

LIMITATIONS ON THE OBLIGATION TO PROVIDE
ACCESS TO ELECTRIC TRANSMISSION
AND DISTRIBUTION LINES

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In response to increasing costs of power and energy and advances in electric transmission technology, electric utilities throughout the United States have received numerous requests to wheel.¹ The majority of the requests have concerned wholesale power, but an increasing number are requests to wheel to retail customers.² In framing their response to these requests, electric utilities have asked counsel to analyze the wheeling provisions contained in the Public Utility Regulatory Policies Act of 1978³ (PURPA) and the antitrust case law developed in the wake of *Otter Tail Power Company v. United States*,^{3,1} and to provide a "yes" or "no" answer to whether they have an obligation under PURPA or the antitrust laws to provide the requested wheeling.

Anyone who has undertaken this analysis will confirm that this question, even in the context of a specific request, does not lend itself to a "yes" or "no" answer. Thus, in view of the potential liability for treble damages, electric utilities have been loathe to refuse a request to wheel even when the request seemed to provide, in their business judgment, an unfair advantage.^{4,1}

This article has several purposes: first, to demonstrate the very limited availability of wheeling under the Federal Power Act, as amended by PURPA;

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¹Wheeling is the "transfer by direct transmission or displacement [of] electric power from one utility to another over the facilities of an intermediate utility." *Otter Tail Power Co. v. United States*, 410 U.S. 366, 368 (1973).

²Part II of the Federal Power Act applies to "the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but shall not apply to any other sale . . ." Section 201(b). The sale of electric energy at wholesale is defined "a sale of electric energy to any person for resale," Section 201(d), and should be distinguished from retail sales, *i.e.*, sales to the ultimate consumer of the electricity, which are subject to state regulation. Thus, a request to wheel power to retail customers necessarily involves a party who is not involved in a request to wheel wholesale power, *i.e.*, the ultimate consumer of the electricity.

There are, of course, many different kinds of wholesale sales. For example, a municipal distribution system, which provides retail service within the city's boundaries pursuant to a franchise issued by the city, may purchase full requirements wholesale service, *i.e.*, it purchases at wholesale from a single supplier all the power it resells within the city. A city possessing its own generation may elect to purchase partial requirements wholesale service, *i.e.*, it purchases at wholesale from a single supplier its power and energy needs which are not met by its own generation. Larger utilities typically engage in wholesale transactions involving specific amounts of capacity and associated energy for specific periods of time.

In addition there are a variety of short term wholesale transactions, such as economy sales for periods ranging from one hour to several months, sales intended to replace capacity undergoing maintenance, and various coordination arrangements that permit utilities to coordinate plant additions. These short term transactions may require a different antitrust analysis from that applied to long term transactions; short term transactions are discussed in a separate section below.

^{3,1}Pub. L. No. 95-617, 92 Stat. 3117.

⁴410 U.S. 366 (1973)

¹⁵U.S.C. § 15.

^{4,1}Recently, one utility, in response to a request to wheel power to a retail customer, has attempted to resolve this uncertainty by requesting a federal district court to issue a declaratory judgment declaring that its refusal to provide the requested wheeling would not be violative of the Sherman Act. *Gulf States Utilities Co. v. The City of Lafayette, Louisiana, et al.*, Civil Action No. 84-132 (M.D. La. 1984).

second, to demonstrate that the uncertainty in a utility's obligation to wheel under the antitrust laws cannot be entirely resolved but reflects an inherent uncertainty in the law; third, to demonstrate the courts' recognition that the possession of monopoly power by a regulated company operating as a natural monopoly is too readily inferred from a traditional market share analysis and does not reliably indicate possession of the power to control prices or exclude competitors; fourth, to review the courts' attempt to develop the essential facilities doctrine, in lieu of the market share analysis, as a means of establishing the possession of monopoly power by such regulated companies; fifth, to demonstrate that the present great uncertainty in a utility's obligation to wheel is partly due to the failure of the courts to develop reasonably objective standards for application of the essential facilities doctrine to requests to wheel wholesale power; sixth, to suggest a minimum objective standard for application of the essential facilities doctrine to such requests; and, seventh, to determine if the essential facilities doctrine, as developed for application to requests to wheel wholesale power, should be applied to requests to wheel to retail customers. In short, this article will attempt to identify and to explain the specific circumstances when a utility should reasonably be obligated to wheel.

OBLIGATION TO WHEEL UNDER THE FEDERAL POWER ACT, AS AMENDED BY PURPA

The Federal Power Act ("Act") grants the Federal Power Commission or its successor, the Federal Energy Regulatory Commission ("FERC" or "Commission"), jurisdiction over "the transmission of electric energy in interstate commerce."⁵ Historically, Part II of the Act did not empower the Commission to order a utility to provide wheeling. This limitation on the Commission's powers was recognized by the Commission in a series of cases beginning with *City of Paris v. Kentucky Utilities Co.*⁶ The Supreme Court in *Otter Tail Power Co. v. United States* confirmed that the Commission was not authorized by Part II of the Act to compel wheeling:

So far as wheeling is concerned, there is no authority granted the Commission under Part II of the Federal Power Act to order it, for the bills originally introduced contained common carrier provisions which were deleted. The Act as passed contained only the interconnection provision set forth in § 202(b). The common carrier provision in the original bill and the power to direct wheeling were left to the "voluntary coordination of electric facilities."⁷

In an attempt to circumvent this limitation, it has been argued that the Commission's authority under Section 205 and 206 of the Act to review and modify voluntarily filed rate schedules for transmission service is sufficient to require the filing utility to make wheeling generally available. This argument, however, was rejected in *Richmond Power & Light v. FERC*.⁸

If Congress had intended that utilities could inadvertently bootstrap themselves into common-carrier status by filing rates for voluntary service, it would not have bothered to reject mandatory wheeling in favor of a call for just such voluntary wheeling. What the Commission is prohibited from doing directly it may not achieve by indirection.⁹

⁵Section 201(b).

⁶41 F.P.C. 45, 48 (1969).

⁷410 U.S. at 376-77 (footnote omitted).

⁸574 F.2d 610 (D.C. Cir. 1978).

⁹*Id.* at 620 (footnote omitted).

It was also argued in *Richmond Power & Light v. FERC* that the Commission was empowered to order additional wheeling as a remedy for undue discrimination in the provision of transmission services. Addressing this argument, the court found that a decision to wheel for one customer but not for another was not *per se* unreasonable.¹⁰ Because Richmond had not attempted to establish facts demonstrating that the refusal was unreasonably discriminatory or anticompetitive, the court was not required to address the issue further. In a more recent case, *Florida Power & Light Co. v. FERC*,¹¹ the court expressed "serious doubts that such a petition [for an order requiring wheeling to remedy a discriminatory refusal to wheel] would be successful in the absence of a [transmission] tariff."¹²

The Commission, however, in Opinion No. 198, *Southeastern Power Administration v. Kentucky Utilities Company*,¹³ stated that its inability, pursuant to the sections added to the Act by PURPA, to order wheeling as a remedy for a anticompetitive conduct did not establish that the Commission was without such power under other sections of the Act:

[S]ubsection 211(c)(1) prohibits the Commission from using its new wheeling authority to remedy relationships that are unlawful under the antitrust laws, this is not to be taken as legislative approval of those relationships. The Commission retains full authority to address those relationships under other provisions of the Power Act.¹⁴

The Commission conceded, however, that "[a]t present it is not entirely clear whether we may order wheeling pursuant to sections 205 and 206 even to remedy anticompetitive conduct."¹⁵ Moreover, in the recent initial decision in *Pacific Power & Light Co.*,¹⁶ the Administrative Law Judge, apparently relying on the authority granted by Sections 205 and 206, ordered wheeling as a remedy for undue discrimination.¹⁶ Thus, whether the Commission has the authority under Sections 205 and 206 to remedy a refusal to wheel, which was shown to be unduly discriminatory, by expanding a utility's wheeling obligation beyond that voluntarily undertaken by an agreement to provide specific transmission services to other utilities is still open to debate.

Section 211 of the Federal Power Act,^{16 . 1} enacted by the Public Utility Regulatory Policies Act, granted the Commission authority to order wheeling. This authority, however, is narrowly prescribed, as Sections 211 and 212 of the Act contain a number of standards that must be met before wheeling can be ordered.

It should be recognized at the outset that the Commission's limited authority under Section 211 to order wheeling does not expand its authority to order wheeling under other sections of the Act. In *New York State Electric & Gas Corp. v. FERC*,¹⁷ the court, in accordance with *Richmond Power & Light v. FERC*, ruled that the Commission was not empowered by its review powers under Section 206 to expand a voluntary pre-existing commitment to wheel and that such an expansion could be ordered only after the Commission made the findings required by Sections 211 and 212.¹⁸ Similarly, in *Florida Power & Light Co. v. FERC* the court noted that the

¹⁰*Id.* at 623.

¹¹660 F.2d 668 (5th Cir. 1981), *cert. denied*, 103 S. Ct. 800 (1983).

¹²*Id.* at 675.

¹³25 F.E.R.C. ¶ 61,204 (1983).

¹⁴*Id.* at 61,538.

¹⁵*Id.* at 61,542 n.56.

¹⁶*Pacific Gas & Electric Co.*, Docket Nos. E-7777(II) and E-7796, 26 F.E.R.C. ¶ 63,043 (February 10, 1984).

^{16 . 1}16 U.S.C. § 824j

¹⁷638 F.2d 388 (2d Cir. 1980), *cert. denied*, 454 U.S. 821 (1981).

¹⁸*Id.* at 403.

Commission's authority under Section 206 to modify unreasonable or unduly discriminatory terms in transmission contracts did not empower the Commission to order additional wheeling without complying with the provisions of Sections 211 and 212.¹⁹

As to requests to wheel power to retail customers, the standards of PURPA are quite specific: Section 211(c)(4) provides that "no order may be issued under subsection (a) or (b) of [Section 211] which provides for the transmission of electric energy directly to an ultimate consumer." In short, the limited authority to order wheeling granted by Sections 211 and 212 expressly does not include the power to order an electric utility to wheel to retail customers.

As to requests to wheel wholesale power, the Commission is just beginning to address the standards for availability under PURPA. In a case of first impression, FERC Opinion No. 198, *Southeastern Power Administration v. Kentucky Utilities Company*,²⁰ the Commission denied Southeastern Power Administration's ("SEPA") application under Sections 211 and 212 for an order compelling Kentucky Utilities Company ("KU") to wheel SEPA power to eight municipalities which are presently wholesale power customers of KU.

The Commission's opinion focused on the "threshold requirement" of Section 211(c)(1), *i.e.*, an order compelling wheeling cannot be issued unless "such order would reasonably preserve existing competitive relationships." SEPA and the municipalities argued that this provision requires an examination of the overall competitive relationship between SEPA and KU. In contrast, KU contended that the provision requires an examination of the relationships SEPA and KU have with the municipalities. After reviewing the legislative history of the section, the Commission concluded that "the proper way to determine whether existing competitive relationships would be reasonably preserved is to compare what the wheeling utility currently sells to the customers that are to receive the power and energy to be transmitted and what the utility would sell if it were ordered to wheel."²¹

The Commission rejected SEPA's contention that "existing competitive relationships" must be defined more broadly if Section 211 is to provide any effective remedy to purportedly anti-competitive refusals to wheel. Specifically, the Commission concluded that the Section was designed to be "competitively neutral"²² and "to keep the Commission out of the economic contests among utilities for customers."²³

In that case, SEPA wanted to wheel 25 MW of power and 36,000 MWh of energy to the eight municipalities. These sales by SEPA would displace 18% of the power and 6% of the energy KU currently sells to these municipalities. It was undisputed that these percentages were sufficiently large that the existing competitive relationship between SEPA and KU for sales to these municipalities would not be reasonably preserved by an order compelling KU to wheel this power. Thus, applying its interpretation of Section 211(c)(1) to the facts of this case, the Commission concluded that SEPA's application failed to meet the threshold requirement of Section 211(c)(1).

Opinion No. 198, of course, has larger implications. Specifically, Opinion No. 198 would seem to make it extremely difficult to obtain an order under Section 211

¹⁹660 F.2d at 673.

²⁰25 F.E.R.C. ¶ 61,204 (1983), *rehearing denied*, 26 F.E.R.C. ¶ 61,127.

²¹*Id.* at 61,536.

²²*Id.* at 61,537.

²³*Id.* at 61,540.

compelling a utility to wheel power to its full requirements customers.²⁴

In summary, the Commission has no authority to compel a utility to accede to a request to wheel power to *retail* customers; has limited but as yet unprecisely defined authority under Section 211 to order a utility to wheel wholesale power; and may have authority (this issue is unresolved) to order wheeling pursuant to Sections 205 and 206 as a remedy for anticompetitive conduct. More to the point of the present article, a utility's obligation to wheel under the Act is invoked only by application to and upon order by the Commission. Thus, this obligation is different in character from an obligation to accede to a request for wheeling imposed by the antitrust laws and policed by the federal courts' authority to award treble damages.

OBLIGATION TO WHEEL UNDER THE ANTITRUST LAWS

An obligation to wheel arises under the antitrust laws, if at all, pursuant to § 2 of the Sherman Act which provides, *inter alia*, that it is a violation of the Act to "monopolize or attempt to monopolize . . . any part of the trade or commerce among the several states."²⁵

In certain circumstances a refusal to deal with a competitor is a violation of § 2. Therefore, in these instances, § 2 imposes an obligation to deal. Ordinarily, such an obligation attaches only if the company refusing to deal possesses monopoly power and the refusal is an abuse of that power.²⁶ The particular circumstances under which a single-firm monopolist has a duty to deal is, however, "one of the most unsettled and vexatious [questions] in the antitrust field."²⁷

Section 2 has, of course, been applied to refusals to deal by non-regulated and regulated companies, including refusals to wheel by electric utilities. As discussed below, there is an inherent uncertainty in determining whether any company, whether it is regulated or unregulated, has an obligation to deal imposed by Section 2. The courts, however, have recognized that the market share analysis traditionally used to test refusals to deal by non-regulated companies does not provide reliable results when applied to regulated companies which operate as natural monopolies. Specifically, the substantial market share of a regulated company does not support the usually reliable inference of monopoly power; this substantial market share is simply the result of regulation and does not reflect the regulated company's ability to control prices or exclude competition in this market. Accordingly, the courts have revived an earlier analysis, the essential facilities doctrine, and have applied this doctrine to refusals to deal by regulated companies for the purpose of providing direct, reliable evidence of monopoly power, *i.e.*, the ability to control prices or exclude competition. The courts' development of this analysis, however, has not remedied the initial problem posed by application of the traditional market share analysis to such companies. Due to the courts' failure to establish objective standards

²⁴In its order denying rehearing, the Commission stated that "at some point the business that the wheeling order would cause to be shifted from one utility to another would be small enough that competitive relationships would not be significantly altered' but that this question "we necessarily leave to another day" (Slip Op. at 6).

²⁵15 U.S.C. § 2.

²⁶"As a general rule, a company has the right to deal with whomever it chooses. *Associated Press v. United States*, 326 U.S. 1, 14-15 (1945). This right is limited when the company possesses a monopoly because the danger exists that it may use its monopoly position to decrease competition in other markets by refusing to deal with competitors. Accordingly, courts have held that in certain instances a monopolist's refusal to deal violates the antitrust laws." *Mid-Texas Communications Systems, Inc. v. American Telephone & Telegraph Co.*, 615 F.2d 1372, 1387 (5th Cir.), *cert. denied*, 449 U.S. 912 (1980).

²⁷*Byars v. Bluff City News Co., Inc.*, 609 F.2d 843, 846 (6th Cir. 1979).

for determining whether a facility is "essential," this doctrine, in the same manner as the market share analysis, has reduced proof of the possession of monopoly power by a regulated company to a perfunctory matter.

A. *There is an Inherent Uncertainty in any Obligation to Deal Imposed By Section 2*

The Supreme Court has stated that the offense of monopolization has two elements: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power . . ." ²⁸ The Supreme Court has also stated that monopoly power is "the power to control prices or exclude competition." ²⁹ Thus, the most direct manner of proving monopoly power is to demonstrate a company's actual control over prices or its exclusion of competitors. This was the manner of proof in early antitrust cases. ³⁰

Subsequently, the courts developed a "shortcut formula" ³¹ for proving monopoly power, *i.e.*, monopoly power was inferred from possession of a predominant share of the relevant market. This shortcut relied heavily on the concept of the relevant market, which ordinarily is critical in monopolization cases because the definition of the relevant market "determines market share and market share all but determines whether one is a monopolist." ³²

The concept of the relevant market has two separate components: the relevant product market and the relevant geographic market. ³³ In defining the relevant product market, "the reality of the marketplace must serve as the lodestar." ³⁴ The marketplace imposes two general constraints in determining the relevant product market. First, the product market must reflect transactions between buyers and sellers, in the sense that there must be actual or potential competition for the products within the defined market. ³⁵ Second, a relevant product market appropriate for Section 2 analysis must include all products that are reasonably interchangeable for the same purposes. ³⁶ This rule simply acknowledges that the power to control the price of one product does not establish monopoly power within the ambit of Section 2 when there are close substitute products to which buyers will turn in response to a price increase in the product.

The standards used to determine the appropriate geographic market are essentially similar to those used to determine the relevant product market. In particular, the relevant geographic market must correspond to the commercial realities of the industry and must be economically significant. ³⁷ An often stated formulation of the relevant geographic market is the area in which sellers of the

²⁸United States v. Grinnell Corp., 384 U.S. 563, 570 (1966).

²⁹*Id.* at 571; United States v. E.I. duPont De Nemours & Co., 351 U.S. 377, 391 (1956).

³⁰Byars v. Bluff City News Co., 609 F.2d at 850. *See* United States v. International Harvester Co., 274 U.S. 693 (1927); United States v. U.S. Steel Corp., 251 U.S. 417 (1920).

³¹Byars v. Bluff City News Co., 609 F.2d at 850.

³²*Id.* at 850 n.17.

³³United States v. Empire Gas Corp., 537 F.2d 296, 303 (8th Cir. 1976), *cert. denied*, 429 U.S. 1122 (1977).

³⁴*Id.*

³⁵City of Cleveland v. Cleveland Electric Illuminating Co., 538 F. Supp. 1306, 1310 (N.D. Ohio 1980).

³⁶"In considering what is the relevant market for determining the control of price and competition, no more definite rule can be declared than that commodities reasonably interchangeable by consumers for the same purposes make up that 'part of the trade or commerce,' monopolization of which may be illegal." United States v. E.I. duPont De Nemours & Co., 351 U.S. 377, 395 (1956).

³⁷Brown Shoe Co. v. United States, 370 U.S. 294, 336-37 (1962).

product at issue compete and to which purchasers can practicably turn for supplies.³⁸

The determination of the relevant market is a question of fact³⁹ which often cannot be precisely resolved.⁴⁰ This question of fact, which is fundamental to a finding of monopolization under the traditional market share analysis, introduces an unavoidable degree of uncertainty in determining whether a company has an obligation to deal.

The second element of monopolization, the element of abuse of monopoly power, is also a question of fact and, therefore, introduces further uncertainty in determining whether a company has an obligation to deal. In the context of a monopolist's refusal to deal, there are two theories for finding the requisite abuse of that power to establish a Section 2 violation: the intent theory and the bottleneck theory.⁴¹ The intent theory "focuses on the monopolist's state of mind"⁴² and requires evidence of a specific⁴³ intent to create or maintain monopoly power. In contrast, the bottleneck theory,⁴⁴ which purports to be a more objective analysis, "examines the detrimental effect [of the refusal to deal] on competitors."⁴⁵

B. A Market Share Analysis Does Not Support A Reliable Inference of the Possession of Monopoly Power By Regulated Companies

Otter Tail involved, among other significant conduct,⁴⁶ a refusal to wheel wholesale power by Otter Tail Power Company (Otter Tail) to municipalities which Otter Tail formerly served at retail but which desired to operate municipal electric distribution systems. The government, as plaintiff, alleged that Otter Tail's conduct constituted a monopolization of commerce in violation of Section 2. The relevant product market which Otter Tail allegedly monopolized was the sale of electric power at retail⁷ and the relevant geographic market was the aggregate of towns in Otter Tail's service area.⁴⁸

Following a traditional market share analysis, the trial court inferred from Otter Tail's substantial market share that Otter Tail possessed monopoly power in

³⁸"... [t]he relevant geographic market, for antitrust purposes, comprises that area within which the sellers of a commodity effectively compete, and in which prospective purchasers are effectively offered a choice as among alternative sources of supply." *City of Cleveland v. Cleveland Electric Illuminating Co.*, 538 F. Supp. at 1318; *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961); *United States v. Empire Gas Corp.*, 537 F.2d at 304.

³⁹"Defining the relevant market, the threshold requirement under Section Two, is essentially a matter of resolving factual issues." *Pinder v. Hudgins Fish Co.*, 570 F.2d 1209, 1220 (5th Cir. 1978) (footnote omitted); *California Steel and Tube v. Kaiser Steel Corp.*, 650 F.2d 1001, 1003 (9th Cir. 1981); *City of Cleveland v. Cleveland Electric Illuminating Co.*, 538 F. Supp. at 1320.

⁴⁰"... [A] certain amount of fuzziness is often inherent in the task of defining a relevant geographic market, and the final decision must often be a compromise." *United States v. Empire Gas Corp.*, 537 F.2d at 304.

⁴¹*Byars v. Bluff City News Co.*, 609 F.2d at 855.

⁴²*Id.* at 856.

⁴³"Although a general intent to monopolize is all that is ordinarily required to find a § 2 violation, cases discussing a monopolist's duty to deal have effectively required a finding of *specific* intent to monopolize." *Id.* at 859 (footnote omitted).

Other courts have required specific intent in cases involving refusals to deal by regulated companies or in natural monopoly settings. *Hecht v. Pro-Football, Inc.*, 570 F.2d 982, 990 (D.C. Cir. 1977), *cert. denied*, 436 U.S. 956 (1978); *City of Mishawaka v. American Electric Power Co.*, 616 F.2d 976, 985 (7th Cir. 1980), *cert. denied*, 449 U.S. 1096 (1981).

⁴⁴A refusal to wheel power would satisfy the conduct element of a § 2 violation. *City of Groton v. Connecticut Light & Power Co.*, 662 F.2d 921, 926 (2d Cir. 1981).

⁴⁵*Byars v. Bluff City News Co.*, 609 F.2d at 856.

⁴⁶See *infra* note 57.

⁴⁷*United States v. Otter Tail Power Co.*, 331 F. Supp. 54, 58 (D. Minn. 1971).

⁴⁸*Id.* at 58-59.

this relevant market.⁴⁹ As to the second element of monopolization, abuse of monopoly power, the trial court relied on the bottleneck theory.⁵⁰ Specifically, the trial court found that Otter Tail was "dominant in operation of subtransmission lines in [its service area]," that it was "not economically feasible or practical for a municipality to construct its own subtransmission line,"⁵¹ that Otter Tail's "control over transmission facilities in much of its service area gives it substantial effective control over potential competition from municipal ownership,"⁵² and that "by its refusal to sell or wheel power [Otter Tail] prevents that competition from surfacing."⁵³

The Supreme Court, without much discussion, affirmed this portion of the trial court's decision but did not necessarily affirm the trial court's analysis.⁵⁴ The dissent, which would have found Otter Tail's conduct to be exempt from the antitrust laws, excepted to the trial court's "mechanical" application of the traditional market share analysis to a regulated company operating as a natural monopoly.⁵⁵

The Court in this case has followed the District Court into a misapplication of the Sherman Act to a highly regulated, natural monopoly industry wholly different from those that have given rise to ordinary antitrust principles.

* * *

The District Court concluded that Otter Tail had substantial monopoly power at retail and "strategic dominance" in the subtransmission of power in most of the market. The District Court then mechanically applied the familiar Sherman Act formula: since Otter Tail possessed monopoly power and had acted to preserve that power, it was guilty of an antitrust violation.⁵⁶

The dissent specifically criticized the trial court's market share analysis, noting that Otter Tail's 91% market share was based on simply the number of towns served but that a 28.9% share resulted if market share was measured in terms of actual retail sales. The dissent also noted that "another reasonable geographical

⁴⁹Otter Tail served 465 towns in its service area and municipalities served only 45 towns. From this information, the trial court calculated that Otter Tail possessed 91% of the relevant market and concluded that this market share was "certainly enough to justify the inference that [Otter Tail] possesses monopoly power in the area". *Id.* at 59. Including the 105 towns served by rural electric cooperatives, Otter Tail's market share was reduced to 75.6%, which was still sufficiently large for the trial court to infer possession of monopoly power. *Id.* at 59.

⁵⁰"Having found that Otter Tail does possess monopoly power, the second question is whether Otter Tail has sought to maintain that power. A principal contention of the government is that the defendant has been able to maintain this power because of its strategic dominance of transmission capacity in most of the Otter Tail area." *Id.*

⁵¹*Id.*

⁵²*Id.* at 59-60.

⁵³*Id.* at 61.

⁵⁴Numerous courts and commentators have emphasized that *Otter Tail* involved significant conduct in addition to a simple refusal to deal including Otter Tail's refusal to sell wholesale power to these municipalities and Otter Tail's institution or financial support of court litigation intended to frustrate the sale of revenue bonds to finance the municipal systems. Otter Tail's overall conduct was "unusually predatory" and went well beyond a simple refusal to deal. *Byars v. Bluff City News Co.*, 609 F.2d at 857; *Mid-Texas Communications Systems Inc. v. American Telephone and Telegraph Co.*, 615 F.2d at 1389 n.14; Note, *Unclogging the Bottleneck: A New Essential Facilities Doctrine*, 83 COLUM. L. REV 441, 451 (March 1983).

⁵⁵410 U.S. at 383 (Stewart, J., dissenting).

⁵⁶*Id.* at 382-83 (footnote and citation omitted). In particular, the dissent stated that "[n]owhere did the District Court come to grips with the significance of the Federal Power Act either in terms of the specific regulatory apparatus it established or the policy considerations that moved the Congress to enact it. *Id.* at 383. . . The dissent further noted that the nature of the industry and the Act "left room for the development of economies of large scale, single company operations," which included "natural monopolies at retail and similar economies of scale in the subtransmission of power." *Id.* at 384.

market unit might be each individual municipality. Viewed this way, whichever power company sells electricity at retail in a town has a complete monopoly.⁵⁷

Several other antitrust suits against electric utilities for refusals to wheel followed in the wake of *Otter Tail*. The dissent's objection to the mechanical application of the standard Section 2 Sherman Act formula and, in particular, the dissent's suggestion that a market share analysis was inherently difficult and perhaps produced misleading results when applied to regulated companies operating as natural monopolies was not lost, but was echoed in a call for the application of new standards, in lieu of market share data, in monopolization cases involving regulated companies which operated as natural monopolies.⁵⁸

Several courts responded to this call and questioned the use of the traditional market share analysis in monopolization cases involving regulated companies operating as natural monopolies. For example, the Fifth Circuit in *Alameda Mall v. Houston Lighting & Power Co.*⁵⁹ stated that:

Monopolization cases involving such regulated industries are special in nature and require close scrutiny. The reason for this is that regulation is considered an adequate replacement for the lack of competition that exists with a natural monopoly. In such a case, controlling a predominant share of the relevant market cannot infer the traditional monopoly power associated with an entity outside the regulated field.⁶⁰

Again, in *Mid-Texas Communications Systems, Inc. v. American Telephone & Telegraph Co.*,⁶¹ the Fifth Circuit held that the fact of regulation must be considered in determining whether a company possesses monopoly power. This case concerned a refusal by AT&T to provide toll interconnections to an independent telephone company, which was formed for the purpose of providing service within a new residential development, with the Bell System. AT&T contended that it had the right under Section 201(a) of the Communications Act to oppose interconnections which were not in the public interest and, accordingly, a refusal to provide such interconnections was not a violation of the antitrust laws. The Fifth Circuit ruled, *inter alia*, that the trial court erred in directing the jury to assume the existence of monopoly power while refusing to instruct the jury on the regulatory mechanism to compel interconnection.⁶²

Finally, the Seventh Circuit in *MCI Communications Corp. v. American Telephone and Telegraph Co.*,⁶³ expressly rejected the traditional market share analysis as a reliable method of establishing the possession of monopoly power by a regulated company:

⁵⁷*Id.* at 383 n.1.

⁵⁸Watson & Brunner, *Monopolization by Regulated "Monopolies": The Search for Substantive Standards*, 22 ANTITRUST BULL. 559 (1977).

⁵⁹615 F.2d 343 (5th Cir.), *cert. denied*, 449 U.S. 870 (1980).

⁶⁰*Id.* at 354 (footnote omitted).

⁶¹615 F.2d 1372 (5th Cir.), *cert. denied*, 449 U.S. 912 (1980).

⁶²*Id.* at 1387.

⁶³708 F.2d 1081 (7th Cir.), *cert. denied*, 104 S. Ct. 234 (1983). MCI raised various allegations against AT&T. Fifteen counts, all based on § 2, went to the jury, which found for MCI on ten of these counts and returned a single award of damages. Among MCI's allegations were that AT&T's pricing of its long distance services, which competed with the services offered by MCI, was predatory; that AT&T unlawfully refused MCI access to its local distribution facilities which are an essential facility for MCI to offer long distance services; and, that AT&T also refused MCI access to its multi-point interconnections which are an essential facility for MCI to offer long distance service.

Cases dealing with non-regulated industries have developed a number of analytic tools designed to aid courts in identifying each of these elements. In many instances, however, these tools are of only limited value in resolving monopolization charges against regulated monopolies. See Watson & Brunner, *Monopolization by Regulated "Monopolies": The Search for Substantive Standards*, 22 Antitrust Bull. 559, 563 (1977). In particular, the presence of a substantial degree of regulation, although not sufficient to confer antitrust immunity, may affect both the shape of "monopoly power" and the precise dimensions of the "willful acquisition or maintenance" of that power. *Id.*

According to the Supreme Court, monopoly power may be defined as "the power to control prices or exclude competition" in a relevant market. *United States v. E.I. du-Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956). In many cases involving unregulated industries, however, courts have eschewed examination of the ostensible monopolist's actual degree of control over prices or competition, and have relied solely on statistical data concerning the accused firm's share of the market. Where that data reveals a market share of more than seventy to eighty percent, the courts have inferred the existence of monopoly power.

Such a heavy reliance on market share statistics is likely to be an inaccurate or misleading indicator of "monopoly power" in a regulated setting. In many regulated industries, each purveyor of service, regardless of absolute size, is in a monopoly position with regard to its customers. Indeed, while a regulated firm's dominant share of the market typically explains why it is subject to regulation, the firm's statistical dominance may also be the result of regulation. See *United States v. Marine Bancorporation*, 418 U.S. at 633. For these reasons, the size of a regulated company's market share should constitute, at most, a point of departure in assessing the existence of monopoly power. Ultimately, that analysis must focus directly on the ability of the regulated company to control prices or exclude competition — an assessment which, in turn, requires close scrutiny of the regulatory scheme in question.⁶⁴

As the Seventh Circuit stated, the problem with the traditional market share analysis in the context of a natural monopoly is that "while a regulated firm's dominant share of the market typically explains *why* it is subject to regulation, the firm's statistical dominance may also be the *result* of regulation."⁶⁵ In effect, the problem with the traditional market share analysis was that the uncertainty in the obligation to deal necessarily was improperly resolved against the regulated company. For example, the factual question of the relevant geographic market for retail sales was often found to be the regulated company's service area⁶⁶ and in this relevant market the regulated company almost always possesses a sufficient market share to support an inference of monopoly power. Thus, compliance with regulation, *i.e.*, an obligation to serve at retail, would create a large market share but would not necessarily reflect the company's power to control prices or exclude competitors from this market, which is the true character of monopoly power.

In lieu of the traditional market share analysis, the Seventh Circuit held that "the analysis [of whether AT&T possesses monopoly power] must focus directly on the ability of the regulated company to control prices or exclude competition."⁶⁷

⁶⁴*Id.* at 1106-07 (footnote omitted).

⁶⁵*Id.* at 1107.

⁶⁶Indeed, in *Borough of Lansdale v. Philadelphia Electric Co.*, 692 F.2d 307 (3d Cir. 1982), plaintiffs argued that the relevant geographic market for both retail and wholesale sales was identical to defendant's service area as a matter of law. The court rejected this argument and held that:

The definition of the relevant geographic market, therefore, is a question of fact to be determined in the context of each case in acknowledgment of the commercial realities of the industry under consideration. We are not persuaded that the electric utility industry has distinguishing characteristics that would allow us to short-circuit the fact-finder's function.

692 F.2d at 311 (citation omitted).

⁶⁷*MCI Communications Corp. v. American Telephone and Telegraph Co.*, 708 F.2d at 1107.

Thus, in cases involving a refusal to deal by regulated companies which operate as natural monopolies, the Seventh Circuit returned to the method of proof required in antitrust cases from an earlier era, *i.e.*, direct evidence of the power to control prices or exclude competitors.

C. Development of the Essential Facilities Doctrine to Determine the Ability of A Regulated Company to Control Prices or Exclude Competition

Having questioned the reliability of the traditional market share analysis as a basis to infer possession of monopoly power, a need arose for a framework to demonstrate direct evidence of monopoly power, *i.e.*, evidence of the ability to control prices or exclude competition. The courts turned to the essential facilities doctrine.

The essential facilities doctrine provides that a company in possession or control of an "essential" facility must provide its competitors with reasonable access to this facility.⁶⁸ Accordingly, a refusal to provide reasonable access to the essential facility is a violation of Section 2.

Application of the essential facilities doctrine poses an obvious question: What are the relevant criteria to determine whether a facility is "essential"? The cases arising in a nonregulated setting do not provide much substantive guidance. For example, the Court of Appeals for the District of Columbia Circuit has ruled that a facility is deemed to be essential "if duplication of the facility would be economically infeasible and if denial of its use inflicts a severe handicap on potential market entrants."⁶⁹ The theory is that possession of a facility which is necessary to enter a market and which cannot be economically duplicated by the potential entrant provides the "ability to exclude competitors" and, thus, is evidence of the possession of monopoly power. The court did not, however, provide any objective cost-based standard to determine whether a facility could be economically duplicated by a potential market entrant.

The essential facilities doctrine was not developed in the regulated context. It was first applied to a railroad bridge,⁷⁰ and was subsequently applied to warehouse space,⁷¹ to an allotment of selling time,⁷² and to a sports stadium.⁷³ It is appropriate, however, that it should find its greatest application in the regulated context because natural monopoly services often involve facilities which could not be economically duplicated by another market entrant.

In four recent antitrust cases involving refusals to deal by regulated utilities, the courts have applied the essential facilities doctrine. A review of these cases

⁶⁸There is some question whether the essential facilities doctrine should apply if the essential facility is owned by one company rather than by a group of companies or if it should apply with the same force. The Sixth Circuit has stated that "there may indeed be significant considerations of fairness and efficiency where a single innovative firm builds or obtains a unique facility." *Byars v. Bluff City News Co.*, 609 F.2d at 856 n.33. The Seventh Circuit, however, has ruled that the essential facilities doctrine does apply even if the purported essential facility is owned by a single firm. *MCI Communications Corp. v. American Telephone and Telegraph Co.*, 708 F.2d at 1147 n. 100.

⁶⁹*Hecht v. Pro-Football, Inc.*, 570 F.2d 982, 992 (D.C. Cir. 1977), *cert. denied*, 436 U.S. 956 (1978) (footnote omitted).

⁷⁰*United States v. Terminal Railroad Ass'n.*, 224 U.S. 383 (1911).

⁷¹*Gamco, Inc. v. Providence Fruit & Produce Bldg.*, 194 F.2d 484 (1st Cir.), *cert. denied*, 344 U.S. 817 (1952).

⁷²*American Federation of Tobacco Growers v. Neal*, 183 F.2d 869 (4th Cir. 1950).

⁷³*Hecht v. Pro-Football, Inc.*, 570 F.2d 892 (D.C. Cir. 1977).

demonstrates the courts' difficulty in attempting to develop a reasonable doctrine for testing refusals to deal by regulated companies.

*Town of Massena v. Niagara Mohawk Power Co.*⁷⁴ concerned a conditional refusal to wheel wholesale power by Niagara Mohawk Power Company (Niagara Mohawk) to the Town of Massena (Massena). Massena had recently condemned Niagara Mohawk's local distribution facilities for the purpose of operating a municipal electric distribution system and had made arrangements to purchase wholesale power from The Power Authority of the State of New York (PASNY). Because PASNY had no transmission facilities, Massena requested Niagara Mohawk to wheel the PASNY power to Massena.⁷⁵ Niagara Mohawk refused to wheel until Massena agreed to arrangements for severance of the borderline feeders to Massena, to condemnation of certain substations used in providing service to Massena, and to compensation for the additional capacity necessary for Niagara Mohawk to maintain a second delivery point to Massena.

Following the same path as the trial court in *Otter Tail*, the trial court found, pursuant to a market share analysis, that Niagara Mohawk possessed monopoly power in the retail market; that Niagara Mohawk's transmission lines were an essential facility; and, that Niagara Mohawk's control of this essential facility provided it with the power to exclude competition for the retail distribution franchise in Massena.⁷⁶ In effect, the court found that Niagara Mohawk's control over transmission enabled it to exclude competitors for the franchise to serve Massena at retail and, thus, was direct evidence of its monopoly power in the market for wholesale power:

The primary requisite to a finding of monopolization is the possession of monopoly power, *i.e.*, the power to control prices or exclude competition. Niagara-Mohawk's ability to control prices is, of course, regulated by the Federal Energy Regulatory Commission and The New York Public Service Commission. Nevertheless, the proof has shown that the Company's control of the transmission market gives it power to exclude potential competitors.⁷⁷

Thus, the Court applied the essential facilities doctrine to conclude that Niagara Mohawk possessed monopoly power in the market to provide retail service in Massena pursuant to franchise, *i.e.*, the power to exclude competitive sellers of wholesale power to Massena.

In addition to proof of monopoly power, a finding of monopolization in violation of Section 2 also requires proof of abuse of monopoly power, the second element of monopolization. The trial court held that an anticompetitive intent, in satisfaction of the abuse element, should not be inferred simply from success in precluding market entry in cases involving natural monopolies.⁷⁸ Because the competition at issue was franchise competition, which is competition for a natural monopoly service, the court ruled that Niagara Mohawk's conditional refusal to wheel wholesale power, although excluding competitors for the franchise to serve Massena, did not alone satisfy the intent element of a Section 2 violation. In fact, upon reviewing the evidence, the court found that Niagara Mohawk's refusal to wheel until Massena agreed to proper condemnation arrangements was based upon legitimate business reasons and was not motivated by any anticompetitive purpose. Accordingly, the Court found no violation of Section 2.

⁷⁴1980-2 Trade Cas. ¶ 63,526 (N.D. N.Y. 1980).

⁷⁵Massena had, at first, intended to construct its own transmission line to PASNY's hydroelectric facility.

⁷⁶1980-2 Trade Cas. at 76,802.

⁷⁷*Id.* at 76,821 (citations omitted)

⁷⁸*Id.* at 76,803.

Apart from the ultimate result, this case is important for the analysis, or lack of analysis, applied by the court in finding that Niagara Mohawk's transmission lines were an essential facility. The trial court did not perform any significant analysis; specifically, the court concluded that construction of a transmission line to an alternative supplier of wholesale power was impractical because the cost of constructing such a line, when added to the cost of purchasing Niagara Mohawk's distribution facilities, would preclude Massena from providing competitive retail service, *i.e.*, passing a rate savings to its consumers.⁷⁹ The trial court, noting the language of cases applying the essential facilities doctrine to non-regulated companies, concluded that "these elements [facility cannot be practically duplicated] are present in this case and Niagara Mohawk's transmission network can easily be characterized as an 'essential facility,' vis-a-vis Massena's attempt to enter the retail distribution market."⁸⁰

Borough of Lansdale v. Philadelphia Electric Co.,⁸¹ concerned, *inter alia*, a refusal by Philadelphia Electric Company (Philadelphia Electric) to wheel wholesale power to the Borough of Lansdale (Lansdale), which is the only municipality operating an electric distribution system in Philadelphia Electric's service area. Since 1972, Lansdale had purchased its full requirements from Philadelphia Electric, but in 1977 Lansdale requested Philadelphia Electric to wheel wholesale power from an alternative supplier. Philadelphia Electric declined this request⁸² and Lansdale brought an action under the antitrust laws.

The parties agreed that two product markets were at issue: retail sales and wholesale sales. The relevant geographic market, however, was disputed. Lansdale contended that the relevant geographic market for wholesale sales was Philadelphia Electric's service area because it was impractical for Philadelphia Electric's wholesale customers to construct transmission lines to an alternative wholesale supplier. Under a traditional market share analysis, Philadelphia Electric's market share in this relevant geographic market would almost certainly have supported an inference of monopoly power over wholesale sales.

In contrast, Philadelphia Electric argued that the relevant geographic market for wholesale sales was much larger, *i.e.*, the market included Philadelphia Electric and seven nearby utilities, because these alternative suppliers could be available through municipally constructed transmission lines. In support of this argument, Philadelphia Electric presented evidence that construction of a transmission line from Lansdale would be cheaper than wheeling and that the wholesale power rates of the other utilities were more favorable than Philadelphia Electric's rate.⁸³ Under a traditional market share analysis, Philadelphia Electric's market share in this relevant geographic market would almost certainly *not* have supported an inference of monopoly power over wholesale sales.

The dispute went to the jury, which found that Philadelphia Electric did *not* possess monopoly power in the wholesale market. In effect, the jury, in determining the relevant geographic market, was allowed to find as a question of

⁷⁹*Id.* at 76,801.

⁸⁰*Id.* at 76,812 n.41.

⁸¹692 F.2d 307 (3d Cir. 1982).

⁸²Philadelphia Electric agreed to wheel unit power, *i.e.*, "power from a generating facility in which Lansdale was part owner."

²Defendant's expert, Dr. John Lannon, testified that defendant had "taken the position that if Lansdale goes into the electric business and . . . builds or purchases an interest in its own generation . . . the Philadelphia Electric Company will wheel for the Borough"

Id. at 309. Lansdale had generation within the city, but had not operated it since 1972.

⁸³*Id.* at 312-13.

fact whether Philadelphia Electric's transmission system was an essential facility which provided Philadelphia Electric with monopoly power over the sale of wholesale power to Lansdale. As guidance in resolving this factual question, the trial court allowed the jury, *inter alia*, to compare the construction cost of an alternative line to the cost of wheeling by Philadelphia Electric.

Lansdale appealed and the Third Circuit affirmed the jury's finding of the absence of monopoly power, which could be based on several different theories, in language which indicated that the absence of monopoly power was based on the inability to exclude competitors from the wholesale market rather than on a market share analysis: "[A] jury could reasonably conclude that Philadelphia Electric lacked the physical power to exclude wholesale competitors from its service area [E]ven were we to conclude that the jury accepted Lansdale's definition of the relevant geographic market, we could not hold its finding of lack of monopoly power to be unsupported."⁸⁴ Thus, the Third Circuit relied on the essential facilities doctrine to determine whether Philadelphia Electric possessed monopoly power in the wholesale market.

Lansdale also alleged that Philadelphia Electric had monopolized the retail market. The Third Circuit, however, found that whether Philadelphia Electric possessed monopoly power in the retail market was irrelevant.⁸⁵ In effect, the court concluded that only the wholesale power market was at issue in the context of a refusal to wheel wholesale power. Thus, the court rejected as irrelevant the market in which the traditional market share analysis had continued to be used in some fashion in *Otter Tail* and *Massena*. This finding is appropriate because it reflects the fact that the competition at issue in a request to wheel full requirements wholesale power is competition to serve the franchise area at retail. This competition takes place in the wholesale market because it is competition among suppliers to sell wholesale power to Lansdale. Thus, it is the ability to exclude wholesale competitors — and not any measure of Philadelphia Electric's "market power" in the retail market — that is relevant.

City of Chanute v. Kansas Gas & Electric Company,⁸⁶ also involved a conditional refusal to wheel wholesale power. Two municipal wholesale customers of Kansas Gas and Electric Company (KG&E) had obtained a small allotment of SEPA power and had requested KG&E to wheel this power. A third municipal wholesale customer had purchased unit power in a remote generating facility and also had requested KG&E to wheel this power. KG&E allegedly refused to wheel except on condition that the three municipalities modify their present wholesale power contracts with KG&E. The three municipalities subsequently brought an action against KG&E, alleging a refusal to wheel in violation of the antitrust laws, and requested damages and injunctive relief.

At an early stage in the proceedings, the three municipalities filed a motion for a preliminary injunction compelling KG&E to wheel the power at issue. The trial court, in granting the preliminary injunction, found that the municipalities had carried their burden of proof as to probable success on the merits. Specifically, the trial court held that they had made a more compelling case for monopoly power in the transmission services market under the bottleneck theory than under the traditional market share analysis.⁸⁷

The municipalities' evidence, supporting the trial court's finding that they had raised "more than a substantial question as to KG&E's monopoly power over

⁸⁴*Id.* at 313-14.

⁸⁵*Id.* at 312.

⁸⁶564 F. Supp. 1416 (D. Kan. 1983), *appeal docketed*, No. 83-1818 (10th Cir. 1983).

⁸⁷*Id.* at 1422.

transmission facilities,"⁸⁸ was principally an assertion that the cost to wheel power over KG&E's transmission lines was less than the cost of constructing a transmission line to an alternative supplier.⁸⁹ This comparison, then, was apparently adopted by the trial court as the standard for determining whether KG&E's transmission system was an essential facility, in the context of requests to wheel wholesale power to these municipalities.

It is also important to note that the municipalities were not requesting KG&E to wheel full requirements wholesale power, but relatively small allotments of wholesale power.⁹⁰ Thus, the municipalities' estimate of construction costs, measured in cents per Kwh, reflected a very limited use of the available transmission capacity of the proposed alternative line over its lifetime.

In *MCI Communications Corp. v. American Telephone and Telegraph Co.*,⁹¹ one issue before the court was whether AT&T's local telephone lines were essential facilities to which MCI needed access in order to compete with AT&T in providing long distance phone services. The Seventh Circuit identified four elements of the essential facilities doctrine:

The case law sets forth four elements necessary to establish liability under the essential facilities doctrine: (1) control of the essential facility by a monopolist; (2) a competitor's inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility.⁹²

Without any objective analysis, the court concluded that AT&T's distribution lines were an essential facility for MCI to offer long distance service:

AT&T had control over the local distribution facilities that MCI required. The interconnections were essential for MCI to offer FX and CCSA service [long distance phone service]. The facilities in question met the criteria of "essential facilities" in that MCI could not duplicate Bell's local facilities. Given present technology, local telephone service is generally regarded as a natural monopoly and is regulated as such. It would not be economically feasible for MCI to duplicate Bell's local distribution facilities (involving millions of miles of cables and lines to individual homes and businesses), and regulatory authorization could not be obtained for such an uneconomical duplication.⁹³

The Seventh Circuit specifically rejected AT&T's arguments that MCI had presented no evidence to support a finding that these facilities were essential and that the trial court had provided no guidance to the jury on what constituted an

⁸⁸*Id.*

⁸⁹See testimony of plaintiffs' witness Mr. Bernstein at hearing on May 13, 1983, especially Vol. II at 117.

⁹⁰In fact, this power may not be technically wholesale power if title to the power is transferred to the municipalities at the generating facility.

⁹¹708 F.2d 1081 (7th Cir. 1983).

⁹²*Id.* at 1132-33. The first element, "control of an essential facility by a monopolist", suggests that the essential facility doctrine should be used only to determine abuse of monopoly power rather than to determine possession of monopoly power. Other portions of the opinion, however, indicate that the court relied on its finding that AT&T's local systems were an essential facility to conclude that AT&T possessed monopoly power in this market and attempted, by refusing to provide interconnections, to extend this monopoly power into the competitive market for long distance service:

Such a refusal may be unlawful because a monopolist's control of an essential facility (sometimes called a "bottleneck") can extend its monopoly power from one stage of production to another, and from one market into another.

Id. at 1132. The court also noted with approval the trial court's instruction that "essential facilities doctrine is applicable where 'a business holds a monopoly over an essential facility that other businesses need in order to compete' . . ." *Id.* at 1146 n. 98.

⁹³*Id.* at 1133.

essential facility. In particular, the court held that the elements of the doctrine provided the jury with adequate instruction because, *inter alia*, "essential" is a term of ordinary meaning.⁹⁴

These four cases indicate that the courts are foregoing a market share analysis and are relying, in its place, on the essential facilities doctrine to establish monopoly power in the context of refusals to deal by regulated companies operating as natural monopolies. The courts have not, however, provided objective guidelines for the requisite proof to establish that a facility is essential and the cases suggest that such proof may almost be assumed. As to the second element of monopolization — abuse of monopoly power — the burden of proving specific intent to monopolize has been shifted to the defendant under the guise of showing a legitimate business reason.⁹⁵ In summary, the courts' development of the essential facilities doctrine has not been entirely satisfactory because it has not solved the problem which prompted the courts to question the reliability of a market share analysis, *i.e.*, an almost *per se* finding of the possession of monopoly power by regulated companies operating as natural monopolies.

D. *Estimating Actual and Minimum Entry Costs for the Purpose of Determining Whether a Transmission System is an Essential Facility in the Context of Franchise Competition*

In the non-regulated setting, the basic character of an essential facility — that it cannot be economically duplicated by a competitor — is appropriate for determining whether a facility is essential. In the regulated setting, however, this criterion may be misleading. For example, in *MCI Communications Corp. v. American Telephone & Telegraph Co.*, a purported essential facility was AT&T's local distribution phone lines. MCI alleged that it needed access to this facility, not to displace AT&T's local service, but to compete with AT&T for long distance service. The crucial point is that MCI's purpose potentially required access to every customer connected to AT&T's local phone systems. In this context, whether duplication of the entire facility is economic may be an appropriate criterion to determine if the facility is essential. Moreover, in this context, a jury may be competent to make a finding of "essential" facility without any further guidance.

In contrast, in the context of a request to wheel wholesale power by a competitor in the market to serve a particular franchise at retail,⁹⁶ to ask whether the purported essential facility, *i.e.*, the utility's entire transmission system, can be economically duplicated is inappropriate. The problem posed in this context is *access* by the franchise holder to an alternative wholesale supplier. Such access may be provided by wheeling, which utilizes in some limited fashion the utility's entire transmission

⁹⁴*Id.* at 1147 n.98.

⁹⁵The theoretical justification is that a valid business purpose can offset a finding of monopolistic intent." *Byars v. Bluff City News Co.*, 609 F.2d at 862 n.53.

⁹⁶The following discussion of objective cost standards to determine whether a transmission system is an essential facility is in the context of a request to wheel wholesale power to an electric distribution system providing or attempting to provide retail service within a single long term franchise. In this context, the competition between the utility controlling the purported essential facility and the party making the request for wheeling is franchise competition. This competition was, of course, the competition at issue in *Town of Massena v. Niagara Mohawk, Borough of Lansdale v. Philadelphia Electric Co.*, and *City of Chanute v. Kansas Gas and Electric Company*.

It is appropriate to focus on the specific competition placed into issue by a request for wheeling in determining whether a facility is essential, because an obligation to wheel under the essential facilities doctrine runs to competitors. Thus, a facility may be essential as to some form of competition but not for others. For example, whether a transmission system is an essential facility as to requests by alternative wholesale suppliers to wheel supplemental short-term wholesale power does not address franchise competition but another form of competition.

system. A reasonable businessman would not, however, duplicate this entire transmission system simply to obtain access to another supplier; he would construct a new line to the transmission system of the nearest alternative supplier. Therefore, it is inappropriate to ask whether a utility's entire transmission system could be economically duplicated and to conclude from the readily obtained "no" answer that it is an essential facility imposing an obligation to wheel wholesale power.

The courts have recognized this distinction, although not expressly. For example, the courts in *Town of Massena v. Niagara Mohawk Power Corp.*, *Borough of Lansdale v. Philadelphia Electric Co.*, and *City of Chanute v. Kansas Gas and Electric Company*, did not simply ask, as the court did in *MCI Communications Corp. v. American Telephone and Telegraph Co.*, whether the purported essential facility could be economically duplicated. Instead, the courts in *Borough of Lansdale v. Philadelphia Electric Co.* and *City of Chanute v. Kansas Gas and Electric Company*, chose to compare the current cost of constructing a new line providing access to an alternative supplier with the cost of wheeling over the existing facility. The court, in *Town of Massena v. Niagara Mohawk Power Corp.*, chose to compare Niagara Mohawk's retail rates with the retail rates Massena would be able to offer if wheeling over Niagara Mohawk's transmission system was not available. Thus, the courts have recognized that some legal guidance, some objective cost-based standard, is necessary before a finding of essential facility, imposing an obligation to wheel wholesale power in the context of franchise competition, can be made. The guidance provided by the courts on this point, however, has been inadequate.

Despite its use by some courts, a simple comparison of the current cost of constructing a new line to wheeling costs over the existing facility may be inappropriate for several reasons. Most importantly, it has no logical basis. The question posed by the access problem is this: Would a reasonable businessman conclude that the market represented by the franchise for retail sales justified, over the term of the franchise, the cost of constructing a new line to obtain access to an alternative supplier? The assumption in this definition of essential facility is that the potential entrant should be expected to incur ordinary start-up costs to enter the market, including the construction costs necessary to obtain access to a supplier. Only if these start-up costs are so high as to preclude his competitive entry into the market over the long-term should the existing facility be deemed an "essential" facility.⁹⁷

The error made by the *Lansdale* and *Chanute* courts in simply comparing current construction costs to wheeling costs is that the wheeling rate over the existing facility simply has no relation to the amount of these start-up costs. The wheeling rate reflects the utility's investment in its entire transmission plant, which has been constructed over a period of time to serve many purposes, and the utility's present use of that investment in making retail and wholesale sales. Thus, the wheeling costs over the existing facility has no relation to whether the estimated retail market represented by the franchise will be sufficient to allow the potential entrant to offer a competitive service at a rate which recovers his necessary start-up costs.

The wheeling rate over the existing facility is nothing more than the reasonable cost of access, as determined by a regulatory authority, if access to this facility should

⁹⁷One commentator has proposed an objective definition for essential facility which supports this analysis. Specifically, it is proposed that a facility is essential only if, *inter alia*, "duplication of the facility is beyond the standard cost of entry into the foreclosed market." Note, *Unclogging the Bottleneck: A New Essential Facilities Doctrine*, 83 Colum. L. REV. 441, 443 (1983). In effect, it is proposed that a new entrant should expect to bear the standard costs of entry.

be made available or compelled.⁹⁸ It is not a measure of the ordinary start-up costs for entry into the market to provide retail service within the franchise. Thus, a comparison of current construction costs of a new line to the wheeling rate over the existing facility reflects a definition of "essential" which incorrectly assumes that the potential entrant should have the cheapest available access: If the current cost of construction is less than the cost of wheeling over the existing facility, then the potential entrant would certainly choose to build. If the cost of construction is greater, then this simplistic definition of essential facility would compel access to the existing facility. Contrary to the guidance suggested by the court in *MCI Communications Corp. v. American Telephone and Telegraph Co.*,⁹⁹ this definition of "essential" does not comport with the plain meaning of the word, but is closer to a definition of a "most economical facility" doctrine. Thus, this definition does not address whether the essential facility poses a competitively insurmountable entry barrier, and accordingly, is erroneous.

This conclusion is supported by another portion of the Seventh Circuit's decision in *MCI Communications Corp. v. American Telephone and Telegraph Co.* In addition to the alleged refusal to provide MCI with access to AT&T's local facilities, MCI alleged that AT&T engaged in predatory pricing of its Telpak and Hi-Lo services for long distance communications. The jury found that Telpak was lawfully priced, but found that Hi-Lo was priced below its fully distributed cost and, accordingly, its price was predatory.¹⁰⁰ AT&T appealed the trial court's instructions on predatory pricing and the jury's finding that Hi-Lo pricing was predatory and prevailed before the Seventh Circuit.

As to the jury instructions on this issue, the trial court "refused to instruct the jury as to which cost measure was the correct legal standard to determine predatory pricing. Instead [it] left the choice of a cost-based standard for predation — in this case fully distributed costs (FDC) or long-run incremental costs (LRIC) — for the jury to decide as a question of fact."¹⁰¹ The Seventh Circuit found this to be error. Specifically, the Seventh Circuit held that "the choice of a cost-based standard for evaluating claims of predatory pricing is a question of law to be decided by the trial judge."¹⁰²

The Seventh Circuit also rejected the jury's finding of predatory pricing because Hi-Lo service was priced below fully distributed cost.¹⁰³ In particular, the Seventh Circuit held that fully distributed cost "fails as an economically relevant measure of cost for antitrust purposes because it relies on historical or embedded costs. For it is current and anticipated cost, rather than historical cost that is relevant to business decisions to enter markets and price products."¹⁰⁴ The Seventh Circuit conceded that fully distributed costs had a proper role in ratemaking, *i.e.*, to determine a maximum reasonable rate, but ruled that pricing below this maximum reasonable rate was fully consistent with the goals of the antitrust laws.¹⁰⁵

⁹⁸For example, the wheeling rate which entered into the court's comparison in *City of Chanute v. Kansas Gas and Electric Co.* was the FERC approved rate.

⁹⁹708 F.2d at 1147 n.98.

¹⁰⁰*Id.* at 1111.

¹⁰¹*Id.*

¹⁰²*Id.*

¹⁰³The court reaffirmed its rule that "liability for predatory pricing must be based upon proof of pricing below cost." *Id.* at 1114. This suggests that an obligation to wheel arises only when a competitor, even if it is more efficient, cannot compete for a particular customer because the rate offered by the utility controlling the purported essential facility and determined on a rolled-in basis is subsidized by other customers.

¹⁰⁴*Id.* at 1116-17.

¹⁰⁵*Id.* at 1124.

The Seventh Circuit's finding that the proper cost-based standard for evaluating predatory pricing was a question of law suggests, in the context of a request to wheel wholesale power, that the cost-based standard for determining "essential" is a question of law and certainly should not be submitted to the jury without considerable guidance. This follows because the question of "essential" in this context is not simply whether the facility can be economically duplicated but involves an inquiry into the proper measure of costs to obtain access to an alternative supplier and, perhaps, a comparison to the costs of the existing facility.

Similarly, the Seventh Circuit's finding that fully distributed cost are not relevant to antitrust pricing considerations also suggests that wheeling costs, which are typically derived from approved rates based upon fully distributed cost, are an inappropriate cost standard for defining "essential." In particular, wheeling costs reflect the "historical" cost of the existing facility, rather than "current and anticipated costs . . . [which] are relevant to business decisions to enter markets" ¹⁰⁶ Therefore, wheeling costs do not measure acceptable market entry costs.

The courts have, perhaps, relied on evidence of the cost of wheeling over the existing facility to determine whether the facility is "essential" because it is readily available and because a cost analysis of the real question posed by the access problem is difficult. A proper cost analysis would be a complicated problem involving the cost of constructing and maintaining the proposed line, the useful life of the line, estimated retail sales and revenues under the franchise during the life of the line, and thus, estimated loading of the line, and, the estimated cost of wholesale power from alternative suppliers.

Whether the facility is determined to be essential turns on whether a reasonable businessman, weighing these factors, would be persuaded to incur these costs in expectation of receiving an acceptable rate of return on his investment. Thus, the question may be posed as whether another utility would choose, as a business decision, to construct a line, as an alternative to the purported essential facility, in order to obtain the retail franchise. For example, if the municipality presently has the franchise, then the cost of constructing a transmission line to obtain access to an alternative wholesale supplier could be factored into the municipally-set rate for retail service. The "essential" facility question would seem to be whether the resulting retail rate was "competitive" in some sense, *i.e.*, if the rate was not "competitive" then the cost of obtaining access would preclude its entry into the market (retail service under the franchise) as anything other than a captive wholesale purchaser.

Two general problems are presented by this approach. First, it is quite common for municipal rates to be set at a level which produces revenues in excess of costs for the purpose of funding other municipal functions and, thereby, reducing more obvious municipal taxes. If the present municipal rate is not cost-based, than its use as a basis for comparison would produce misleading results in this analysis.

Second, "competitive" must be given some objective meaning. Certainly, if the resulting municipal rate would be less than the retail rate if the franchise had been awarded to the utility possessing the purported essential facility, then the facility is *not* essential. To assume the reverse, *i.e.*, if the resulting municipal rate was greater than the facility necessarily is essential,¹⁰⁷ would not be warranted. The utility's retail rate is cost-based and reflects economies of scale in the operation, *inter alia*, of its

¹⁰⁶*Id.* at 1116-17.

¹⁰⁷This is apparently the test for essential facility applied by the court in *Town of Massena v. Niagara Mohawk Power Co.*

transmission system.¹⁰⁸ In contrast, the municipality's present rate may not be cost-based and may not represent efficient design or operation of the distribution system. Moreover, the resultant municipal rate probably will not reflect economies of scale in its transmission investment. A monopolist is not barred from taking advantage of economies of scale:

A firm that has lawfully acquired a monopoly position is not barred from taking advantage of scale economies by constructing, for example, a large and efficient factory.¹⁰⁹

Therefore, this advantage enjoyed by the utility owning the existing facility must be factored into the definition of "essential." For all these reasons, there should be some margin *above* the utility's retail rate which would include "competitive" rates offered by the municipal. The problem is quantification.

An improvement to the present cost-based standard of comparing construction costs to wheeling costs may be the following: If the courts choose to compare construction costs of an alternative line to wheeling costs, then the following two conditions should be incorporated to provide a *minimum* cost-based standard for "essential" facility.

First, the cost of the proposed transmission line, determined in cents per Kwh over the expected life of the line, should be based upon full utilization of the line insofar as the present and estimated load of the municipality permits. This condition is necessary to insure that the standard for determining whether a facility is "essential" measures market barriers and, thus, measures the full ability of the potential entrant to obtain wholesale power from an alternative source for the purpose of providing service under the franchise.

In practical terms, the cost of constructing a line for access to an alternative supplier, in cents per Kwh, is largely dependent upon the total amount of energy delivered over the line during its lifetime. A holder of the franchise should not be allowed to limit this amount of energy below its total requirements and, thereby, to manufacture an artificially high cents per Kwh cost for the purpose of forcing a finding that the utility's transmission system is essential and, therefore, imposing an obligation to wheel. For example, a municipality could contract to purchase a small portion of its wholesale requirements and insist, under the essential facility doctrine, that the utility to which it is interconnected wheel this power. The relevant construction cost, which measures the municipality's ability to obtain economical access to alternative suppliers, must reflect full use of the proposed line rather than limited use corresponding to the limited purchase selected by the municipality.

The point is that whether a transmission system is an essential facility should not be subject to manipulation by the municipality in selecting the amount of its purchase from an alternative supplier. This condition, imputing the full requirements of the franchise area as the load on the line in calculating the cost per Kwh for construction of the line providing access to an alternative supplier, will preclude such manipulation.

Second, this current cost of construction of an alternative line should not be compared to actual wheeling costs which reflect embedded costs, but to wheeling costs produced by a rate designed in accordance with a replacement cost methodology. A comparison to such wheeling costs is consistent with the Seventh

¹⁰⁸Such economies of scale do exist. *Otter Tail Power Co. v. United States*, 410 U.S. at 384 (Stewart, J., dissenting).

¹⁰⁹*Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 274 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980).

Circuit's finding that "it is current cost . . . , rather than historical cost that is relevant to business decisions to enter markets . . . ,"¹¹⁰ and should be used if wheeling costs are to be considered as an estimate of actual entry costs.

A comparison of construction costs to wheeling costs that incorporates these two conditions, although not addressing the real question posed by the problem of access, does provide an objective cost standard for determining whether a facility is essential in the context of franchise competition and provides a minimum amount of protection to utilities against the unwarranted imposition of obligations to wheel. The alternative is no test at all, because the embedded costs reflected in the actual wheeling rate will almost always, when compared to current construction costs of a alternative line, insure a finding of essential facility.

E. Application of the Essential Facilities Doctrine in the Context of Requests to Wheel By Alternative Suppliers of Wholesale Power

A request to wheel wholesale power by an actual or potential competitor in the market to serve a particular franchise has, of course, another side: the corresponding request to wheel by the alternative supplier of wholesale power.¹¹¹ The competition between an alternative supplier and the utility controlling the purported essential facility is competition to provide a whole range of wholesale services — not only full requirements service but other supplemental wholesale services including short-term sales. Thus, the competition between an alternative supplier and the utility controlling the purported essential facility is different from the competition between this utility and a municipal electric distribution system to provide retail service pursuant to a franchise.

As discussed, an obligation to wheel under the essential facilities doctrine runs to competitors. Thus, the standard to determine whether a facility is "essential" must incorporate the particular competition placed into issue by the request. (In a sense, this simply means that the concept of the relevant product market plays a role in the essential facilities doctrine.)

Also, as discussed, the definition of the relevant geographic market, within which the possession of monopoly power is to be determined, depends upon the competition at issue. Thus, the scope of the relevant geographic market will vary with the competition at issue.

The effect of these two considerations in applying the essential facilities doctrine is more easily demonstrated by assuming a definite, although general, situation: Assume (1) that Company A controls the purported essential facility, *i.e.*, the potential wholesale purchaser (City M) is located within Company A's service area; (2) that Company A's service territory is surrounded by the service territories of four utilities, Companies B, C, D, and E; (3) that Company B is the alternative supplier requesting Company A to wheel wholesale power to City M; (4) that the nearest alternative supplier to City M is Company C and not Company B; and (5) that Company B's service area is surrounded by the service areas of four utilities, Companies A, C, E, and Y.

In the context of franchise competition between City M and Company A, the essential facilities question is whether it is economical for City M to construct a line to Company C which will provide its full requirements. In contrast, in the context of competition between Company A and Company B to provide full requirements

¹¹⁰444 U.S. at 1117.

¹¹¹In this discussion, it will be assumed that the alternative supplier is *not* located within the service area of the utility controlling the purported essential facility. The special problems which are posed by a "captive" alternative supplier are discussed below.

wholesale power to City M, the essential facilities doctrine would *seem* to suggest that the question is whether it is economical to construct a line from Company B to City M for the purpose of providing City M's full requirements. Because this line would be longer, this analysis would suggest a greater possibility that Company A's transmission system is an essential facility if the alternative supplier is Company B rather than Company C.¹¹²

This analysis, however, would be incomplete because it fails to account for the relevant geographic market. In the context of franchise competition, the relevant geographic market was the franchise area. For this reason, consideration of the relevant geographic market played no role in applying the essential facilities doctrine to franchise competition. In the context of competition between alternative wholesale suppliers, however, the relevant geographic market plays a crucial role.¹¹³

As discussed above, the relevant geographic market is defined, in part, as the area in which the seller could reasonably be expected to market its product. The chief limitations on the seller's marketing of power are those associated with transportation of the product, either in the form of transmission charges or line losses. In the situation we have posed, Company B wants to market wholesale power to purchasers in Company A's service area. It follows that Company B should reasonably expect to market its wholesale power to purchasers located within the service area of any utility which is adjacent to Company B's area, *i.e.*, Companies A, C, E, and Y. Thus, the relevant geographic market is the combined service area of Companies A, B, C, E, and Y.

It must be emphasized that the essential facilities doctrine provides an analysis for establishing monopoly power *within* the confines of the relevant market concept. The essential facilities doctrine is a more reliable alternative in regulated markets to the analysis which infers monopoly power from market share. However, application of the essential facilities doctrine to find monopoly power must still be determined in the proper relevant product market and relevant geographic market. This follows because only in relation to the proper relevant market does monopoly power have any anticompetitive significance.

The question becomes: Does Company A's control of its transmission system provide it with monopoly power in this relevant geographic market. An analysis of two cases suggests that Company A's ability to foreclose Company B from a portion of the relevant geographic market does not impose an obligation to wheel upon Company A.

In *American Football League v. National Football League*,¹¹⁴ the American Football League (AFL) contended, *inter alia*, that there were only 31 metropolitan areas within the United States capable of supporting a professional football team and that the National Football League's (NFL) possession of franchises in eleven of these cities provided it with monopoly power, thereby limiting the AFL's ability to operate successfully. The Fourth Circuit found that a professional football team, once

¹¹²Company A and Company C may compete to provide other supplemental wholesale services to City M, for example, limited amounts of short-term wholesale power.

The standard for determining whether a facility is essential must be changed to reflect this different competition. Specifically, for limited amounts of power over short durations, the cost per Kwh of the alternative line would be much greater than for competition to provide full requirements service over the duration of the franchise. Thus, for this competition, it would seem to be more likely that Company A's transmission system was an essential facility.

¹¹³In a sense, this can be seen because the essential facilities question posed by franchise competition and by competition to provide full requirements wholesale power would be the same if Company C provided wheeling to Company B. Thus, Company B's access to the transmission systems of utilities other than Company A is placed into issue by this competition.

¹¹⁴323 F.2d 124 (4th Cir. 1963).

located, generally enjoys a natural monopoly.¹¹⁵ Although choosing to concentrate on competition between the leagues for franchise locations, the court found the relevant market to be nationwide rather than the aggregate of these sites. The court ruled, however, that possession of the natural monopoly sites would bear upon the NFL's possession of monopoly power in this market:

The relevant market is nationwide, though the fact that there are a limited number of desirable sites for team locations bears upon the question of [the NFL's] power to monopolize the national market.¹¹⁶

The Fourth Circuit affirmed the district court's "plainly correct" finding that the NFL did not have the power to monopolize the relevant market.¹¹⁷ In so ruling, the Fourth Circuit noted that 20 of the 31 desirable sites were entirely open to the AFL¹¹⁸ and concluded that the evidence did not require a finding that the NFL "had it wished, could have placed a team in every location sought by [the AFL], or in a sufficient number of them to have destroyed the league."¹¹⁹

In effect, the Fourth Circuit found that the NFL, by reason of its existing franchises which operated as natural monopolies, could foreclose the AFL from a portion of the relevant geographic market, but did not foreclose a sufficiently large portion to prevent the AFL from successfully entering the market.

In the situation we have posed, Company A's transmission system may be a natural monopoly. The essential facilities doctrine, if applied to the area defined as Company A's service territory, may produce a finding that Company A's transmission system is an essential facility. However, applying the doctrine to the entire relevant geographic market, Company A's ability to exclude Company B from competing for wholesale sales in this portion of the relevant geographic market does not support a finding that Company A has monopoly power, *i.e.*, the power to exclude Company B from successfully entering the relevant geographic market. In short, Company A has no control whatsoever over Company B's ability to sell wholesale power in the other portions of the relevant geographic market — the service area of Companies B, C, E, and Y.

In apparent contrast is *Hecht v. Pro-Football, Inc.*¹²⁰ Plaintiffs were a group of promoters who unsuccessfully sought to obtain an American Football League franchise for the Washington, D.C. area. Defendants were the owners of the Washington Redskins, the National Football League franchise in the Washington, D.C. area, and the owners of the local stadium. Plaintiffs alleged that they were unable to obtain a franchise because a contract governing the use of the only stadium in the area prevented the use of the stadium by any football team other than the Redskins.

It was undisputed that the relevant product market was professional football. The relevant geographic market, however, was disputed. Plaintiffs contended that the relevant geographic market was the Washington, D.C. area and defendants contended that the relevant geographic market was the nation as a whole.

The Court of Appeals, reversing the trial court's instruction that the relevant geographic market was nationwide, held that the relevant geographic market was the Washington, D.C. metropolitan area and further held that the trial court erred

¹¹⁵*Id.* at 130. A few larger cities could, and did, support two teams.

¹¹⁶*Id.*

¹¹⁷*Id.*

¹¹⁸*Id.* at 131.

¹¹⁹*Id.*

¹²⁰570 F.2d 982 (D.C. Cir. 1977), *cert. denied*, 426 U.S. 956 (1978).

in failing to give defendants' jury instructions concerning the essential facilities doctrine as it applied to the stadium.¹²¹ In so holding, the court distinguished *American Football League v. National Football League*, in which a nationwide relevant market had been found:

Defendants' citation of *American Football League v. National Football League*, 323 F.2d 124 (4th Cir. 1963), is inapposite. That case concerned the "competition between the leagues for franchise locations;" since each league was considering expansion to a host of desirable sites, the court properly held that the market, geographically, was "at least as broad as the United States, including Hawaii and portions of Canada." 323 F.2d at 130. This case, by contrast, concerns the potential competition between two teams for customers in one location. Unlike the NFL, the Redskins as "sellers" do not operate nationally; unlike the AFL, Hecht is not trying to expand nationally. He sought merely to compete with the Redskins on their home turf.¹²²

Thus, the court's determination that the relevant geographic market was a single city rather than the entire nation was based on its finding that Hecht intended to compete only in the Washington, D.C. area while the AFL intended to compete for franchises in a number of desirable locations.

In the situation we have posed, it could not reasonably be concluded that Company B intended to compete for wholesale sales only in Company A's service area. The service areas of Companies C, E, and Y are equally accessible to Company B and there is no reason for Company B to distinguish Company A's service territory for the territories of Companies C, E, or Y. For this reason, the relevant geographic market cannot be limited to Company A's service area and, thus, Company A's ability to exclude Company B from a portion of the relevant geographic market does not establish Company A's possession of monopoly power in this market.¹²³ Accordingly, in the context of this competition, Company A has no obligation to wheel for Company B.¹²⁴

It should be noted that this conclusion is consistent with the courts' unexplained focus on the point of view of the potential wholesale purchaser rather than the potential alternative wholesale supplier in applying the essential facilities doctrine. If this conclusion were not correct and the geographic market comprised only the service area of the company controlling the purported essential facility, then it would have been a simple matter to identify a remote alternative supplier and force a finding that the utility controlling the purported essential facility had an obligation to *this supplier* to wheel, rather than address the more difficult question of whether the utility has an obligation to the *potential buyer* to wheel.

F. *Special Problems Posed By an Alternative Supplier Located Within the Service Area of the Utility Controlling the Purported Essential Facility*

One assumption in the situation posed above was that the alternative supplier was not located within the service area of the utility controlling the essential facility. The contrary assumption, that the alternative supplier is interconnected only with the utility controlling the purported essential facility, is possible¹²⁵ and poses separate problems.

¹²¹*Id.* at 992.

¹²²*Id.* at 989 n.20.

¹²³This is, of course, a factual question in each case. Except in unusual circumstances, however, the portion of the market foreclosed will be significantly less than 50%.

¹²⁴This conclusion applies to all wholesale power sales — full requirements or any supplemental sales. The reason is that the relevant geographic market analysis does not vary with these different products.

¹²⁵Ordinarily, it will be a municipality desiring to market its excess generating capacity.

For purposes of discussion, let us assume that (1) Company A controls the purported essential facility; (2) City B is interconnected only with Company A; (3) Company A is surrounded by the service areas of Companies C, D, E, and F; (4) City B wishes to sell wholesale power to City M which is located wholly within Company A's service territory; and (5) City B also wishes to sell wholesale power to City N, which is located in Company C's service territory.

The competition between Company A and City B is the same as in the previous example; they potentially compete to sell all wholesale service. The principal difference is in the relevant geographic market.

First, as to City B's request that Company A wheel power to City M, the relevant geographic market, unlike the previous example, is not necessarily any larger than Company A's service area.¹²⁶ In this event, the relevant geographic market is a question of fact and, if found to be Company A's service area, then the question posed by the essential facilities doctrine is whether it is economically feasible for City B to construct a line to City M. If it is not economically feasible, then Company A's transmission system is an essential facility providing Company A with monopoly power in this market for wholesale services.

The analysis which should be applied to determine whether the transmission system is "essential" is in principal the same analysis which was applied in the section addressing franchise competition. The fact that Company A and City B compete to sell products in addition to full requirements wholesale service will, however, complicate the analysis. For example, Company A and City B could compete for short-term sales. This product would radically change the cost per Kwh of the construction cost of an alternative line because such costs could not be properly amortized over a long period. In brief, the possibility of competition for other supplemental wholesale services would seem to increase the likelihood that Company A's transmission system will be found to be an essential facility.

Second, as to City B's request that Company A wheel power to City N, the relevant geographic market necessarily includes at least the service area of Companies A, C, D, E and F. This follows because City B's request indicates an intention to compete in the service area of the companies adjacent to Company A.

It does not follow, however, as it did in the preceding section, that Company A does not possess monopoly power in this relevant geographic market. Because City B is interconnected only with Company A, Company A's control of its transmission system governs City B's access to the entire relevant geographic market and not just a portion of it.

The essential facilities problem, then, is access by City B to an alternative system, *i.e.*, whether it is economically feasible for City B to construct a line to the nearest alternative system. This problem poses the same cost standard as discussed above for determining whether Company A's transmission system is an essential facility.

Assuming, as is quite likely in this context, that Company A's transmission system is an essential facility, it does not necessarily follow that Company A has an obligation to wheel. Company A would possess monopoly power, but a finding of monopolization in violation of § 2 requires the additional finding of conduct which is an abuse of monopoly power. The Seventh Circuit's decision in *MCI Communications Corp. v. American Telephone and Telegraph Co.*¹²⁷ is relevant to this point.

¹²⁶ A request to wheel unit power from a generating facility located outside Company A's service area raises the same problem: The relevant market for this power is wholly within Company A's service area. In effect, the unit power is not being marketed in any other portion of the relevant geographic market other than Company A's service area.

¹²⁷ 708 F.2d 1081 (7th Cir.), *cert. denied*, 104 S.Ct. 234 (1983).

MCI alleged that two AT&T facilities were essential. First, as discussed, MCI alleged that access to AT&T's local lines was essential for it to compete with AT&T for long distance services. Second, MCI alleged that AT&T's interconnections for multipoint service were an essential facility.

"Multipoint service described the situation where AT&T provided a private line to a customer between city A and city B, and MCI provided a private line between city B and city C. MCI sought an interconnection in city B between its own line and AT&T's line so that MCI's customer in city C could have uninterrupted service between city C and city A."¹²⁸ In requesting multipoint service, MCI in effect sought access to certain long distance facilities of AT&T for the purpose of enhancing its ability to compete with AT&T for long distance services in areas where MCI had long distance facilities in place:

MCI claimed that its ability to compete in the market for city B to city C communications was substantially impaired if it was not able to offer its customers through service over AT&T's lines to other cities which MCI did not serve itself.¹²⁹

The jury found that AT&T had denied interconnections for multipoint service to MCI with the intent to retain its monopoly. AT&T appealed this finding and the Seventh Circuit reversed.

The Seventh Circuit stated that there were two theories upon which denial of multipoint interconnections could have violated the antitrust laws. First, "the denial of multipoint interconnections could have been a violation of the antitrust laws if sufficient evidence had been presented that these were 'essential services.'"¹³⁰ The court, however, rejected this theory finding that "as a matter of law there was not sufficient evidence presented at trial to permit a finding that interconnection for multipoint service involved 'essential services.'"¹³¹ In so ruling, the court relied on the fact that MCI's business was to construct such intercity circuits. Thus, economic infeasibility had not been demonstrated:

The evidence presented did not demonstrate either that the duplication of Bell's intercity lines was economically infeasible or that the denial of access inflicted a severe handicap on market entrants. MCI's primary business was to build precisely the type of facilities to which it sought access from the Bell System.¹³²

The second possible basis for imposing antitrust liability upon AT&T for the denial of multipoint interconnection would be a determination that AT&T's actions in this respect were sufficient evidence of an intent to monopolize.¹³³ The court ruled, however, that sufficient evidence had not been presented to permit a finding that AT&T's denial of multipoint service was primarily motivated by an illegal intent to monopolize.¹³⁴ Supporting this holding was the court's finding that it was legitimate business conduct for AT&T, although a monopolist, to refuse, absent regulatory compulsion, to make its entire network available to a competitor:

¹²⁸*Id.* at 1147.

¹²⁹*Id.*

¹³⁰*Id.* at 1148.

¹³¹*Id.*

¹³²*Id.*

¹³³The court stated that the intent theory was independent from the essential facility theory. However, as noted in *Byars v. Bluff City News Co.*, 609 F.2d at 856, there are, in practice, many overlapping considerations.

¹³⁴708 F.2d at 1149.

Multipoint interconnection was the device through which MCI sought access to the full scope of AT&T's nationwide long distance network. Granting MCI multipoint interconnections would have enabled MCI to compete with AT&T for long distance traffic into areas where MCI may have made no significant capital investment. At the time in question, the FCC may or may not have intended . . . to impose upon AT&T the extraordinary obligation to fill in the gaps in its competitor's network.

* * *

Therefore, as a pure matter of antitrust law (without any regulatory component), we decline to hold AT&T liable for a refusal to make available its full nationwide network to a competitor.

The Seventh Circuit's definition of the essential facilities doctrine suggests that a finding of essential facility coupled with a simple refusal to deal proves monopolization in violation of § 2. This interpretation minimizes the importance of the conduct element in a § 2 case.

In traditional § 2 cases, once monopoly power had been established by a market share analysis, the courts had used either the essential facilities doctrine or an intent theory to establish abusive conduct.¹³⁵ In cases involving regulated industries, however, the courts have foregone the traditional market share analysis to infer monopoly power and, instead, have applied the essential facilities doctrine to find monopoly power. Monopoly power having been found under the essential facilities doctrine, too little substance is given to the conduct element of a § 2 violation if it too is satisfied by the finding that an essential facility exists. Some further evidence of anticompetitive conduct should be required.

In any event, the courts have also ruled that a legitimate business reason offsets a finding of anticompetitive intent.¹³⁶ Thus, even if a simple refusal to provide access to an essential facility satisfies the conduct element, the Seventh Circuit's discussion of anticompetitive intent may be read as identifying legitimate business reasons which will offset this finding.

The specific reasons identified by the Seventh Circuit may frequently apply to the situation we have posed, *i.e.*, a request by City B that Company A wheel wholesale power. If City B has no significant transmission system, then the wheeling requested would require Company A to make its entire transmission network available to a competitor and, specifically, would enable City B "to compete [with Company A] . . . into areas where [it] may have made no significant capital investment." According to the Seventh Circuit, a refusal to accommodate such a request would not be anticompetitive. In effect, such a refusal, even by a monopolist, would be legitimate business conduct.

This conclusion can be traced back to the essential facilities doctrine. We proposed that a potential entrant should be expected to incur ordinary start-up costs and only if the necessary start-up costs to enter a market were so high as to preclude his entry would a facility be deemed essential. In the example we have posed, City B is a potential entrant, as a *seller* in the wholesale power market but has not made any investment in transmission facilities. Thus, City B is attempting to avoid incurring any transmission-related start-up costs.¹³⁷

Finally, the conclusion that a refusal to wheel is not anticompetitive is particularly appropriate in the context of supplemental wholesale services.

¹³⁵See *Byars v. Bluff City News Co.*, 609 F.2d at 855-56.

¹³⁶*Id.* at 862 n.53.

¹³⁷Ordinary start-up costs to enter the wholesale market include transmission and generation costs. City B has found it economic to incur generation costs — indeed, it must have done so to have power to sell. It would seem to be incumbent upon City B to demonstrate that it is not equally economic to incur transmission start-up costs.

Company A does not design its transmission system for the purpose of marketing supplemental wholesale services. The capacity to make these sales is available because Company A's system is designed to utilize economies of scale in transmission. As held by the Second Circuit in *Berkey Photo, Inc. v. Eastman Kodak Co.*,¹³⁸ it is not anticompetitive for a monopolist to take advantage of scale economies present in a lawfully acquired monopoly. Thus, a refusal to wheel supplemental wholesale power to a company which has made no transmission investment is simply a refusal to make economies of scale available to a competitor. This conduct is not anticompetitive under *Berkey*.^{138.1}

In summary, a request to wheel by so-called "captive" wholesale suppliers poses difficult and unsettled questions. There are, however, in certain circumstances strong arguments that a refusal to wheel power, particularly supplemental wholesale power, is legitimate business conduct.

G. *Application of the Essential Facilities Doctrine to Requests to Wheel to Retail Customers*

In addition to requests to wheel wholesale power, utilities have received requests to wheel power to retail customers. Ordinarily these requests concern large industrial customers rather than residential customers. Thus, our discussion will focus on this retail customer class.

Application of the essential facilities doctrine to requests to wheel power to retail customers, although generally similar to application of the doctrine to requests to wheel wholesale power, raises some new issues. The competition placed into issue by a request to wheel power to retail customers is retail competition in the usual sense — it is *not* franchise competition, *i.e.*, competition for the natural monopoly market within each town for the distribution and sale of electricity.¹³⁹

The cases addressing requests to wheel wholesale power emphasize that "traditional competition at the distribution level is virtually nonexistent."¹⁴⁰ Because "in the absence of competition . . . there is no room to apply the essential facilities doctrine,"¹⁴¹ these cases suggest that there is no competition to support application of the essential facilities doctrine in the context of requests to wheel power to retail customers remote from the requesting parties service area.

This conclusion probably goes too far: there is competition, at least potential competition, between utilities to serve retail customers.¹⁴² The significance of this point, however, is that application of the essential facilities doctrine to requests to

¹³⁸ 603 F.2d 263, 274 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980).

^{138.1} It must be acknowledged that there is tension between *Berkey Photo, Inc. v. Eastman Kodak Co.* and the essential facilities doctrine. Specifically, under *Berkey Photo* a monopolistic is under no obligation to share its economies of scale with competitors. In contrast, a facility is more readily characterized as essential if it is sized to take advantage of economies of scale and the competitor seeking access to this facility is too small to justify construction of an alternative facility which would enjoy the same economies. We have attempted to defuse this tension by adopting a cost-based definition of "essential" which reflects the full economies available to both the company possessing the purported essential facility and the company requesting access to this facility.

¹³⁹ *Otter Tail Power Co. v. United States*, 410 U.S. at 369.

¹⁴⁰ *Town of Massena v. Niagara Mohawk Power Co.* 1980-2 Trade Cas. ¶ 63,526 at 76,798 (N.D.N.Y. 1980).

¹⁴¹ *MCI Communications Corp. v. American Telephone and Telegraph Co.*, 708 F.2d at 1147 n.100.

¹⁴² The Seventh Circuit, in concluding that AT&T's local phone lines were an essential facility, ruled that these local lines could not be economically duplicated and also stated that "regulatory authorization could not be obtained for such an uneconomical duplication." *MCI Communications Corp. v. American Telephone and Telegraph Co.*, 708 F.2d at 1133. Regulatory considerations also bear upon requests to wheel to retail customers. State law may preclude construction of duplicate transmission or distribution lines or state law may assign retail service areas and, thus, preclude any competition.

wheel power to retail customers, unlike requests to wheel wholesale power, need be examined only from the perspective of the potential seller.

From the perspective of a potential retail seller, there are two relevant situations. First, there is the case where the potential retail seller (City B) is located wholly outside the service area of Company A, in which the potential retail customer is located. The essential facilities analysis in this situation is the same as that applied to requests to wheel wholesale power by a remote supplier. Specifically, the relevant geographic market is necessarily sufficiently large to preclude a finding that Company A has monopoly power by reason of its ability to exclude City B from a portion of the market.

The second case is, of course, where City B is interconnected only with Company A. The essential facilities analysis is again the same as in the wholesale case. If the potential retail customer is also located within Company A's service area, then the question is whether it is economically feasible to construct a line from City B to this customer. If the potential retail customer is not located wholly within Company A's service area, the question is whether it is economically feasible to construct a line from City B to the nearest alternative system.

In the second case, it is quite likely that resolution of these factual questions will compel the conclusion that the transmission system is an essential facility. In this event, whether there is an obligation to wheel will turn upon resolution of the second element of monopolization — abuse of monopoly power.

The arguments raised above for the proposition that a simple refusal is not anticompetitive conduct apply with even greater force to requests to wheel power to retail customers. For example, assuming that the potential supplier is a municipal generation and distribution system with excess capacity (a reasonable assumption for a "captive" alternative supplier), it has constructed or purchased facilities for the purpose of providing retail service — the electric distribution facilities within the city. Thus, the local distribution facilities, its capital investment, are the same "type of facility to which it [seeks] access"¹⁴³ under the essential facilities doctrine. Moreover, a request to wheel to retail customers is intended to enable the municipality to compete for retail sales in areas remote from its franchise area, *i.e.*, where it has made "no significant capital investment."¹⁴⁴ Finally, imposing this obligation to wheel would require the utility to make its entire distribution network available to its competitor, thereby, filling in "the gaps in its competitor's network."¹⁴⁵ This suggests that it is legitimate business conduct for a monopolist to decline a request to wheel to retail customers by such an alternative supplier.

This conclusion was implicitly recognized by the court in *Town of Massena v. Niagara Mohawk Power Co.*¹⁴⁶ The court implicitly recognized that Massena's purchase of Niagara Mohawk's distribution facilities within the city was an ordinary start-up cost for Massena to obtain the franchise to provide retail service. Massena could not require Niagara Mohawk to wheel power to retail customers within the city without making this investment in distribution facilities. However, a request for wheeling to retail customers, apart from the franchise setting, makes just this request. The point is that a potential entrant into the retail market, apart from the franchise setting, should be expected to incur some start-up costs; a request to wheel to retail customers, unaccompanied by any corresponding investment, is an attempt totally to avoid such start-up costs and should not invoke an obligation to wheel.

¹⁴³*MCI Communications Corp. v. American Telephone & Telegraph Co.*, 708 F.2d 1081, 1148 (7th Cir. 1983).

¹⁴⁴*Id.* at 1149.

¹⁴⁵*Id.*

¹⁴⁶1980-2 Trade Cas. ¶ 63,526 (N.D.N.Y. 1980).

In summary, application of the essential facilities doctrine to requests to wheel to retail customers also poses difficult and unsettled questions. In certain circumstances, however, strong arguments can be made for legitimately declining to wheel.

CONCLUSION

We have attempted to demonstrate that the adoption of the essential facilities doctrine to determine possession of monopoly power may be a positive step toward more realistic analysis of refusals to deal by regulated companies. Without objective cost standards, however, to determine whether a facility is essential, this step may be counter-productive or even meaningless. Accordingly, in the context of requests to wheel, we have attempted to identify the specific competition to be protected and the proper standards for determining whether a facility is "essential".

The obligation to wheel in many circumstances is a factual question and, thus, remains uncertain. The courts will resolve the questions on a case-by-case basis. However, one area of uncertainty — the scope of legitimate business conduct suggested by *AT&T* — can be clarified by the courts and, potentially, could be resolved to limit further a utility's obligation to wheel.