MEMORANDUM

From: AMC Staff

To: Commissioners

Date: July 21, 2006

Re: Supplemental Regulated Industries Discussion Memorandum—Merger Review in Regulated Industries

---

At the Commission's deliberation meeting on July 13, 2006, Commissioners requested that staff provide additional information about the different ways in which the federal antitrust agencies and regulatory agencies are authorized to conduct the review of mergers in regulated industries.[1] This memorandum first elaborates on possible approaches to merger review in regulated industries as discussed at the July 13 meeting. It then sets forth some brief examples of different statutory schemes in this area, and identifies some instances in which an agency (*e.g.*, the Federal Communications Commission ("FCC")) construes its statutory mandate to require it to evaluate not only whether a merger is likely to harm competition, but also whether the merger is likely to *enhance* competition. This may reflect the differences between competitive, unregulated markets and markets undergoing the transition to deregulation, where a regulatory agency may wish to encourage entry to limit the market power of incumbent monopolists. The following paragraphs outline the basic possibilities.

---

[1] *See also* Discussion Memorandum for Regulated Industries, 10-18 (July 11, 2006).

1. **<u>Exclusive authority for the federal antitrust agency, with advisory role for regulatory agency.</u>** The federal antitrust enforcement agency would have exclusive authority to review and challenge mergers or acquisitions of regulated firms under the antitrust laws. The regulatory agency would have no independent authority to prohibit or impose conditions on any merger or acquisition, for any reason. *Example: The Federal Energy Regulatory Commission's ("FERC") absence of jurisdiction to review acquisitions of voting securities of natural gas companies (discussed infra*). The antitrust agency could, however, be obliged to consult with the relevant regulatory agency to assist in its understanding of any competitive issues arising from the regulatory environment.

2. **<u>Dual, concurrent authority for the federal antitrust agency and regulatory agency.</u>** The federal antitrust enforcement agency and the regulatory agency would have dual, independent authority to review mergers and acquisitions in regulated industries. The antitrust agency would have full authority under the antitrust laws. The regulatory agency would review the merger under its applicable public interest standard. The conclusion the antitrust agency reached regarding the merger's effect on competition would have the following relevance to the regulatory agency's public interest review.

A. **<u>Preclusive effect regarding competition issues.</u>** The federal antitrust agency's conclusions on competition issues would be "binding" on the regulatory agency, with preclusive effect on the economic competition portion of the regulatory agency's public interest determination. The regulatory agency could prohibit or impose conditions on a merger or acquisition based on other public interest considerations, but the regulatory agency would have to articulate clearly and with sufficient basis why those public interest considerations outweigh the antitrust agency's conclusion regarding competitive effects. *Example: None found during limited research.*

B. **Presumptive or substantial weight regarding competition issues.** The federal agency's conclusions on competition issues would be given presumptive or substantial weight by the regulatory agency in making its public interest determination. The regulatory agency could reach a different conclusion on the economic competition issues, and could also impose conditions on a merger or acquisition based on other public interest considerations, but would have to articulate clearly and with sufficient basis why it reached a different conclusion regarding competitive effects or why other public interest considerations outweigh the antitrust agency's conclusion regarding competitive effects. *Example: None found during limited research.*

C. **No particular weight regarding competition issues.** The antitrust agency's conclusions on competition issues would not be entitled to any particular weight in the regulatory agency's public interest determination. The regulatory agency could impose conditions on a merger or acquisition based on either competition concerns, other public interest considerations, or a combination of both. *Examples: Review of mergers in various industries by the FCC, the FERC, and certain banking agencies (although the antitrust agency—DOJ in that case—must apply the relevant banking "public interest" standard in its evaluation of the merger, not the Clayton Act Section 7 standard).*

3. **Exclusive authority for regulatory agency, with advisory role for antitrust agency.** The antitrust agency would not have authority to review and challenge a merger or acquisition under the antitrust laws. The regulatory agency would have exclusive authority to prohibit or impose conditions on the merger or acquisition. The antitrust agency's role would be

limited to participating in the regulatory agency's review. The antitrust agency's assessment of competitive effects could be given preclusive, presumptive, or no particular weight in the regulatory agency's public interest assessment. *Example: The Surface Transportation Board's ("STB") jurisdiction with respect to railroad mergers. (The STB is required to give "substantial weight" to DOJ's views, but it makes its own determination of how to weigh any likely anticompetitive effects under the public interest standard.)*

<u>Banks: Coordinated Merger Review by Antitrust Agency and Regulatory Agency.</u>

- **Bank mergers subject to pre-merger competitive review according to provisions enacted prior to the HSR Act and thus are exempt from the HSR process.**[2] 15 U.S.C. § 18a(c)(7). The banking agencies, pursuant to their statutory authority to review bank mergers, are prohibited from approving transactions that the responsible banking agency finds to be anticompetitive. The relevant statutory standard is identical to the wording of Section 7 of the Clayton Act (subject to a "convenience and needs" defense discussed below). 12 U.S.C. § 1828(c)(5). **The banking agency must request "reports on the competitive factors" from DOJ before making any determination.** *See id.* § 1828(c)(4). DOJ submits a report, typically with a recommendation as to whether the transaction should be found to be anticompetitive. **The agency need not accept DOJ's recommendation**.

- **Even if DOJ finds that the merger is anticompetitive, the banking agency may approve the merger if it finds that "the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served."** *Id*. § 1828(c)(5)(B). The statute also provides that "[i]n every case, the responsible agency shall take into consideration the financial and managerial resources and future prospects of the existing and proposed institutions, and the convenience and needs of the community to be served." *Id*. § 1828(c). The burden of establishing this "convenience and needs" defense is on the merging banks. *See id*. § 1828(c)(5).

- **DOJ also has authority to challenge bank mergers.** Although banks are not required to file pursuant to the premerger notification requirements of HSR, DOJ has notice of the proposed merger from the request for a recommendation provided by the bank regulatory agency. Moreover, the bank regulatory agency must immediately notify the Attorney General of any approval of a proposed merger transaction. *Id*. § 1828(c)(6). DOJ may challenge a bank merger approved by the banking agency, provided it files its challenge in a district court within 30 days of the approval (or shorter periods in certain circumstances). *Id.* If it does, there is an automatic stay and the merger is blocked, pending the outcome of the case. *Id*. § 1828(c)(7)(A).

- **DOJ is not allowed to challenge the merger under the Clayton Act, but instead must use the same standard used by the banking agency.** *Id*. § 1828(c)(7)(B). This standard is similar to the Clayton Act, but includes the public interest exceptions outlined above. If the banking agency or DOJ does not challenge the merger or if the challenge is unsuccessful, the merger itself becomes immune from challenge under all antitrust laws except for Section 2 of the Sherman Act. *Id*. § 1828(c)(7)(C).

---

[2] A variety of banking agencies have broad regulatory authority over banks and other financial institutions, including the authority to review mergers and acquisitions. This memorandum summarizes only the bank merger statutory scheme; financial holding company mergers are governed by a similar process, and credit unions are subject to HSR review (since they are not subject to a banking agency's pre-merger competitive review).

- **Although not required by statute, DOJ and the banking agency often work closely in reviewing banking mergers. In 1995, DOJ, the Federal Reserve, and the Office of the Comptroller of the Currency jointly adopted what have come to be known as the Bank Merger Screening Guidelines.** *See* Department of Justice, Bank Merger Competitive Review (available at: http://www.usdoj.gov/atr/public/guidelines/6472.htm). These Guidelines include “screens” to “identify proposed mergers that clearly do not have significant adverse effects on competition.” *Id*. **There still are minor differences between how DOJ and the banking agencies implement the Screening Guidelines, however.** For example, the banking agencies still define the product market as the cluster of services known as commercial banking, whereas DOJ disaggregates the cluster into its constituent parts. *See* ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS (“ALD”) 1321-22 (5th ed. 2002).

<u>Energy: Sole Review by Antitrust Authorities in Some Areas; Dual Review in Others.</u>

- The Federal Energy Regulatory Commission (FERC) has the general authority to regulate aspects of the energy industry, including issuing certificates of public necessity for various facilities. FERC regulates electricity, natural gas, LNG terminals, hydropower, and petroleum. Pursuant to this authority, FERC reviews certain proposed mergers involving natural gas companies or electric companies.[3]

<u>Natural Gas</u>

- **The antitrust agencies have sole jurisdiction to review acquisitions of voting securities of natural gas companies.** *See* ALD at 1292 (citing 15 U.S.C. § 717f (granting authority to FERC only to issue certificates of public convenience); *California v. FPC*, 369 U.S. 482 (1962) (holding Section 717f does not deprive courts of jurisdiction to enforce antitrust laws). FERC has no regulatory authority over such transactions. *Id.* **Nearly all natural gas mergers in the recent past have been voting securities acquisitions.**

- **FERC and the antitrust agencies have concurrent jurisdiction over asset acquisitions of natural gas companies.** *See* ABA SECTION OF ANTITRUST LAW, ENERGY ANTITRUST HANDBOOK: A GUIDE TO THE ELECTRIC AND GAS INDUSTRIES 77 n.263 (2002) ("ABA ENERGY HANDBOOK"). Such mergers are subject to HSR review and also require FERC approval. FERC authority over asset acquisitions stems from the fact that natural gas companies must obtain a "certificate of public convenience and necessity" from FERC before acquiring or operating new facilities. 15 U.S.C. § 717f(c)(1)(A).

- **FERC applies a public interest standard in reviewing asset acquisitions of natural gas companies.** FERC may not approve an asset acquisition, unless the applicant proves that the proposed acquisition "is or will be required by the present or future public convenience and necessity." *Id*. § 717f(e). Moreover, FERC has "the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require." *Id*.

- **In deciding whether the "public convenience and necessity" standard has been met, FERC "balance[s] the public benefits against the potential adverse consequences."** *Natural Gas Pipeline Co. of America*, 110 F.E.R.C. ¶ 61,341, at 61,343 (2005). **For example, when evaluating whether proposals for new pipelines meet the public convenience and necessity standard, FERC's goal is "to give appropriate consideration to the *enhancement* of competitive transportation alternatives,** the possibility of overbuilding, subsidization by existing customers, the applicant's responsibility for unsubscribed capacity, the avoidance of unnecessary disruptions of the

[3] The SEC formerly played a role in the review of acquisitions of certain public utility assets, under the Public Utilities Holding Company Act of 1935 (PUHCA). *See* 15 U.S.C. §§ 79 *et seq.* Congress recently repealed PUHCA. *See* Energy Policy Act of 2005, Pub. L. No. 109-58, §§ 1261-77, 119 Stat. 594, 972-78.

environment, and the unneeded exercise of eminent domain in evaluating new pipeline construction.(emphasis added)." *Id*.

Electric Utility Companies

- **FERC and the antitrust agencies have concurrent jurisdiction over electric utility company mergers.** Such mergers require FERC approval and also are subject to HSR review and challenge under Section 7. *See* 16 U.S.C. § 824b; 15 U.S.C. § 18a. **Thus, if FERC approves a merger, the antitrust agencies may nevertheless seek to place conditions on the merger, and *vice versa*.**

- Electric utility companies must secure an order of authorization from FERC before they may sell, lease, or otherwise dispose of their facilities. 16 U.S.C. § 824b(a). FERC shall grant an order of authorization only if the sale, lease, or disposition of the electric utility company "will be consistent with the public interest." *Id*. The electric utility company has the burden of proving that the transaction is in the public interest, although it need not prove that the transaction will provide a positive benefit. *See Utah Power & Light*, 41 F.E.R.C. (CCH) ¶ 61,283, at 61,752.

- FERC may also place terms and conditions on the transaction, "as it finds necessary or appropriate to secure the maintenance of adequate service and the coordination in the public interest of facilities subject to [FERC's] jurisdiction." 16 U.S.C. § 824b(b).

- **In 1996, FERC issued a policy statement in which it stated that it would use the *Horizontal Merger Guidelines* as the analytical framework for analyzing the effect of proposed mergers on competition.** Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act, Order, No. 592, 61 Fed. Reg. 68,595, 68,596 (1996). In seeking approval of a merger, parties still have the burden to prove that the merger is consistent with the public interest, but can do so by using the analysis found in the Horizontal Merger Guidelines.

- **FERC has stated that its public interest standard for electric utility company mergers generally involves "consideration of three factors: (1) the effect on competition; (2) the general effect on rates; and (3) the effect on regulation."** *Trans-Elect, Inc., Michigan Electric Transmission Co., LLC, Trans-Elect NTD Path 15, LLC,* 110 FERC ¶ 61,389, at 61,389 (2005).

<u>Telecommunications: Dual Review by Antitrust and Regulatory Agencies.</u>

- **The Federal Communications Commission (FCC) and the antitrust agencies have concurrent jurisdiction over communication industry mergers.** The primary authority for the FCC's role in review of such mergers is its control over the granting and transferring of electromagnetic spectrum licenses. *See* 47 U.S.C. §§ 214, 310(d); *see generally* ABA SECTION OF ANTITRUST LAW, TELECOM ANTITRUST HANDBOOK 70-83 (2005) ("ABA TELECOM HANDBOOK"). Almost every communications industry merger involves the transfer of such licenses. The FCC also has specific authority under the Clayton Act to review common carrier mergers, although this authority is not often used. *See* 15 U.S.C. §§ 18, 21(a); *see also* ABA TELECOM HANDBOOK at 71. **The FCC may refuse to approve a transfer or impose such "terms and conditions as in its judgment the public convenience and necessity may require."[4] Mergers involving communications industries are thus subject to FCC review, as well as being subject to separate HSR review by the antitrust agencies. Even if the FCC approves a merger, the antitrust agencies can seek to place conditions on the merger.**

- **FCC Authority under Section 310(d)**

  - All broadcasters, cable companies, and direct broadcast satellite companies must have a station license in order to transmit their signals. *See generally* 47 U.S.C. §§ 301 *et seq*. If such a company seeks to transfer a station license, it must first obtain approval from the FCC. 47 U.S.C. § 310(d).

  - **To approve a proposed transfer, the FCC must determine that it will serve the "public interest, convenience, and necessity."** *Id*.; *see also In re application of General Motors Corp. & Hughes Elec. Corp and the News Corp. Ltd.*, 19 F.C.C.R. 473, 483 (2004).

  - **In describing the contours of the public-interest standard, the FCC has explained that "the public interest evaluation under Section 310(d) necessarily encompasses the broad aims of the Communications Act, which includes, among other things, preserving and *enhancing* competition in relevant markets**, ensuring that a diversity of voices is made available to the public, and accelerating private sector deployment of advanced services. . . . That policy is shaped by Congress and deeply rooted in a preference for competitive processes and outcome.(emphasis added)" *Id*. at 483-84 (citations and internal quotations omitted).

  - **This analysis differs from the competitive analysis conducted by DOJ and the FTC. "Our determination of the competitive effects of the proposed transaction under the public interest standard is not limited by traditional antitrust principles . . . .** The review conducted by DOJ is pursuant to Section 7 of the Clayton Act, which prohibits transactions that are likely to substantially lessen competition in any line of commerce. The Commission, on the other hand, is charged with determining whether the transaction serves the broader public interest." *Id*. at 484 (citations omitted).

---

[4] 47 U.S.C. § 214(c). *See also* 47 U.S.C. § 303(r).

- **FCC Authority under Section 214**
  - **Section 214 provides the FCC with authority to review the extension or acquisition of common carrier lines, under a public interest standard.** *See* 47 U.S.C. § 214(a), *In re Application of GTE Corp. & Bell Atlantic Corp.*, 15 F.C.C.R. 14,032, 14,045 (2000).[3] The questions that the FCC considers under the Section 214(c) standard are: "(1) whether the transaction would result in a violation of the Communications Act; (2) whether the transaction would result in a violation of the Commission's rules; (3) whether the transaction would substantially frustrate the Commission's ability to implement or enforce the Communications Act; and (4) whether the merger promises to yield affirmative public interest benefits that could not be achieved without the merger." *Id*. at 14,046 (citations omitted).
  - **The FCC distinguishes its competitive analysis under Section 214 from the antitrust review performed by the antitrust agencies.** "Our analysis of public interest benefits and harms under parts three and four of the public interest test includes, but is not limited to, an analysis of the potential competitive effects of the transaction, informed by traditional antitrust principles. Although an antitrust analysis focuses solely on whether the effect of a proposed merger may substantially lessen competition, the Communications Act requires the Commission to apply a different standard." *Id*. at 14,046-47 (citations and internal quotations omitted). **In particular, the FCC seeks to ensure that the merger in question "will *enhance* competition, not merely [not] lessen it" and yield overall public interest benefits. *Id*.**

[3] The FCC at times refers to a single public-interest standard applicable under Sections 214(a) and 310(d). *See id.* at 14,046 ("The public interest standard under sections 214(a) and 310(d) involves a balancing process that weighs the potential public interest harms of the proposed transaction against its potential public interest benefits.").

Transportation: Exclusive Review by Regulatory Agency.

- The Surface Transportation Board (STB) is both an adjudicatory and regulatory body with jurisdiction over railroads and certain motor carriers. STB was created in 1995 and is the successor agency to the Interstate Commerce Commission.

Railroads

- **The STB has exclusive jurisdiction over rail carrier mergers.** 49 U.S.C. § 11321(a). Merger transactions that are approved by STB are exempt from the antitrust laws, including state and municipal laws. *Id*.
- **In reviewing mergers between Class I railroads (the largest rail carriers), the STB applies a public-interest standard under which it must consider at least the following:** "1) the effect of the proposed transaction on the adequacy of transportation to the public; 2) the effect on the public interest of including, or failing to include, other rail carriers in the area involved in the proposed transaction; 3) the total fixed charges that result from the proposed transaction; 4) the interest of rail carrier employees affected by the proposed transaction; and **5) whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region or in the national rail system.**" *Id*. § 11324(b). If STB finds that the transaction is "consistent with the public interest," the merger will be approved, although STB may impose conditions on the transaction. *Id*. § 11324(c). **Although the final decision belongs only to the STB, that agency is required to give "substantial weight" to DOJ's views on the likely competitive effects of a proposed merger.**
- If the merger does not involve Class I railroads, the merger shall be approved, unless STB finds that "1) as a result of the transaction, there is likely to be substantial lessening of competition, creation of a monopoly, or restraint of trade in freight surface transportation in any region of the United States; and 2) the anticompetitive effects of the transaction outweigh the public interest in meeting significant transportation needs." *Id*. § 11324(d).