies that market power existed prior to the merger, but the FERC did not make any such finding. The phraseology may reflect the Commission’s predilection to believe that control of transmission assets conveys some market power, a proposition many would dispute.

26. *Id.* at 61,375. “Large” utility systems normally possess correspondingly “large” reserves, sometimes even greater than required due to forecasting errors, often giving them “large” market shares of uncommitted capacity. In many instances, however, customer demand in the region is less than supply, which may result in a competitive (albeit “concentrated”) market.

27. *Id.* at 61,376. On rehearing, the FERC described its ruling as grounded in its limited *authority* under section 203, not as a matter of its discretion: “Indeed, the Commission is prohibited from conditioning a merger to affirmatively place competitors in a better position than they would be absent the merger without a showing of potential anticompetitive or other harm that would warrant a remedy.” 64 F.E.R.C. at 61,013-14 (“the Commission cannot order network transmission in this case because it is not needed to remedy a specific anticompetitive harm arising from the merger proposal under review”).

harms having a direct nexus to the merger itself (not preexisting market imperfections) should be at issue in a section 203 proceeding.²⁸

The FERC's change of heart may simply reflect the fact that Entergy already had in place an open access transmission tariff and thus the Commission did not have to find the merger anticompetitive in order to require the filing of such a tariff. There may also be a more fundamental reason: a FERC more confident of its remedial transmission authority. A merger proceeding is no longer the FERC's only chance to remedy problems stemming from transmission control, given the Commission's expanded authority under section 211. Whatever the reason, *Entergy/GSU*, not *NU/PSNH*, likely will provide the model for disposition of competitive issues in future section 203 cases.

C. *The Cincinnati Gas & Electric Co. and PSI Energy Inc.*²⁹

The *CINergy* merger proceeding marked the first time in recent years where the Commission approved a major, contested section 203 application without a hearing on any issue.³⁰ In particular, the FERC summarily disposed of issues that had been set for hearing just a few months before in *Entergy/GSU*. These issues included the merger's effect on operating costs and rates. In each instance, PSI and CG&E proposed rate and other commitments to address these particular concerns prior to the FERC's decision on whether to set the case for hearing.³¹

Also notable was the fact that the Commission rejected the persistent attempts by IPALCO Enterprises, Inc. (which had launched a hostile bid for PSI) to delay action on the application.³² The FERC rejected IPALCO's pleas, and in doing so provided the "bookend" to its earlier decision in *Kansas City Power & Light Co. (KCP&L)*.³³ There, the FERC had expedited its consideration of a tender offer despite the fact that the target had urged the FERC to move slowly or not at all.

28. For example, Northeast Utilities argued that (1) NU's possession of a large share of the surplus generating capacity in New England was unintended and essentially meaningless, given that there were ample alternatives available for the few utilities that were capacity-deficient in the short-run; and (2) there was, in fact, no increase in transmission control as a result of the merger because, pre-merger, PSNH would not provide firm transmission over its system, but post-merger it would. These arguments were rejected. 56 F.E.R.C. at 62,006-07, 62,012 ("Even assuming that NU's transmission commitments will improve the transmission service offered by the applicants, this fact alone would not render the proposed merger pro-competitive, as claimed by NU.").

29. *The Cincinnati Gas & Elec. Co. and PSI Energy, Inc. (CINergy)*, 64 F.E.R.C. ¶ 61,237 (1993), *withdrawn*, 66 F.E.R.C. ¶ 61,028 (1994).

30. While no hearing was held in *UtiliCorp United, Inc. and Centel Corp.*, 56 F.E.R.C. ¶ 61,031 (1991), the combination involved much smaller utilities and the merging entities were not directly interconnected.

31. CG&E and PSI "commit[ted], as a condition of the merger, to not increasing wholesale rates solely because of the merger." *CINergy*, 64 F.E.R.C. at 62,712. CG&E and PSI also "commit[ted] to take certain measures to further strengthen and integrate the[ir] transmission systems." *Id.* at 62,715.

32. IPALCO had argued in its proxy materials sent to PSI shareholders that the *CINergy* deal was in trouble with regulators and, in particular, that the number and hostility of the interventions in the FERC proceeding indicated that the FERC would not act on it until after lengthy hearings.

33. 53 F.E.R.C. ¶ 61,097 (1990).

On rehearing, however, certain parties argued that the Commission's approval of the merger was based on a misapprehension—i.e., that each of the three state commissions that would regulate CINergy's operating affiliates had authority to approve aspects of the proposed reorganization.³⁴ Moreover, the State of Ohio argued that its retail rate authority would be "impaired" by the formation of a registered holding company, given the D.C. Circuit's decision in *Ohio Power Co. v. FERC*.³⁵ The FERC responded by withdrawing its prior order approving the merger and convening a settlement conference to determine whether the concerns of the States could be resolved consensually.³⁶ The Commission's order stated that "we are deeply concerned about the state of the record on the issue of whether this merger will impair effective regulation"; the FERC cautioned that it would "set appropriate issues for hearing" if the matters were not resolved.³⁷

III. THE VITALITY OF THE "COMMONWEALTH" FACTORS

A. *Commonwealth Appendixes*

In *Commonwealth Edison Co.*,³⁸ the Commission set forth six factors it would generally consider in reviewing a section 203 application. In recent years, four of the six factors have atrophied, much like the human appendix: they have remained a part of the section 203 anatomy, but have not performed a regularly needed function. More recently, however, one of the factors seems to be enjoying a comeback, but it is not at all clear as yet how it will be applied.

1. Reasonableness of the Purchase Price

The most obvious appendix is the reasonableness of the purchase price. In recent years, the Commission has not set this issue for hearing in any proceeding. Instead, the Commission has subdivided the issue into three parts and treated each as follows. First, the Commission will not consider the effect of the purchase price "on shareholders" because the "federal and state securities laws provide a mechanism to address these concerns."³⁹ Second, the FERC will not consider a purchase price's "direct" effect on rates (which might occur by passing through an "acquisition adjustment") until a rate is filed under section 205.⁴⁰ Third, the Commission will consider the "indirect" effect of the purchase price on the cost

34. The Applicants took the position that under the original structure (whereby PSI Energy and CG&E would merge into CINergy) such prior approvals were required, but under the revised structure (whereby PSI Energy and CG&E would retain their corporate identities) no such approvals were required.

35. 954 F.2d 779 (D.C. Cir. 1992).

36. *CINergy*, 66 F.E.R.C. ¶ 61,028 (1994).

37. *Id.*

38. 36 F.P.C. 927 (1966).

39. *KCP&L*, 53 F.E.R.C. at 61,285 n.88; *Southern Cal. Edison Co. and San Diego Gas & Elec. Co. (SoCal/SDG&E)*, 47 F.E.R.C. ¶ 61,196, at 61,673 n.20 (1989), *reh'g*, 49 F.E.R.C. ¶ 61,091 (1989).

40. *KCP&L*, 53 F.E.R.C. at 61,285 n.87.

of capital only as part of the larger issue of a merger's effect on operating costs and rates (which is another *Commonwealth* factor).⁴¹ Given this treatment, the issue no longer appears to serve an independent purpose.

2. Coercion

The next candidate for elimination is coercion. To be sure, "coercion" has roots in criminal law,⁴² constitutional law (a "coerced" confession) and testamentary law (a "coerced" last will and testament), but its relevance to a section 203 proceeding is anything but clear. In *Commonwealth*, the issue was framed as whether Commonwealth, a "dominant utility in northern Illinois," could "coerce" Central into merging by "inhibit[ing] Central's efforts to secure meaningful interconnections which could enhance its independent status."⁴³ Presumably, the potential for such "extra high voltage coercion" is hardly a concern today, given the FERC's considerable authority under FPA sections 210 and 211. Moreover, even in the context of a hostile bid for control, the Commission has not found "coercion" to be an issue.⁴⁴

3. Accounting Treatment

There are essentially two methods of accounting for business combinations: the pooling of interests method and the purchase method. The latter involves recording an "acquisition adjustment," while the pooling method does not. The Commission in only one recent case has set the accounting issue for hearing,⁴⁵ and the issue is likely to remain of limited importance in the future. For example, even if "purchase" accounting is permitted, an acquisition adjustment would not (absent a settlement) be reflected in rates in a section 203 proceeding; it requires a section 205 filing. Moreover, a merged company would still be required to file its accounting entries for approval by the Chief Accountant post-merger.⁴⁶ To be sure, merging companies may desire to have their accounting methodology approved

41. See *Kansas Power & Light Co. and Kansas Gas & Elec. Co. (KP&L/KG&E)*, 54 F.E.R.C. ¶ 61,077, at 61,255 (1991).

42. There is a crime of criminal coercion. See MODEL PENAL CODE § 212.5.

43. 36 F.P.C. at 940.

44. In *SoCal/SDG&E*, which began as an unsolicited offer by SoCal, the Commission found no coercion, although it did consider whether employment contracts given SDG&E employees by SoCal signified that SDG&E was "coerced" into accepting SoCal's offer. 47 F.E.R.C. at 61,676. In *KCP&L, KG&E* alleged that KCP&L was "coercing" it into merging by refusing, over the years, to purchase KG&E's interest in a jointly owned generating plant. The FERC rejected the claims as unsupported. 53 F.E.R.C. at 61,288.

45. The Commission stated that "[a]pplicants have not provided adequate support for the proposed accounting treatment," particularly their "fail[ure] to adequately explain why the \$250 million cash election and Entergy Corporation's stock repurchase program fail to satisfy the criteria of APB No. 16 for use of the pooling of interests method." *Entergy/GSU*, 62 F.E.R.C. at 61,373. It also stated that "[a]lthough the proposed accounting treatment for merger transactions generally has not . . . presented issues requiring further consideration at hearing, the appropriate accounting method is significant in this case because . . . an acquisition adjustment, if permitted, could amount to almost \$400 million." *Id.*

46. *KCP&L*, 53 F.E.R.C. at 61,289 n.99.

prior to closing, and for this reason the consideration of a merger's accounting treatment may not become obsolete.

4. The Effectiveness of Regulation

The issue of the impairment of the effectiveness of regulation has had a relatively vague job description in recent years. The issue was set for hearing in *Utah Power & Light Co., PacificCorp, and PC/UP&L Merging Corp. (UP&L/PP&L)*⁴⁷ although it is unclear whether the hearing process provided much value. No impairment of regulation was found and, in fact, the Commission ended up sort of picking a fight with the effected State commissions—i.e. the States objected to the ALJ's finding that their regulation of the merged company would be impaired post-merger.⁴⁸ Since *UP&L/PP&L*, the Commission has confronted a variety of utility combinations, but has not found any of them to “impair” regulation,⁴⁹ much less to warrant a hearing on it.

The Commission's order in *CINergy*, however, may have marked a renaissance for this issue. As discussed earlier, the Commission was “deeply concerned” over the record on whether creation of a registered holding company might impair effective regulation. This concern may, in part, reflect the Commission's general frustration with the *Ohio Power Co. v. FERC (Ohio Power)* decision,⁵⁰ as well as reflecting the personal experiences of the current Commissioners. For example, Commissioner Massey experienced the “Middle South” wars over the Grand Gulf nuclear plant, Commissioner Bailey was previously a State Commissioner responsible for regulating the subsidiary of a registered holding company, and Chair Moler was at the Commission when the *Ohio Power* decision was issued.

Perhaps for this reason, the order in *CINergy* appears to give a closer look at the issue of when a merger might be deemed to “impair” the effectiveness of regulation. The FERC's prior decisions had made it clear that even if a merger shifts regulatory authority from the States to the Federal Government (or vice versa), this will not constitute an “impairment” of

47. 41 F.E.R.C. ¶ 61,283 (1987), 45 F.E.R.C. ¶ 61,095 (1988), *reh'g*, 47 F.E.R.C. ¶ 61,209 (1989), *Environmental Action v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991). The FERC stated that “[t]he potential for misallocation of costs, abuses such as diversion of funds away from operating purposes, and the impairment of prudence reviews are . . . examples of concerns raised in this proceeding. These issues raise questions of fact that require evidentiary proceedings.” *UP&L/PP&L*, 41 F.E.R.C. ¶ 61, 283.

48. *UP&L/PP&L*, 45 F.E.R.C. at 61,295.

49. These structures have ranged from creating a registered holding company, *Fitchburg/Unitil*, 58 F.E.R.C. ¶ 61,201 (1992), to creating two affiliated operating companies in an “exempt” holding company system, *KP&L/KG&E*, to adding an operating company to an existing registered system *Entergy/GSU, NU/PSNH*, and *Southern/Savannah*, 42 F.E.R.C. ¶ 61,240 (1988).

50. *Ohio Power Co. v. FERC*, 954 F.2d 779 (D.C. Cir. 1992).

regulation.⁵¹ Rather, the FERC stated that it was only concerned with regulatory "gaps."⁵²

Given the Commission's order and the Commissioners' public statements in *CINergy*, however, it remains to be seen whether SEC regulation of inter-affiliate transactions under *Ohio Power* will be seen as creating a "gap" in regulation. To be sure, many consumer advocates, and perhaps even some at the FERC, would consider SEC regulation of transactions between affiliates of a registered holding company to be less than rigorous. But it is quite another thing to hold that a merger impairs the "effectiveness" of regulation simply because it transfers regulatory oversight of certain transactions to a sister Federal agency that is considered by some to be "ineffective."

Ironically, the concern that *Ohio Power* has created a regulatory "gap" by divesting the FERC of jurisdiction over certain affiliate transactions is the mirror image of the State's concerns that *Mississippi Power & Light Co. v. Mississippi ex rel. Moore* (*Mississippi Power & Light*)⁵³ divested their jurisdiction over certain affiliate transactions. After *Mississippi Power & Light*, state regulators worried that the review of the prudence of large-scale generating projects entered into by affiliates of a registered holding company would be transferred to the FERC—an agency many of them viewed as never having seen a nuclear plant it didn't like.⁵⁴ *Ohio Power* is merely the counterpart decision from the FERC's point of view, with concerns that the SEC has never seen an affiliate contract it didn't like. Thus, both *Mississippi Power & Light* and *Ohio Power* have brought sharply into focus the distrust by one regulator of another regulator's ability to rigorously review (or interest in reviewing) particular transactions previously thought to be within the former regulator's domain. It remains to be seen whether this general distrust among regulators will constitute cause for the FERC to modify its precedents on when a merger could impair regulation.

Finally, there is the issue of the post-merger allocation of costs between affiliates or divisions. While intercompany or inter-divisional allocations of utility costs may become more complex as the result of a utility merger, this has not been found to "impair" regulation. Indeed, in *UP&L/PP&L* the merged company was to operate divisions in seven states (each of which would have to allocate its costs), but the FERC rejected the ALJ's

51. In *Entergy/GSU*, the FERC held that the transfer of authority from the states to the FERC over certain rate matters "does not suggest any diminishment of effective regulation." 62 F.E.R.C. at 61,374. Conversely, in *UP&L/PP&L*, the FERC found that the transfer of its authority over inter-company rates to the States (which would now regulate inter-divisional allocations) would likewise not impair the effectiveness of regulation. 45 F.E.R.C. at 61,296-97.

52. The Commission explained in *CINergy* that "[w]hen Commonwealth Edison Company referred to impairment of effectively regulation by 'this Commission' and appropriate state regulatory authorities, the Commission's concern was with ensuring 'effective and continuing regulation—i.e. with avoiding a regulatory gap.'" 64 F.E.R.C. at 62,710 n.278.

53. 487 U.S. 354 (1988).

54. See *Powerplant Costs*, Hearing before the Subcommittee on Energy Conservation and Power of the Committee on Energy and Commerce of the House of Representatives, 99th Cong. 2d Sess. (Mar. 20, 1986).

finding that “[r]egulators will virtually be at the mercy of the merged company in determining inter-company cost allocations. . . .”⁵⁵

B. The Effect on Operating Costs and Rates

1. The FERC’s Evolving Approach

The FERC’s consideration of a merger’s effect on operating costs and rates has evolved from a fairly sweeping inquiry of aggregate merger-related savings to a more particularized inquiry focusing on the risk of actual merger-related cost or rate increases. Only a few years ago, it was typical for a merger application to be filed without any supporting testimony or other data on whether the merger would “increas[e] the operating costs that might be expected otherwise to result from independent operation or have an adverse effect on rate levels.”⁵⁶ For example, the applicants in *UP&L/PP&L* did not submit “any specific information” regarding costs or rate impacts.⁵⁷ Similarly, in *NU/PSNH* the applicants provided “no comparison” of costs and rates for the pre- and post-merger companies.⁵⁸ Not surprisingly, these parties (and others)⁵⁹ received a trial-type hearing on the potential rate and cost impacts of the merger.

What did these hearings produce? As to operating costs, the result was the same in each case: the merger was found to produce net operating cost savings.⁶⁰ With respect to “rate” issues, however, the relevant orders differed. For example, in *UP&L/PP&L* the Commission imposed strict post-merger rate filing requirements on the merged company “to ensure that the cost savings that have been projected in support of the merger are fully reflected in wholesale rates.”⁶¹ The FERC did so, it stated, because “[w]here a corporate reorganization or merger generates significant cost savings, there is very little incentive for the new utility to come forward with new rates that fully reflect those savings.”⁶²

By contrast, in *NU/PSNH* and *KP&L/KG&E* (which was settled), the FERC did not impose a requirement that applicants file post-merger rate

55. 45 F.E.R.C. at 61,297.

56. *Commonwealth*, 36 F.P.C. at 937.

57. 41 F.E.R.C. at 61,754.

58. 50 F.E.R.C. ¶ 61,266.

59. *KP&L/KG&E*, 54 F.E.R.C. at 61,252 (“Applicants have not provided detailed support for any of the claimed benefits of the proposed merger; instead, they have provided only bare estimates of the total merger benefits. . . .”); *KCP&L*, 53 F.E.R.C. at 61,285 (“KCP&L’s application provides no comparison between the present rates and costs of KCP&L and KG&E, and those anticipated for the combined companies”); *SoCal/SDG&E*, 47 F.E.R.C. at 61,673 (“The joint application provides no comparison between the present rates and operating costs of Edison and San Diego and those anticipated for the merged company.”).

60. *UP&L/PP&L*, 45 F.E.R.C. at 61,299; *NU/PSNH*, 56 F.E.R.C. at 61,993.

61. *UP&L/PP&L*, 45 F.E.R.C. at 61,303.

62. *Id.* at 61,302. The Commission rejected the applicants commitment to reduce UP&L divisional rates by 2 percent and freeze PP&L divisional rates for five years, and instead required UP&L and PP&L to file a wholesale rate case one, three and five years following the merger. *Id.* at 61,304.

cases.⁶³ In both proceedings, a substantial acquisition adjustment was involved, and for whatever reason customer groups were not adamant in demanding such post-merger rate filings.⁶⁴

More recently, merging applicants have been more forthcoming in their section 203 applications. For example, in *Entergy/GSU* the applicants submitted their case-in-chief testimony on “merger benefits” along with their application. The FERC nevertheless ordered a hearing on cost and rate impacts, but not because of an absence of information. While the FERC criticized several aspects of the applicants’ testimony,⁶⁵ it likely focused on two specific “risks” that the merger potentially posed. First, pending lawsuits by Cajun Electric Power Cooperative represented a litigation risk of \$2.4 billion to GSU (an amount exceeding the entire ten-year projection of merger savings).⁶⁶ Second, the projected merger benefits were weighted heavily towards GSU and the Commission was concerned that under certain assumptions “the merger might impose substantial costs on some of the [Entergy] Operating Companies (e.g., Louisiana Power).”⁶⁷

At the hearing, two conditions were offered by Entergy to alleviate, in part, the concerns regarding these risks: a fuel clause “tracker” and an agreement in principle on capital cost impacts.⁶⁸ These conditions, among

63. In *NU/PSNH*, the agreements governing the post-merger integrated operations of NU and PSNH were filed and approved along with the section 203 application. These agreements included the Sharing Agreement, whereby the savings from integrated operations would be divided between NU and PSNH; the Capacity Interchange Agreements, whereby PSNH and NU agreed to provide each other short-term capacity when the other company was “short” under the NEPOOL Agreement; and the Seabrook Power Contract, which governed sales of Seabrook capacity from NU’s new subsidiary, North Atlantic Electric Corp., to PSNH. 56 F.E.R.C. at 61,987.

64. The settlement in *KP&L/KG&E* did “not address the timing of subsequent general rate case filings by the Companies,” although it provided that in any such filing the companies could “seek recovery of the acquisition adjustment only to the extent that the net benefits of the merger equal or exceed the amount of the acquisition adjustment proposed to be recovered.” 56 F.E.R.C. at 62,378. The settlement otherwise “impose[d] an obligation on the Applicants to hold ratepayers harmless for merger-related costs not offset by merger-created benefits.” *Id.* at 62,377.

65. The Commission also took issue with the applicants use of nominal dollar estimates of merger savings, rather than present value estimates; fuel cost projections that appeared to overstate capacity factors for coal-fired generating units and otherwise exaggerated savings given the similarity of fuel mix; non-fuel operation and maintenance savings estimates that were not reduced by implementation costs; and capacity deferral benefits that included “discrepancies” when compared to capacity addition studies performed by Entergy in other proceedings. *Entergy/GSU*, 62 F.E.R.C. at 61,370-72. While these issues may not have been insignificant, they might not have, standing alone, warranted a hearing.

66. *Id.* at 61,371.

67. *Id.* at 61,372 n.80. In particular, there was a concern of the “Middle South” regulators that GSU ratepayers were expected to benefit from the dispatch of Entergy’s low cost nuclear units without having to bear the capacity costs associated therewith (the allocation of which had spawned litigation throughout the 1980s).

68. The applicants proposed, and the Commission accepted, conditions whereby (1) a “fuel tracker” would be established to determine whether any operating company had incurred, over the ten years following the merger, increased net fuel costs because of the merger and, if so, to have such increased costs refunded by the other operating companies achieving net fuel cost savings, *Entergy/GSU*, 65 F.E.R.C. ¶ 61,332, mimeo at 81; and (2) Entergy would not oppose “in principle” establishing the cost of capital of the operating companies “as if there had been no merger.” *Id.*, mimeo at 94. The first condition addressed the potential for fuel cost shifts to existing Entergy companies, while the

others, were accepted by the Commission in finding the merger not adversely affecting operating costs and rates.⁶⁹

In *CINergy*, the applicants provided testimony on projected merger benefits with their application, but also offered a “hold harmless” protection for wholesale customers. They committed that, post-merger, wholesale rates “will not reflect merger-related costs to the extent such costs are not offset by merger related benefits.”⁷⁰ As in *Entergy/GSU*, there were allegations that the merger posed the risk of cost increases (in *CINergy*, it was the potential for a forced divestiture of CG&E’s gas properties), but unlike *Entergy/GSU* the rate commitments were made prior to the issuance of a hearing order, and the Commission relied on them in summarily disposing of cost and rate issues.⁷¹ As indicated, the Commission later withdrew its order, which may result in modifications to the hold harmless commitment.⁷²

2. Retail Rate Impacts

The issue of a merger’s impact on retail rates has had an undistinguished tenure in section 203 proceedings. In *Commonwealth*, the FERC acknowledged that the issue of retail rate levels “is a matter for the state commission,” but held, “[n]evertheless it is our responsibility under the FPA in determining whether a merger is consistent with the public interest to consider what effect the fact of merger would have on rate levels or on state regulation of retail rate design.”⁷³ Accordingly, the Commission evaluated the potential for adverse retail rate impacts,⁷⁴ but ultimately concluded, “we need not attempt to evaluate here the extent of such [impacts]” because “the entire rate design question is a matter of retail rate regulation coming within the competence of the Illinois Commission.”⁷⁵ This was, to say the least, a circular exercise.

second was designed to mitigate the impact on existing Entergy operating companies of a potential loss of the Cajun litigation.

69. The Commission did not require Entergy/GSU to make a general rate filing post merger.

70. Applicants’ Response to Staff Request for Information, EC93-6-000 (filed July 26, 1993).

71. See *CINergy*, 64 F.E.R.C. at 62,714 (“The Applicants’ hold harmless condition has influenced our decision not to set this issue for hearing.”). The Commission, however, “strengthened” the applicants’ hold harmless commitment by requiring CG&E and PSI to file two general rate cases (sales and transmission rates), one within 60 days following the merger and one five years following the merger. The FERC stated *CINergy* will “have the burden of *convincingly* demonstrating in their section 205 filing that their wholesale customers have, in fact been ‘held harmless’; that any rate increase is *not* related to the merger.” *Id.* The applicants were also required to submit yearly cost of service “informational” filings “demonstrating the costs and benefits associated with the merger for the prior calendar year.” *Id.*

72. *CINergy*, 66 F.E.R.C. ¶ 61,028.

73. 36 F.P.C. at 938.

74. The Commission was concerned that “a retail rate design such as that apparently contemplated by Commonwealth, wherein it would apply its present rate schedules to Central’s customers, makes the Rockford area shoulder some of the higher distribution costs of other Commonwealth service areas. Over a period of time this could dilute the advantages of the merger to Central’s customers.” *Id.* at 939.

75. *Id.*

Unfortunately, the FERC's consideration of retail matters in other cases has not been more satisfying. In *UP&L/PP&L*, for example, the Commission held there is "no support for [the] assertion that the effect [of a merger] on retail rates is within the exclusive jurisdiction of the affected state commissions" and set the matter of retail rate impacts for hearing.⁷⁶ However, after hearing, the FERC approved the merger on the condition that certain wholesale rate filings be made, but said nothing at all about retail rate impacts.⁷⁷

Since *UP&L/PP&L*, the Commission has given indications that retail rate impacts should not be considered in a section 203 proceeding. For example, in *SoCal/SDG&E*, the City of San Diego requested that the Commission "make clear" that the issue of retail rates was within the scope of the hearing order.⁷⁸ The Commission declined the invitation, however, stating: "As to retail rates, these are outside our jurisdiction; presumably the effects of the proposed merger on retail rates will be investigated by the California Public Utilities Commission which also has jurisdiction over this transaction."⁷⁹

In *NU/PSNH*, the applicants urged the Commission not to set retail rate impacts for merger, arguing that "PSNH's retail rates will increase after the merger but . . . the rates must be increased to place the company on a firm financial footing." NU also "pointed to the Bankruptcy Court's responsibility to assess the financial feasibility of the plan, and the rate agreement with New Hampshire officials as reasons why this Commission should not inquire into the effect on PSNH's retail rates."⁸⁰ The FERC agreed, holding that "the effect of the merger upon retail rates need not be addressed."⁸¹

In *KP&L/KG&E*, the Kansas Commission expressed concern over the substantial acquisition adjustment that could be recorded as a result of the merger. The FERC responded by stating that "the Kansas Commission must approve the merger, and can in its own proceeding address the indirect effect of the purchase price on *retail* costs and rates."⁸² In an accompanying footnote, the FERC stated quite broadly, but without explanation, that "[r]etail rate effects are not within the scope of a section 203 proceeding."⁸³

Finally, in *CINergy* the applicants proposed a hold harmless commitment applicable to wholesale, but not retail, rates. On rehearing, certain parties, including the Ohio Commission, requested that the Commission

76. 41 F.E.R.C. at 61,752. At hearing, the ALJ did not make specific findings on the merger's impact on retail rates. 43 F.E.R.C. at 65,334, 65,356 (Finding No. 37). Instead, he found only that applicants' proposal to *reduce* retail rates was unsupported by cost of service studies. *Id.* at 65, 356.

77. See 45 F.E.R.C. at 61,303-05 (discussing only wholesale rate issues).

78. 49 F.E.R.C. at 61,356.

79. *Id.* at 61,359.

80. 50 F.E.R.C. at 61,828.

81. *Id.* at 61,836. Similarly, in *Entergy/GSU* the Commission stated, "we believe that the effect of the proposed merger on retail rates need not be addressed." 62 F.E.R.C. at 61,372 n.82.

82. 54 F.E.R.C. at 61,255.

83. *Id.* at 61,255 n.56.

address retail rate impacts, including whether a retail “hold harmless” condition should be offered. The Commission’s subsequent order withdrawing its approval of the merger focused on whether the merger might impair regulation and did not specifically refer to retail rate impacts.⁸⁴

The Commission should clarify the confusion in the law. It is suggested here that the FERC carefully consider whether it should, absent exceptional circumstances, decline to analyze a merger’s effect on retail rates, just as it has declined consideration of a merger’s effect on retail competition.⁸⁵ While well-motivated, making retail rate findings in a section 203 proceeding may draw the FERC into conditioning a merger on the adoption of retail rate plans and then overseeing their implementation.⁸⁶ This could place the FERC into an area (retail ratemaking) where it does not have jurisdiction and, in doing so, could call into question a State’s ability to rule on similar questions in a later retail proceeding.⁸⁷ It would seem that, in most cases, the States can protect themselves on retail rate issues—either at the time they review a proposed merger or, if they lack jurisdiction over the merger, in wholesale rate proceedings involving the creation of or amendments to a “System Agreement” or in subsequent retail rate proceedings.

To be sure, some would take exception with this view. For example, in *Middle South Energy, Inc. (Middle South)*,⁸⁸ which involved allocating the Grand Gulf nuclear plant among Entergy’s operating companies, the FERC “equalized” the nuclear investment costs of all the Entergy operating companies, including the investment costs for nuclear plants then in retail rate base. Admittedly, in doing so the FERC may have been motivated by the potential imbalances in retail rate levels among the Entergy operating companies that could have resulted from a failure to order any such equalization. But even so, the relief was necessary to make a *wholesale* rate schedule between the Entergy affiliates just, reasonable and not

84. 66 F.E.R.C. ¶ 61,028 (1994).

85. In regards to retail gas and electric markets, the Commission stated that:

We shall not set for hearing issues regarding competition in retail gas and electricity markets because these issues are outside of our jurisdiction. If the merger is consummated, any allegations that Kansas Power has unfairly priced its retail gas service to favor its or KGE’s retail electric service (or vice versa) or has refused to provide retail gas service to favor its or KGE’s retail electric service (or vice versa), are matters for the state commissions, particularly the Kansas Commission. 54 F.E.R.C. at 61,254.

86. Consideration of retail rate matters may also be a slippery slope. For example, if the FERC considers retail rate impacts where there is no State jurisdiction over a merger, should it consider retail matters where (a) State jurisdiction exists, but the exercise of it is alleged to be “ineffective,” or (b) where State statutes evince a determination that there is no need for State PUC pre-approval of a particular form of transaction?

87. In *New Orleans Pub. Serv. Inc. v. The Council of New Orleans*, 911 F.2d 993, 1002 n.5 (5th Cir. 1990), the Fifth Circuit held that where “some of the issues that were relevant to FERC’s wholesale rate proceeding were also relevant to the [retail] proceeding . . . the [State regulator] would have been bound by FERC’s resolution of those issues.” Other cases suggest that where an issue is properly presented for consideration before both the FERC and a State PUC, “preemption” of the State’s factual determination would not occur. See *Monongahela Power Co.*, 39 F.E.R.C. ¶ 61,350 (1987).

88. 31 F.E.R.C. ¶ 61,305 (1985), *reh’g denied*, 32 F.E.R.C. ¶ 61,425 (1985).

unduly discriminatory. While the FERC generally agreed that it "has jurisdictional authority to order a form of production cost equalization," it cautioned that the "exercise of this jurisdiction must be tempered and weighed against the policy consideration that generation facilities and retail rate regulation should be left to the states."⁸⁹

The purpose here is not to suggest that the policy or jurisdictional questions raised by a merger's potential impact on retail rates permit an easy resolution. Rather, it is to suggest that the FERC reconcile the various decisions discussed above and enunciate a clear policy on this matter. The issue is too important to remain suspended in its presently uncertain state.

C. *The Effect on Competition*

Only a few years ago, the most difficult issue facing the Commission in a merger proceeding was the effect of the merger on competition. In the *UP&L/PP&L*, *SoCal/SDG&E* and *NU/PSNH* proceedings, there were highly controversial competitive issues presented and in each case there was substantial uncertainty as to how the FERC would react.⁹⁰ The Commission set each matter for hearing and found two of the proposed mergers to harm competition.⁹¹ As a remedy, the FERC imposed a requirement that the merged company open up its transmission grid.⁹²

Since then, the process has been inverted. In both *Entergy/GSU* and *CINergy*, the applicants provided a pro forma open access transmission tariff in their applications, seeking thereby to avoid a hearing on competitive issues. In both cases, a hearing was indeed avoided, with the FERC finding, on a summary basis, that the tariffs would mitigate any "increase" in transmission market power resulting from the merger and that no market power in generation existed.⁹³

Does this mean that competitive issues in future cases will generate a yawn? Not necessarily. Consider the following two scenarios. First, suppose that in a capacity-short region the only utilities with substantial uncommitted generating capacity merged. Would this give the merged company "market power" in the short-run in selling its "surplus" generation?⁹⁴ In such an instance, the FERC presumably would have several

89. *Middle South*, 32 F.E.R.C. at 61,952 (1985).

90. The *UP&L/PP&L* merger combined UP&L's "strategic" transmission network with PP&L's surplus generation. *SoCal/SDG&E* involved allegations that SDG&E was being acquired for its projected load growth, to be served with high-cost affiliate contracts. *NU/PSNH* involved allegations that it created a "transmission curtain" around Boston and Rhode Island.

91. The *SoCal/SDG&E* merger was the exception, being abandoned prior to issuance of a Commission order.

92. Only the form of relief differed: in *UP&L/PP&L*, the company was required to abide by transmission "conditions," while in *NU/PSNH* the company was required to file open access transmission tariffs.

93. 62 F.E.R.C. at 61,374; 64 F.E.R.C. at 62,727.

94. In *NU/PSNH*, the FERC found that NU possessed 65 percent of the uncommitted generating capacity in the region. This may not have concerned the FERC because (1) there were relatively few utilities forecasting a need for short-run capacity in NEPOOL and consequently the supply of bulk

options. Theoretically, it could disapprove the merger, finding it anticompetitive. It could also approve the merger, relying on the ultimate discipline for potential monopoly power—cost-based rates.⁹⁵ This salve was relied upon for more than half a century when transmission-dependent wholesale customers had very few or no options. The FERC also could determine that, despite such a short-run competitive concern, on the whole the merger was consistent with the public interest.⁹⁶ It is now well-established that:

In evaluating [a merger], the Commission is required to find that the entire transaction, taken as a whole, is consistent with the public interest. Each element of the transaction need not benefit every utility or individual which might be affected; rather, the whole transaction must be consistent with the interest of “the public.” There is no reason to think that the interest of [an] individual [company] is synonymous with the “public” interest. . . . The statute does not require . . . that FERC establish conditions so that every effect of an approved merger could withstand the “public interest” test.⁹⁷

While the factual scenario suggested here may be extreme, it may well be that concerns over the competitiveness of generation markets may receive closer attention in the future. As the industry moves toward “open access” on all transmission grids and market based rates for wholesale transactions, the FERC may give more attention to short-term imperfections in generation markets. A merger proceeding will likely be no exception.

Second, changes in the pricing of transmission services could present new challenges to the FERC’s existing market definition model. The FERC currently treats each wholesale customer as a “destination market” and evaluates its options, given the utilities with whom it is directly interconnected or can access through an open access transmission tariff. For such a customer, a merger may actually increase its options by (1) opening up a transmission grid previously not subject to an “open access” obligation, or (2) that failing, providing access over two interconnected systems for one charge. The latter justification works because of “postage-stamp” pricing.⁹⁸

If transmission service were to be priced on a distance-sensitive basis, however, a more particularized analysis might be required. Assuming transmission was generally available on the merging companies’ grids pre-merger (which may increasingly be the rule, not the exception), a customer interconnected therewith might not see any change in its options. It very well could access the same markets before and after the merger at the same price (but may have one less option from which to purchase power). It is

power, though concentrated, exceeded demand; and (2) with NU’s tariff in place, NEPOOL utilities could access power from the New York Power Pool, thereby increasing their generation options.

95. This would not, however, guarantee a “market based” rate.

96. This could be, for example, because it lowered operating costs or increased competition in long-run markets (by opening up the companies’ transmission grids).

97. *Northeast Util. Serv. Co. v. FERC*, 993 F.2d 937, 939 (1st Cir. 1993).

98. Postage-stamp pricing allows customers to access a delivery and receipt point anywhere on a utility’s system for the same rate.

not that such a merger would be anticompetitive, but rather that a pro-competitive aspect might no longer exist in the form it does today.

D. *Commonwealth Parasites*

Perhaps seizing on the nonexclusiveness of *Commonwealth's* six factors, a few interlopers have managed to find their way into section 203 proceedings.

1. Operational Impacts

For a brief period several years ago, the FERC would rather routinely require applicants to demonstrate the operational "impacts" of their merger on interconnected systems. For example, in *Tucson Electric Power Co. (Tucson Electric)* the FERC stated:

Several parties expressed concern that the combined systems, once merged, may be dispatched in such a manner as to adversely affect the use and operation of interconnected transmission systems without compensation. Therefore, we will direct that the parties address this issue, as well as the concerns associated with unintended power flows over affected systems. Several parties expressed concern that the merger will threaten the availability of capacity on Tucson's system and frustrate existing "as available" contracts. . . . Therefore, we will direct that the hearing address the use and operation of the merged companies facilities under existing contracts.⁹⁹

In *SoCal/SDG&E*, the Commission similarly required the companies at hearing to "show the impact of the merger on other systems."¹⁰⁰

Since *SoCal/SDG&E*, however, the Commission has not set such matters for hearing. In *Entergy/GSU*,¹⁰¹ for example, the FERC held that its intervening decision in *American Electric Power Service Corp.*¹⁰² had made clear that interconnected utilities must, "in the first instance," attempt to solve operational matters consensually before coming to the Commission. Thus, it held:

The issues identified by CLECO in its motion for clarification—decreased transmission availability, operational complications, or loop flows—are issues that must, in the first instance, be addressed by CLECO and the applicants, either in bilateral discussions or through procedures designed for resolving these issues provided for under the Southwest Power Pool. If those efforts prove unsuccessful, CLECO, as note above, may file with the Commission to be compensated for any adverse effects that may result if the merger is consummated.¹⁰³

99. 44 F.E.R.C. ¶ 61,441, at 62,395 (1988).

100. 47 F.E.R.C. at 61,673. The exception was the *NU/PSNH* proceeding, where similar "operational" allegations were made, but the Commission declined to set them for hearing. The FERC stated: "Because the NEP, Northeast and PSNH systems are all currently dispatched by NEPOOL, and will continue to be dispatched by NEPOOL after the merger, we do not believe there is any reason why any potential unintended power flow problems cannot continue to be handled under the NEPOOL agreement." 50 F.E.R.C. at 61,836.

101. 62 F.E.R.C. ¶ 61,156 (1993).

102. 49 F.E.R.C. ¶ 61,377, at 62,381 (1990); see also *Public Serv. Co. of Ind.*, 51 F.E.R.C. ¶ 61,367, at 62,211-121 (1990), *aff'd on other grounds*, *Northern Ind. Pub. Serv. Co. v. FERC*, 954 F.2d 736 (D.C. Cir. 1992); *Vermont Elec. Power Co.*, 48 F.E.R.C. ¶ 61,330, at 62,085 (1989).

103. *Entergy/GSU*, 62 F.E.R.C. at 62,096.

The Commission reiterated the point in a later *Entergy/GSU* order, stating “as a general matter, a merger proceeding is [not] the appropriate forum for determining operational impacts—particularly rate impacts—on interconnected systems.”¹⁰⁴

This notwithstanding, on one related, but distinct, issue—“whether the Applicants will be able to operate the merged system as planned” and thus “can substantiate the projected cost savings that they claim”—the FERC permitted a hearing in *Entergy/GSU*. This issue arose from an interconnected utility’s claim that its contracts with GSU would limit the economic dispatch options of the merged company.¹⁰⁵

A similar approach was taken in *CINergy*. There, American Electric Power alleged that over 90 percent of the energy dispatched between PSI and CG&E would flow over AEP’s transmission network.¹⁰⁶ By contrast, CG&E and PSI argued that they would upgrade their existing interconnection so that its rated capacity would equal or exceed any power transfers between them.¹⁰⁷ The Commission declined to set the matter for hearing, stating that “integral to our decision not to set the projected merger benefits for hearing . . . is Applicants’ commitment to take certain measures to further strengthen and integrate the transmission systems of PSI and CG&E.”¹⁰⁸ The Commission also explained that, unlike in *Entergy/GSU*, “AEP does not claim that the Applicants will be contractually prohibited from operating their combined systems as planned.”¹⁰⁹

While the issue appears settled at present, *Entergy/GSU* and *CINergy* may not represent the last word on merger-related operational impacts. By their very nature, mergers will invariably produce operational impacts on interconnected systems. Vertically integrated utilities plan and site generation and transmission to meet load on a localized basis, and all resources on the system are centrally dispatched to economically and reliably meet such load. When two systems are combined and operated as a single system, the

104. *Entergy/GSU*, 64 F.E.R.C. at 61,015.

105. *Id.*

106. AEP argued: “the Applicants propose a day-to-day operating regime that is fundamentally at odds with accepted good utility practice. Lacking the effective strength to integrate the operation of their systems, they do not propose to build or acquire it. Instead they would appropriate the transmission facilities of AEP System Companies and of other systems as critical components of their internal interconnected operations, freely transmitting flows between their divisions over these facilities in either direction as it suits their own purpose.” AEP Protest and Motion to Intervene at 3, No. EC93-6-000 (filed Jan. 27, 1993).

107. CINergy responded: “Contrary to AEP’s suggestion, there is nothing inadequate about the CG&E-PSI interconnection. The interconnection, as planned to be upgraded, will have a thermal rating sufficient to accommodate anticipated maximum on-peak transfers of energy between the CG&E and PSI Energy divisions (up to 500 MW) and transmission service will be negotiated (from AEP or others) for any transfers that exceed the thermal capacity of the interconnection (during off-peak hours). Under current industry operating guidelines, this is all that is required.” Answer of CG&E and PSI at 65, No. EC93-6-000 (Filed Feb. 11, 1993).

108. 64 F.E.R.C. at 62,715.

109. *Id.* The Commission also stated that “if unscheduled power flows should occur, the parties are not without means to address the issue, and if such means fail, the parties may then come to the Commission and either seek appropriate compensation or file a complaint.” *Id.*

changes in system dispatch and unit commitment necessary economically and reliably to meet their combined load will alter existing power flow patterns. Because transmission networks are planned principally to dispatch particular generating units to particular load centers, however, the resulting changes in power flows may well place unplanned demands on regional or local transmission networks. These demands may impose no burden at all or very real burdens, and there may or may not be remedies in existing interconnection agreements to address such impacts. Given this technical reality, the FERC will likely be faced with operational complaints on a recurring basis.

2. Environmental Issues

Environmental issues have appeared in two different forms in recent merger cases. First, the Commission's regulations provide that an "environmental assessment" or an "environmental impact statement" under the National Environmental Policy Act (NEPA) need not be prepared in connection with a section 203 application.¹¹⁰ In *SoCal/SDG&E*, however, opponents of the merger contended that "the proposed merger will affect two of the most polluted airsheds in the Nation and will, according to the Applicants' own filings before the California Public Utilities Commission, add substantially to the air pollution in the Southern California area."¹¹¹ The Commission initially declined to require preparation of an environmental assessment, but reversed itself on rehearing, holding " [b]ecause the proposed merger would take place in two of the most heavily polluted air basins in the Nation, and in light of the evidence presented thus far, we believe an EA is warranted."¹¹²

The NEPA issue was raised again in *NU/PSNH*, but the Commission found that exceptional circumstances did not exist there. The Commission reiterated that "mergers are categorically excluded from the requirement to prepare an environmental impact statement" and explained that the decision in *SoCal/SDG&E* was "prompted by specific factual allegations indicating that 'the proposed merger could add hundreds of tons of additional air contaminants to the most polluted air in the Nation.'"¹¹³

The second issue relates to 42 U.S.C. § 7506(c)(1)¹¹⁴ which provides that "[n]o department, agency, or instrumentality of the Federal Government shall . . . approve, any activity which does not conform to an implementation plan after it has been approved or promulgated under section 7410 of this title." In *SoCal/SDG&E*, the State of California argued that the FERC had an "affirmative duty" under section 7506(c) to determine whether the "merger is consistent with the applicable state implementation plan for attaining and maintaining the federal ambient air quality stan-

110. 18 C.F.R. § 380.4(16) (1992).

111. 49 F.E.R.C. at 61,357.

112. *Id.*

113. 56 F.E.R.C. at 62,047.

114. 42 U.S.C. § 7506(c)(1) (1991).

dards.”¹¹⁵ The FERC considered, but did not decide the issue, since it had already directed the preparation of an environmental assessment.¹¹⁶

In *CINergy*, an intervenor argued that section 7506(c) required that applicants submit their post-merger Clean Air Act compliance strategy, which would allow the FERC to determine the merger’s effect on the operation of generating facilities jointly owned by the intervenor and CG&E. The FERC held that arguments regarding “the impact of CINergy’s compliance strategy with the Clean Air Act Amendments upon such [jointly owned] facilities . . . are both premature and highly speculative.”¹¹⁷ It also held that “any limitations regarding the operation of jointly owned generating units . . . will be contained within the four corners of the ownership and operating agreements. . . .”¹¹⁸

3. State-Federal Conflicts

While State-Federal tensions are certainly not a “factor” to be considered in reviewing a section 203 application, they are a powerful political force that can affect the FERC’s consideration of other issues. Three different factual scenarios illustrate the variety of pressures facing the FERC.

First, there is the circumstance of “concurrent” jurisdiction where the States and the FERC may both approve a merger, but in doing so may step on each other’s toes. This occurred in *NU/PSNH*, where the FERC’s initial order was viewed by the States of New Hampshire and Connecticut as depriving native load customers of their fair use of a transmission system they built and paid for.¹¹⁹ The States publicly warned the FERC that they would reconsider their orders approving the merger if the FERC did not remove the oppressive conditions. This forced the FERC to consider on rehearing whether the conditions it sought to impose to alleviate concerns over regional markets could so upset the States that they would deny the merger and throw PSNH back into bankruptcy. The FERC ultimately adjusted its order, thereby avoiding such a head-on conflict, and the merger was approved by all regulators. While such “concurrent” jurisdiction may make each regulator happy in the abstract, in practice it can be a recipe for conflicting decisions, with merging applicants or intervenors often caught in the middle.

Second, there is the situation where a state commission does not have jurisdiction over a proposed merger and seeks recourse at the FERC to

115. 49 F.E.R.C. at 61,355.

116. *Id.* at 61,360.

117. 64 F.E.R.C. at 62,726.

118. *Id.*

119. The State of New Hampshire, in its request for rehearing, stated:

It is undisputed that PSNH and NU built these [transmission] systems to meet the future needs of their native load customers and, in turn, those customers assumed financial responsibility for the systems. Because Opinion 364 does not adopt a hold-harmless provision for native load customers or opportunity cost pricing when setting transmission rates, native load customers will be denied the use of and not be compensated for the loss of economic use of the system they built.

Request for Rehearing of New Hampshire at 3, EC90-10-001 (filed Sept. 9, 1991).

obtain retail rate protections. This occurred in *CINergy*, where the Ohio Commission asked the FERC to investigate retail rate impacts and the merger's effect on retail regulation, arguing that it had no other forum given its asserted lack of authority to approve the merger. In withdrawing its initial order in *CINergy*, the Commissioners' public statements seemed to indicate that the presence or absence of state jurisdiction over a merger will indeed influence the Commission's disposition of these issues. While the ultimate resolution of *CINergy* may shed more light on this issue, it is surely open to debate whether the Commission's "public interest" obligations under section 203 of the Federal Power Act should differ depending on whether or not a state also has jurisdiction over the merger.

Third, a less complicated fact pattern exists where a state commission looks to FERC for wholesale rate protections. In *Entergy/GSU*, the state commissions in Arkansas, Mississippi and New Orleans were concerned that, because they lacked jurisdiction over the merger, the scales had been tilted towards GSU ratepayers (whose regulators did have authority to approve the merger).¹²⁰ These Commissions sought wholesale protections from the FERC (in the form of amendments to Entergy's wholesale "System Agreement"). In this type of situation, the FERC has clear jurisdiction to address the states' concerns and, if its order does not satisfy them, the matter can be taken up on judicial review. The potential for conflict remains, but the solution is much simpler.

IV. JURISDICTION AND RELATED MATTERS

There are several issues bearing on the scope of the FERC's section 203 jurisdiction that should receive closer attention in coming years.

A. *Acquisitions That Are Hostile in Nature*

In *KCP&L*, Kansas City Power & Light had made an unsolicited offer for the shares of KG&E and immediately filed an application requesting approval from the FERC to merge (or effect a similar business combination) with KG&E. KG&E opposed the application, arguing "the Commission does not possess the authority under section 203 to authorize a merger which is proposed to be undertaken by an unsolicited tender offer."¹²¹ The FERC rejected this argument and instead expedited the application, holding:

We find that an acquiror's opposition to a proposed merger *in and of itself* is not enough to cause us to look unfavorably upon an applicant's request for

120. An example, of the tilted scales is in the City of New Orleans' brief which states:

By Entergy's own admission, its merger proposal is designed to gain the approval of GSU's state regulators—the Texas and Louisiana Commissions. This could not be more apparent from the vast and heavily skewed amount of benefits it projects to flow to GSU. As the Commission notes, nearly 85 percent of the Applicants' projected savings from the merger will go to GSU, leaving the [Entergy Operating Companies] with a razor-thin cushion against the risk of possible harm in the event the projections are wrong.

Brief of New Orleans on Exceptions, EC92-21-001 (filed Sept. 29, 1993).

121. 53 F.E.R.C. at 61,282.

section 203 approval. . . . We find no statutory authority or judicial precedent which would require us to distinguish between negotiated mergers and those opposed by the proposed acquiree's board of directors.¹²²

The Commission did, however, "stress that our action today should not be construed as favoring, or disfavoring, KCP&L's tender offer."¹²³

In the future, proposed acquisitions that are hostile in nature may cause the FERC to consider certain undecided jurisdictional issues. For example, does a utility transfer control over its jurisdictional facilities (and thus trigger section 203) when 50 percent or less of its voting securities changes hands or when a majority of its board of directors is replaced in a proxy contest?

There is limited FERC guidance.¹²⁴ In *Central Vermont Public Service Corp.* (*Central Vermont*), a public utility sought to create a holding company and requested that FERC disclaim jurisdiction. The FERC disagreed, holding that "the transfer of ownership and control of [the public utility's] jurisdictional facilities . . . to the newly created holding company, constitutes a disposition of jurisdictional facilities requiring prior Commission approval under section 203."¹²⁵ The FERC stated that the utility's "jurisdictional facilities" would now be "controlled through the parent's ownership of the utility's common stock by virtue of the parent's ability to name [the utility's] board of directors."¹²⁶

Central Vermont left open the question whether a "transfer of control" 50 percent or less, for example, of the voting securities of a public utility would trigger FERC jurisdiction. In *Central Illinois Public Service Co.* (*Central Illinois*), the FERC stated: "It is not our intent to undertake regulation of every stock transfer made by public utility shareholders. Our concern is solely with transfers of *control* of public utilities and, thereby, the jurisdictional facilities of those public utilities."¹²⁷ *Central Illinois* thus left the issue undecided.

In practice, however, the issue may have limited application. Under the Public Utility Holding Company Act, a utility holding company needs prior approval before acquiring 10 percent or more of a second public util-

122. *Id.* at 61,283.

123. *Id.* at 61,284. The Commission took the same approach when the converse set of facts was presented in *CINergy*. There, CG&E and PSI had sought FERC approval of a friendly "merger of equals," while IPALCO Enterprises, Inc. had launched a tender offer for the shares of PSI, and had sought to delay FERC consideration of the *CINergy* application. IPALCO argued that expedited approval of the application would mean the FERC was "choosing sides" in the proxy contest. The FERC rejected IPALCO's pleas, stating, "[i]n acting today, we do so with the full knowledge that [IPALCO] is competing to acquire PSI Resources" and "[o]ur intention in acting now is not to favor, endorse, or inhibit implementation of either Applicants' or IPALCO's proposal." *CINergy*, 64 F.E.R.C. at 62,682. The Commission explained, "[w]e take a neutral stance as between such competing offers." *Id.* at 62,710.

124. Section 203 requires prior Commission approval for the "disposition" of a public utility's jurisdictional facilities. Section 203 also applies where one public utility seeks to purchase, acquire or take the security of another public utility.

125. 39 F.E.R.C. ¶ 61,295, at 61,960 (1987).

126. *Id.*

127. 42 F.E.R.C. ¶ 61,073, at 62,328 (1987).

ity company (the "two bite" rule). In addition, in practice it would be unusual for a potential acquirer to acquire a substantial portion of the outstanding shares of a utility without triggering a "poison pill" or other protective mechanism.

Another scenario is the potential for a change in the board of directors as the result of a proxy contest. On this issue there does not appear to be controlling FERC precedent. In a somewhat analogous context, however, the Federal Communications Commission, in a 1986 Policy Statement on Tender Offers and Proxy Contests, held that "[a]bsent exceptional circumstances, we have determined that proxy contests do not result in substantial changes in corporate control."¹²⁸ It "rejected the contention advanced by a number of parties that a proxy challenge proposing to replace a majority of the Board of Directors, as a matter of law, should be deemed to constitute a substantial transfer of control."¹²⁹

In addition to presenting jurisdictional issues, tender offers and proxy contests may also cause the FERC to reexamine its procedural approach to section 203 applications. For example, the FCC has stated that the principle of "strict governmental neutrality in takeover contests" can be ensured only if the "administrative processes [cannot] be utilized . . . in a manner which favors either the incumbent or the challenger in disputes over corporate control."¹³⁰ In reviewing its procedures, the FCC found that its "long form" procedures could "operate so as to unduly insulate incumbent management from corporate challenges and that delays inherent in our regulatory process can be used as tactical weapons in battles for corporate control."¹³¹

One procedural issue is whether "comparative hearings" on competing section 203 applications would be appropriate.¹³² It does not appear that the FERC has ever squarely addressed the issue, although in *KCP&L* the target company (KG&E) requested that "the Commission defer action on

128. *In re Tender Offers and Proxy Contests*, 59 Rad. Reg. 2d (P & F) 1536, 1551 (1986).

129. *Id.* at 1548.

130. *Id.* at 1540.

131. As a result, the FCC established a "bifurcated" process whereby a tender offeror would submit a "short form" and "long form" application simultaneously. The short form application would request expedited approval to set up a voting trust that would receive the shares tendered. The voting trustee could not be controlled by the offeror in the interim period pending final approval. The long form application would request the traditional approvals required to consummate the transaction. *Id.* at 1562.

132. The comparative hearing is a creature principally of "certificate" applications, where a pipeline (or radio station) seeks a determination that its application to serve particular customers is consistent with the public convenience or necessity. In *Ashbacker Radio Co. v. FCC*, 326 U.S. 327 (1945), two competing applicants sought to operate radio stations at the same frequency and the FCC on the same day approved one application without a hearing and set the other application for hearing. The Supreme Court vacated the FCC order, holding that "where two *bona fide* applications are mutually exclusive the grant of one without a hearing to both deprives the loser of the opportunity which Congress chose to give him." *Id.* at 333.

KCP&L's filing because other offers for KG&E may be forthcoming."¹³³ The FERC rejected the request.¹³⁴

The issue has, however, been addressed at the state level. For example, the Kansas Commission consolidated for hearing the competing applications of KCP&L and KPL to acquire KG&E, although KCP&L soon thereafter withdrew its bid.¹³⁵ In Illinois, an appellate court has ruled that "the question whether a [utility] merger is in the public interest can be meaningfully answered only within the context of possible alternative actions."¹³⁶

B. *The Missouri Basin "Gap"*

The most widely discussed jurisdictional controversy arose out of *Missouri Basin Municipal Power Agency v. Midwest Energy Co. & Iowa Resources, Inc. (Missouri Basin)*.¹³⁷ There, the FERC held that a merger of two utility holding companies (which are not themselves "public utilities" under the FPA) does not require prior approval of the FERC under section 203.

The decision raised the ire of consumer advocates. Consumer advocates have argued that *Missouri Basin* created a "loophole" through which any utility with foresight can pass, viz—each merger partner forms a holding company prior to merging and, thereafter, the holding companies merge without prior FERC approval.¹³⁸ While such a merger would require prior approval of the Securities and Exchange Commission (SEC) (given that the surviving holding company would be acquiring a second utility "bite"), consumer advocates consider SEC approval a "no brainer."

Moreover, the FERC itself stated in *Missouri Basin* that it "share[d] [the] concern" that such a loss of jurisdiction could "complicate" the FERC's task of protecting the public interest.¹³⁹ More recently, a member of the FERC's Office of General Counsel has argued that *Missouri Basin*, while rightly decided, "permit[s] potential utility merger applicants to choose their regulatory forum in order to escape stringent regulatory scrutiny of their proposed merger's effect on the existing competitive situa-

133. 53 F.E.R.C. at 61,283.

134. *Id.* at 61,284. In *NU/PSNH*, certain parties claimed that the PSNH reorganization could not be considered as a merger "benefit" because, under the Reorganization Plan, PSNH would "emerge" from bankruptcy prior to merging with NU and could exist as a stand alone entity without the merger. The ALJ rejected the argument, holding, "there is no requirement that the Commission examine some nonmerger scenario in comparison with the proposal before it." 53 F.E.R.C. at 65,211. The Commission summarily affirmed the Judge. 56 F.E.R.C. at 61,933.

135. *In re Kansas Power and Light Co.*, 127 PUB. UTIL. REP. (PUR) 4th 201, 206 (KCC 1991).

136. *Illinois Power Co. v. Illinois Commerce Comm'n*, 490 N.E.2d 1255, 1257 (Ill. Ct. App. 1986).

137. *Missouri Basin Mun. Power Agency v. Midwest Energy Co. & Iowa Resources, Inc.*, 53 F.E.R.C. ¶ 61,368, *on reh'g*, 55 F.E.R.C. ¶ 61,464 (1991).

138. Allen, *To FERC or Not to FERC*, *ELECTRICITY JOURNAL* (Jan/Feb 1991). If a merger of the two public utility subsidiaries were later desired, it would require FERC review, but the antitrust analysis of a merger of affiliates is ordinarily less rigorous than for a merger of unaffiliated entities. See *United States v. Citizens & Southern Nat'l Bank*, 422 U.S. 86 (1975); *Wisconsin Elec. Power Co. & Wisconsin Mich. Power Co.*, 59 F.P.C. 1196, 1201 (1977).

139. *Missouri Basin*, 55 F.E.R.C. at 62,532.

tion.”¹⁴⁰ In his view, utilities will routinely choose “ineffective regulation” by the SEC over the FERC’s more stringent review.¹⁴¹

These concerns, while well articulated, may underestimate the FERC’s remedial authority to discipline a merging utility’s actions even in the absence of section 203 jurisdiction. Take, for example, the concern that a holding company merger could have “anticompetitive” consequences, but escape rigorous antitrust scrutiny at the FERC.¹⁴² To date, the FERC’s principal concern in a section 203 context has been control of transmission assets, but the FERC is no longer reliant solely on its section 203 conditioning authority to require merging utilities to open up their transmission grids.¹⁴³ Using the Commission’s expanded powers under section 211, a competitor may obtain transmission service from a merged system following the merger.¹⁴⁴

Other issues, such as the effect on operating costs and rates, do not require resolution *only* in a section 203 proceeding.¹⁴⁵ In fact, merger-related rate changes cannot normally be effected without prior approval under section 205.¹⁴⁶ For example, if a merger entailed a large acquisition adjustment, the adjustment normally could not be recovered from ratepayers, or even considered, in a section 203 proceeding.¹⁴⁷

This is not to say that the FERC’s section 203 authority is insubstantial or duplicative of its authority elsewhere. It is to say, however, that dire consequences stemming from a *Missouri Basin* “gap” should not lightly be assumed. Moreover, the notion that utilities will set up holding companies in anticipation of later merging, and thus receiving “light handed” review by the SEC, is overblown. The process of forming a holding company requires prior FERC approval and, in many cases, approval from state regulators and the Nuclear Regulatory Commission. It is not a step to be taken swiftly or secretly. In any event, creation of a holding company is a double-edged sword: it may speed consummation of a friendly merger, but it may also expose the utility as a target more swiftly to be acquired by another utility holding company.¹⁴⁸

140. Spiwak, *Expanding the FERC’s Jurisdiction to Review Utility Mergers*, 14 ENERGY L.J. 385 (1993).

141. *Id.* at 405 n.108. Consumer advocates’ arguments about “ineffective” regulation by the SEC’s PUHCA division date back to the 1980s, when the SEC recommended repeal of the 1935 Act. More recently, Senator Bumpers introduced legislation (S.544, 103rd Cong., 1st Sess.) that would transfer administration of the 1935 Act from the SEC to the FERC, citing concern over the SEC’s administration of the Act.

142. *Id.* at 405.

143. 45 F.E.R.C. ¶ 61,095 (1988); 56 F.E.R.C. ¶ 61,269 (1991).

144. The FERC, in a section 203 proceeding also focuses on control of generation resources and, to the extent this was a concern, could be reviewed by the Justice Department or the SEC.

145. *See* 56 F.E.R.C. at 61,119.

146. The exception, of course, would be cost items, such as fuel, recovered under formula rates.

147. 65 F.E.R.C. ¶ 61,332, mimeo at 116. When an acquisition adjustment is sought to be recovered in rates, the utility must make a “showing of customer specific benefits.” *Id.* (citing *Minnesota Power & Light Co.*, 43 F.E.R.C. ¶ 61,104, at 61,342 (1988)).

148. For example, PSI Energy was wholly owned by a holding company (PSI Resources), but CG&E was not, and the CINergy transaction was thus submitted to the FERC. By contrast, IPALCO

C. SEC "Preemption"

For those who believe the *Missouri Basin* "gap" is a problem, the specter of SEC preemption under FPA section 318 is a nightmare. Section 318 provides that if "any person" is "subject to" a FERC "requirement" that respects the same "subject matter" as a "requirement" of the SEC, the FERC's jurisdiction must give way.¹⁴⁹ The section applies to utility combinations that involve "the acquisition or disposition of any security, capital assets, facilities, or any other subject matter."

At present, the application of section 318 to a FERC merger proceeding is severely limited. In *Southern/Savannah*, the FERC held that where a utility holding company acquires a public utility by merging it with a special purpose subsidiary, section 318 does not apply because (1) different "persons" are involved (the acquired utility is the "applicant" at the FERC, while the holding company is the "applicant" at the SEC); (2) the "subject matter" is different (the public utility is "disposing of utility assets," while the holding company is "acquiring utility securities"); and (3) there is no "direct conflict" between the FERC's review of the transaction and the SEC's review.¹⁵⁰

Notwithstanding *Southern/Savannah*, section 318 may receive closer attention in the future. The problem is that section 318 either applies to very few or, alternatively, very many mergers. To explain, under the FERC's interpretation of the section 318 "same person" requirement, the statute is not applicable to most utility merger transactions for the simple reason that the "applicant" before both agencies is usually different. SEC approval is triggered by a holding company acquiring a second utility "bite," while FERC approval is triggered by a public utility disposing of its facilities.¹⁵¹ Some might argue that, by so interpreting section 318, the FERC has taken the lifeblood out of it. On the other hand, one could give section 318 a more expansive reading—for example, whereby the "same person" requirement would be read to include each party to the transaction. Under such an interpretation, section 318 would eclipse the FERC's authority over many transactions it now regulates, undoubtedly raising the ire of the Commission as well as consumer advocates. This inherent tension in interpreting section 318 (admittedly, not a model of legislative draftsmanship) may well provoke controversy in the future.

V. THE HEARING PROCESS

The Commission has come a long way. In 1966, the Commission stated that "the public interest . . . will generally be best served by setting for hearing all applications requesting approval of the merger and consoli-

Enterprises proceeded with its tender offer for PSI without the FERC approval because both IP&L and PSI Energy were wholly owned by holding companies.

149. 16 U.S.C.A. § 825q (1991).

150. *Southern/Savannah*, 42 F.E.R.C. at 61,779.

151. There are instances where the "applicant" before both agencies would be the same, but they are few.

dation of two or more Class A electric utilities.”¹⁵² Twenty years later, however, the Commission in *UP&L/PP&L* made clear that a hearing will not issue as a matter of course “where the receipt of evidence will not aid the Commission in reaching an ultimate decision.”¹⁵³

This progression continued five years later in *Entergy/GSU*, where the Commission bristled at the notion that “because the Commission has in past merger cases set competition for hearing, precedent requires that the Commission set competition for hearing in *this* proceeding.”¹⁵⁴ Responding, the Commission held it “cannot, and will not, take a ‘cookie-cutter’ approach to merger applications under section 203.”¹⁵⁵ Later the same year, the Commission initially approved the *CINergy* merger without a trial-type hearing on any issue.¹⁵⁶

This evolution is responsible and commendable. Only one modification is suggested here. The FERC has traditionally relied on two, and only two, models of procedure in a merger case: summary disposition or trial-type hearing.¹⁵⁷ There is much room in the middle for flexibility. For example, if a competitive issue cannot be resolved by summary disposition, it may be addressed in a paper hearing.¹⁵⁸ Competitive issues principally involve the analysis of markets, which requires the collection and interpretation of data. In many cases, this data can adequately be collected and explained in written submissions (which may well include affidavits) directly to the Commission itself. While this would deprive the Energy Bar of the opportunity to beat up on a half-dozen economists, Western Civilization no doubt would survive.

Other procedures may be suitable for other issues. For example, “operational” issues, to the extent considered by the FERC, may be better suited for a settlement process, either the appointing of a “settlement judge” or the selection of another form of alternative dispute resolution. As the FERC has recognized, consensual resolution of such day-to-day operational matters is preferable.¹⁵⁹ The ADR procedure “mini-trial” may be suitable for operational issues, given their complex and fact-laden character.¹⁶⁰

152. 35 F.P.C. 877 (1966).

153. 41 F.E.R.C. at 61,753 (quoting *Southwestern Public Serv. Co.*, 23 F.E.R.C. ¶ 61,153 (1983)).

154. 64 F.E.R.C. at 61,010.

155. *Id.*

156. 64 F.E.R.C. ¶ 61,237, *withdrawn*, 66 F.E.R.C. ¶ 61,028.

157. The exception has been settlement conferences held in *KP&L/KG&E* and *CINergy*.

158. Competitive issues have been decided in paper hearings in other settings. See *Public Serv. Co. of Ind.*, 51 F.E.R.C. ¶ 61,367 (1990) (request for market based rates); *Transcontinental Gas Pipe Line Co.*, 48 F.E.R.C. ¶ 61,199 (1989) (gas inventory charges).

159. 62 F.E.R.C. ¶ 61,156 (1993).

160. Harter, *Points on a Continuum: Dispute Resolution Procedures and the Administrative Process*, 1 ADMIN. L. J. 141, (1987).

The minitrial, sometimes referred to as a mini-hearing to indicate the relatively informal nature of the process, is a highly abbreviated litigation process in which litigants present the heart of their case to senior officials of the other party who have authority to settle. . . . An advantage of the minitrial is that it focuses the attention and energy of executives on both sides of the dispute and forces them to participate directly in the negotiated settlement.

The purpose here is not to suggest any one solution, but to encourage the use of a greater range of options.

VI. CONCLUSION

In looking to the future, there is likely only one prediction that will come true with respect to section 203 proceedings: they will continue to be protean in nature, with the applicable standards shifting and the outcomes difficult to predict. Section 203 is surely (and appropriately) a work in progress, appendixes and parasites alike.

Id. at 191. “The minitrial technique lends itself well to cases involving highly technical concepts and disputes involving mixed questions of law and fact.” *Id.* at 198.