FERC Reaffirms Policy for Assessing Horizontal Market Power

FERC retains existing market power analytical framework in a new order.

February 17, 2012

On February 16, the Federal Energy Regulatory Commission (FERC) issued an order that reaffirms its existing policies regarding the analysis of horizontal market power when reviewing mergers and other transactions under Section 203 of the Federal Power Act (FPA) and when assessing eligibility for market-based rate authority under FPA Section 205.[1] FERC's order terminates the proceeding it had initiated with a Notice of Inquiry in March 2011 to review the updated Horizontal Merger Guidelines issued by the U.S. Department of Justice (DOJ) and the Federal Trade Commission (FTC) in 2010 (2010 Horizontal Merger Guidelines).

Horizontal Merger Guidelines

FERC has maintained a five-step analytical framework for assessing horizontal market power in mergers and transactions under FPA Section 203 since it adopted its Merger Policy Statement in 1992. A primary focus of FERC's merger analysis is the competitive effects of a proposed transaction, which FERC analyzes using a Competitive Analysis Screen defined in Appendix A to the Merger Policy Statement. FERC's Appendix A Competitive Analysis Screen is based on the 1992 version of the DOJ/FTC Horizontal Merger Guidelines. The Competitive Analysis Screen entails the definition of product and geographic markets likely to be affected by the proposed transaction and the measurement of changes in market concentrations in the affected markets using defined Herfindahl-Hirschman Index (HHI) standards or other relevant statistical measures. FERC has applied its Appendix A analysis in numerous merger reviews.

The 2010 Horizontal Merger Guidelines deemphasize market definition and the assessment of market concentration in favor of a greater focus on price discrimination and other evidence of competitive impacts. The 2010 Horizontal Merger Guidelines also identify higher HHI levels that can trigger a presumption that a transaction poses a potential threat to competition. In addition, the guidelines provide for the use of a range of analytical tools and evidence to review proposed transactions and less reliance on quantitative measures. The 2010 Horizontal Merger Guidelines were met with mixed reviews, with some commenters criticizing the guidelines for being unclear about where to begin the analysis of

1. *Analysis of Horizontal Market Power Under the Federal Power Act*, 138 FERC ¶ 61,109 (2012).

transactions and less predictive of the outcome of agency merger analyses, and others applauding the flexibility to use a range of analytical tools and evidence in merger reviews.

February 16 Order

In its February 16 order, FERC elected to retain its existing approach for analyzing horizontal market power issues in FPA Section 203 proceedings, finding that its "five-step framework for assessing the competitive effects of a proposed transaction, with the first step consisting of the Competitive Analysis Screen, . . . remains useful in determining whether a merger will have an adverse effect on competition." FERC commended the Appendix A Competitive Analysis Screen for "providing analytic and procedural certainty to industry at a relatively low cost" and rejected arguments that FERC is overly rigid in applying the Competitive Analysis Screen, stating that it believes its "current approach is flexible enough to incorporate theories set forth in the 2010 Guidelines, while still retaining the certainty that the current approach provides."

FERC declined to adopt the 2010 Horizontal Merger Guidelines' higher HHI thresholds, stating that "more stringent thresholds are appropriate, especially given the distinctive characteristics of electricity markets." Citing its extensive experience with electrical markets, FERC elected to retain the HHI thresholds identified in Appendix A.

FERC discussed other aspects of the 2010 Horizontal Merger Guidelines with respect to its merger and transaction analysis but declined to adopt them.

Finally, FERC elected to retain its current horizontal market power analysis for assessing eligibility for market-based rate authority and declined to modify its standard analyses to reflect the 2010 Horizontal Merger Guidelines. FERC will continue to assess horizontal market power in the context of market-based rates using its indicative screens (the Pivotal Supplier Screen and the Market Share Screen) without change to the analyses or to the presumption that a seller that passes both screens does not possess horizontal market power. With respect to the Market Share Screen, FERC will retain its 20% seasonal market share threshold.

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