FERC Reaffirms Merger Policy; Does Not Adopt DOJ/FTC 2010 Horizontal Merger Guidelines

February 27, 2012

Public utilities could face different levels of scrutiny in merger reviews before the U.S. Federal Energy Regulation Commission, and the Department of Justice and the Federal Trade Commission (the Antitrust Agencies).

On February 16, 2011, the U.S. Federal Energy Regulation Commission (FERC) issued an order (138 FERC ¶ 61,109) reaffirming its existing merger review policies for analyzing horizontal market power under Section 203 of the Federal Power Act (FPA) and terminated proceedings to consider incorporating the 2010 Horizontal Merger Guidelines (2010 Merger Guidelines) issued by the Department of Justice and the Federal Trade Commission (collectively, the Antitrust Agencies).

Overlapping Review Under Different Standards

Utility mergers are subject to competition review by the Antitrust Agencies and by FERC. The Antitrust Agencies review potential transactions under Section 7 of the Clayton Act, which prohibits an acquisition if it tends to substantially lessen competition. The 2010 Merger Guidelines, which considerably revised the Antitrust Agencies' 1992 Merger Guidelines, articulate the ways in which the Antitrust Agencies analyze mergers and acquisitions involving actual or potential competitors.

FERC separately reviews public-utility mergers under the statutory standard of FPA Section 203 that mergers must be consistent with the public interest. Competition analysis is part of FERC's public interest review and is based upon the 1992 Merger Guidelines.

Recognizing the duplicative nature of its merger review with that conducted by the Antitrust Agencies, FERC issued a Notice of Inquiry (NOI) in March 2011 seeking comment on whether, and if so how, it should revise its merger review process to align with the changes the Antitrust Agencies made when they moved away from the 1992 Merger Guidelines to the 2010 Merger Guidelines.

2010 Merger Guidelines De-emphasize Market Definition & Concentration

In issuing the 2010 Merger Guidelines, the Antitrust Agencies sought to emphasize competitive effects analysis. In doing so, they de-emphasized market definition and increased, or liberalized, the market concentration threshold of the post-merger Herfindahl-Hirschman Index (HHI). The HHI measures the market concentration in an industry in a

way that gives proportionally greater weight to firms with larger market shares. Under these standards, the Antitrust Agencies consider both the post-merger HHI level and the magnitude of the change in HHI from the pre-merger level (referred to as HHI Deltas in the tables below). The tables below reflect the changes in these thresholds between the 1992 and 2010 Merger Guidelines.

HHI Thresholds

	1992	**2010**
Unconcentrated	< 1,000	< 1,500
Moderately Concentrated	1,000–1,800	1,500–2,500
Highly Concentrated	> 1,800	> 2,500

HHI Deltas Potentially Raising Competitive Concerns

	1992	**2010**
Moderately Concentrated	> 100	> 100
Highly Concentrated	> 50	> 100, < 200

HHI Deltas Presumed Likely to Enhance Market Power

	1992	**2010**
Highly Concentrated	> 100	> 200

In essence, the focus of the 2010 Merger Guidelines was to move away from a rigid methodology toward a more critical analysis of the competitive effects of a merger. In de-emphasizing market definition, the Antitrust Agencies instead engage in a fact-specific inquiry to determine the merged firm's power to harm competition, typically by raising prices. The liberalized HHI thresholds piggyback on the de-emphasis of market definition in focusing on concentration not as its own end, but as "useful to the extent that it illuminates the merger's likely competitive effects."

FERC Does Not Adopt 2010 Merger Guidelines

Upon review of the comments in response to its NOI, FERC chose not to make any modifications to its merger review process. FERC reiterated that its current review process—which is based largely on the 1992 Merger Guidelines' emphasis on market definition and concentration levels as measured by HHI thresholds—allows for a quick, conservative analysis that allows FERC to sort efficiently through potentially problematic transactions. FERC also indicated it believes the lower HHI thresholds of the 1992 Merger Guidelines are more appropriate than the revised 2010 thresholds for analyzing electricity markets. Further, FERC asserted its current framework provides a level of certainty to potential applicants, while maintaining a flexibility to incorporate the theories of the 2010 Merger Guidelines where appropriate.

In deciding not to adopt the 2010 Merger Guidelines, FERC reaffirmed its five-step framework for analyzing the competitive effects of proposed mergers in which the agency assesses:

1. Whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured (based on the HHI thresholds given in the Antitrust Agencies' 1992 Merger Guidelines)
2. Whether the merger, in light of market concentration and other factors that characterize the market, raises concern about potential adverse competitive effects
3. Whether entry would be timely, likely and sufficient either to deter or to counteract the competitive effects of concern
4. Whether efficiency gains can be reasonably achieved by the parties through other means
5. Whether, but for the merger, either party to the transaction would be likely to fail, causing its assets to exit the market

If the transaction does not result in a concentrated market under the first step, it is likely that no further review is needed in the FERC framework.

Merger Reviews May Result in Different Outcomes Under the Divergent Standards

Public-utility mergers could face two different standards of analysis before FERC and the Antitrust Agencies, drawing a distinct question as to what sort of "certainty" public utilities should feel when proposing a merger. As FERC noted in its decision, Federal Trade Commission (FTC) staff stated in a comment responding to the NOI that "excessive

reliance on HHIs—especially in electricity markets—can lead to conclusions that are too lenient or too restrictive in an assessment of market power."

For example, a transaction with a post-merger HHI of 1,250 would be considered "unconcentrated" by the Antitrust Agencies, but "moderately concentrated" by FERC, thus triggering further antitrust review by the more restrictive FERC, but most likely not by the Antitrust Agencies. On the other hand, FERC's reliance on HHIs can also result in an overly lenient assessment of a transaction as compared to the Antitrust Agencies. For example, FERC could determine that a deal with a post-merger HHI of 1,750, with an increase in HHI of 90 points, does not present a competitive issue, but the Antitrust Agencies might determine the transaction was likely to result in anticompetitive effects despite the relatively low HHI concentration levels.

It remains to be seen whether these different standards will yield different results. FERC acknowledges the value of coordination with the Antitrust Agencies when evaluating mergers, and asserts it "will continue to coordinate with staff from the Antitrust Agencies in the future, as appropriate, on a case-by-case basis." In most cases, the authors expect that the outcomes should be similar under both reviews. Nevertheless, parties will need to consider both of these standards in seeking clearance for their transactions.

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