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I. Introduction

A. The antitrust laws have been described as the "Magna Carta of free enterprise." [1]

B. The purpose of the antitrust laws is to protect "competition not competitors."

C. In broad terms, Congress outlawed agreements in restraint of trade, monopolization and acquisitions that may tend to create monopolies.

II. Section 1 of the Sherman Antitrust Act

A. Statutory language: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal."

B. Read literally, the statutory language would outlaw all restraints. Obviously, such a reading of the statute would be overbroad and contrary to the intent of Congress. Section 1 of the Sherman Act outlaws only unreasonable restraints of trade. The key question, therefore, is whether the restraint in question is unreasonable.

C. Courts have devised two analytic tools to distinguish permissible agreements from those that violate the Sherman Act: per se, and rule of reason.

1. Per se

a. Category of offenses reserved for conduct that is so pernicious, so plainly anti-competitive, that they will be deemed unlawful "without elaborate inquiry as to the precise harm that they have caused or the business excuse for their use."[2]

b. Similar to the "strict liability" concept in tort law, once an antitrust plaintiff proves that the defendant committed the act, liability attaches. A defendant is not allowed to offer justifications for the conduct.

c. The following are the offenses that are per se unlawful:

i. Horizontal price-fixing: Agreements among competitors to set, peg or stabilize price or otherwise restrict price competition.

ii. Minimum resale price maintenance (RPM): Agreements between firms at different levels of distribution (e.g., a manufacturer and retailers) to fix the price at which the product is to be resold. Resale prices can be set at a minimum, which requires that prices not be set below a specific level, or at a maximum, which prohibits resale above specific levels. Minimum RPM remains per se unlawful.[3] Maximum RPM, on the other hand, is judged under the rule of reason. [4]

iii. Territorial or customer allocation agreements: Agreements between competitors not to compete against each other with respect to certain customers or in certain territories.

iv. Tying arrangements: Agreements to sell one product (the "tying" product) on the condition that the buyer purchase another product (the "tied" product). Note, however, that not all tying arrangements are per se unlawful. The four requirements for presumptive illegality are: 1) the tying and tied products are "separate" products or services; 2) the availability of the tying product has been "conditioned" upon purchase of the tied product; 3) the party imposing the tie has market power in the tying product; and 4) the arrangement affects a "not insubstantial" amount of commerce.[5]

2. Rule of Reason:

a. Any conduct that does not fall into the per se category is judged under the rule of reason. Most antitrust claims are judged under this standard.

b. The rule of reason analysis requires a balancing of the procompetitive virtues of a particular practice and its anticompetitive effects.[6]

c. In recent years courts have adopted an abbreviated, or "quick look," rule of reason analysis for some restraints.[7]

III. Section 2 of the Sherman Act

A. Statutory language: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of trade or commerce among the several states, or with foreign nations, shall be deemed guilty of a felony..."

1. Two elements of a Section 2 claim: "(1) possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as

distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."[8]

2. Important to understand that the mere possession of monopoly power is not unlawful. An antitrust plaintiff must demonstrate that the monopolist has gained or maintained its monopoly through exclusionary conduct. The courts have defined "exclusionary conduct" as "conduct, other than competition on the merits or restraints reasonably necessary to competition on the merits,"[9] "the employment of unjustified means to gain [monopoly] power,"[10] and "conduct that unnecessarily excluded competition."[11]

IV. Section 7 of the Clayton Act (15 U.S.C. §18)

A. Statutory Language:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the sock or the share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or tend to create a monopoly.

B. The statute is designed to arrest mergers that threaten competition.

C. The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. §18a, and the regulations implementing the statute, 16 C.F.R. Parts 801-03, require the buyer and the seller in certain transactions (buyer only for tender offers) to file "Pre-Merger Notification" forms with the Federal Trade Commission ("FTC") and the Department of Justice ("DOJ"). The parties must wait thirty days (fifteen days in the case of cash tender offers) before consummating the transaction, unless one of the federal agencies serves a request for additional information, commonly known as a "Second Request." A Second Request extends the waiting period for twenty days (ten days in the case of cash tender offer) after the date the parties have substantially complied with the request.

D. The DOJ and FTC have issued Merger Guidelines setting forth the analysis the agencies will employ when screening mergers for possible challenge.

1. Steps in the agencies' analysis:

a. Definition of relevant product market

b. Definition of relevant geographic market

c. Identification of participants in the market

d. Calculation of market concentration

e. Examination of whether there are barriers to entry

f. Determination of the likely competitive effects

g. Examination of whether the transaction will yield efficiencies

2. The product market is the group of products within which competition meaningfully occurs. The task is to draw narrowly a circle that excludes any product to which, within variation in price, only a limited number of buyers will turn (in other words, products whose cross-elasticities of demand are small).

3. The geographic market is the area in which the seller operates and to which the purchaser can practically turn for supplies. If consumers in a given geographic market do not consider products from outside that area as practical, good alternatives, then the geographic area is not in the geographic product market.

4. The agencies use the Herfindahl-Hirshman Index ("HHI") to quantify market concentration. It is calculated by (1) squaring the market share of each competitor and (2) summing the resulting numbers. For example, a market of four firms with market shares of 30%, 30%, 20% and 20%, respectively, would have an HHI of 2600. (900 [302] + 900 [302 ]+ 400 [202] + 400 [202]=2600). The index rises as the number of firms in the market decreases and the disparity in size between those firms increases. The following is the degree of concentration based upon the HHI:

Above 1800 - market considered highly concentrated

1000-1800- market considered moderately concentrated

Below 1000- market considered unconcentrated

Transactions that increase the HHI in highly concentrated markets more than 100 points presumptively raise antitrust concerns.

5. The presence or absence of entry barriers affect significantly the analysis of a merger. An entry barrier is any factor that permits firms already in the market to earn returns above competitive levels while deterring outsiders from entering. Adverse competitive effects are unlikely when entry is easy.

6. The agencies also examine whether the merger will result in efficiencies sufficient to offset any anti-competitive harm. Efficiencies should be merger specific; that is, the parties must demonstrate that the claimed efficiencies could not be realized in the absence of the merger.

E. Vertical Mergers

1. Vertical mergers are mergers between suppliers and customers.

2. A vertical merger can harm competition if:

a. the merged entity is able to raise its rivals' costs

b. the merger grants the merged entity access to competitively sensitive proprietary information

c. the merger raises barriers to entry

d. the merger allows the merged firm to evade rate regulation

V. Comparison of DOJ/FTC Merger and FERC Merger Analysis

A. FERC Merger Analysis

1. FERC has adopted the substance of the DOJ/FTC Merger Guidelines

2. FERC also considers the effects on service and reliability

B. Comparison of the Investigative Approaches of the FERC and Federal Antitrust Agencies

1. DOJ/FTC merger investigations

a. documents and other information collected (by subpoena and voluntary production)

b. witness are examined

c. independent record for possible court challenge built

d. information obtained in the course of an investigation held in strict confidence

2. The FERC merger review process (as well as that of other sectoral regulators)

a. relies upon the parties' merger application to provide information concerning the likely competitive effects of a merger

b. no independent means of gathering information (i.e., no subpoena power)

c. rules of the agency allow intervenors to seek discovery of merger applicants

d. agency has the power to disapprove mergers

e. confidential treatment of information the exception rather than the rule (important because release of competitively-sensitive information may itself be anti-competitive)

IV. Antitrust Exemptions and Immunities

A. Introduction: There are several statutory and non-statutory exemptions to the antitrust laws. The following are the principal exemptions that may apply to firms in the electric power industry.

B. State Action ("Parker") Doctrine

1. Immunizes actions by a state acting in its sovereign capacity[12] and actions by private parties that are authorized and supervised by a state.[13]

2. The Midcal test requires that private parties wishing to avail themselves of "Parker" immunity demonstrate that the conduct: (1) followed a "clearly articulated

and affirmatively expressed state policy and (2) was subject to active supervision by the state."

C. Noerr-Pennington Doctrine: Named after the two Supreme Court cases[14] that developed this doctrine, immunizes conduct intended to influence legislative, executive, and judicial decision-making.

D. Implied Immunity: Provides immunity to parties acting pursuant to federal statutes or regulations that conflict with the antitrust laws. In order for a statute or regulation to repeal by implication the antitrust laws, there must be a finding that there is a "plain repugnancy" between the antitrust laws and the regulatory provisions. Implied repeal of the antitrust laws is disfavored.[15]

E. Filed Rate Doctrine: Doctrine dating back to early part of the last century that provides immunity from antitrust damage actions that arise out of challenges to rates "on file" and approved by federal regulatory agencies.

F. Primary Jurisdiction: Not truly a defense, this doctrine allows a federal court, in instances where the court and a federal agency have concurrent jurisdiction, to abstain from considering an action pending the completion of an administrative proceeding. The invocation of the primary jurisdiction doctrine is appropriate when an agency determination of an issue may "be of material aid" to the court.[16]

VII. Market Power

Definition: Ability of a firm to raise prices profitably above competitive levels for a significant period of time.

A. Rate of return regulation designed to limit the ability of a monopolist to exploit market power.

B. Types

1. Vertical: The ability of a firm to deny or raise the cost of a needed or valuable input to a rival.

2. Horizontal: The ability of competitors at the same level of distribution to raise price above competitive levels.

C. Antitrust Limitation: Antitrust laws are not designed to address pre-existing market power. Mere possession of monopoly is not unlawful. See Section III. C., above.

D. Approaches to addressing market power:

1. Behavioral

2. Structural

E. Behavioral Remedies

1. Through rules, this approach attempts to control the behavior of the monopolist.

2. DOJ, FTC and some commentators see the following difficulties with the

behavioral approach:

a. Incentives to exercise market power are left in place

b. Compliance with rules is difficult to monitor (difficult to detect and document the exercise of market power in many instances)

c. Difficult to craft the correct rules

d. Market power monitoring and mitigation rules may misidentify competitive behavior as anti-competitive behavior

F. Structural Remedies

1. Federal enforcement agencies favor structural remedies that seek to create efficient structures that eliminate the incentive and ability to exercise market power.

2. The agencies see the following benefits of the structural approach:

a. eliminates the incentive and ability to exercise market power

b. does not require ongoing monitoring

G. Regional Transmission Organizations

1. RTOs have been cited by federal agencies as a "promising" solution to vertical market power and as a means to reduce horizontal market power

2. Optimally-sized (large) RTOs:

a. create large geographic markets by eliminating economically inefficient rate pancaking

b. eliminate the ability of transmission owners to favor their own generation over that of competitors play an important role in the control and management of competitively sensitive constrained transmission interfaces

3. The Department of Justice has advocated that Congress pass legislation expressly authorizing the FERC to order the formation of RTOs. The federal agencies are concerned that uncertainty regarding current FERC authority and the current patchwork of voluntary RTOs are hindering the development of a vibrant competitive wholesale power market.

4. The Federal Trade Commission staff has issued four "warning signs" for RTOs:

a. RTOs that are too small

b. the absence of a plan for generation restructuring

c. RTOs that are not sufficiently independent

d. RTO plans that do not effectively deal with transmission congestion

H. Transmission Pricing

1. Federal agencies believe that efficient transmission pricing is critical to wholesale competition. According to the agencies, pricing, in order to be efficient, should be based on sound principles of economics and physics. Thus, according to the DOJ and FTC, transmission pricing should be based upon marginal cost. Marginal costs are the changes in total costs associated with a change in one unit quantity of output.

2. The agencies have explained that the short term benefits of efficient transmission pricing include:

a. prices that send the appropriate signals that channel electricity to the areas of greatest need

b. prices that accurately reflect the constantly changing relative scarcity of transmission capacity

c. prices that enable market participants to use the most efficient combination of transmission capacity and generation at each point in time

d. prices that avoid the need to establish expensive, cumbersome and inefficient administrative methods of rationing scarce transmission capacity

3. The federal agencies view the facilitation of efficient investment decision-making as being the principal long-term benefit of marginal cost-based transmission pricing.

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[1]. U.S. v. Topco Associates, Inc., 405 U.S. 596, 611 (1972).

[2]. Northern Pacific Railway v. United States, 356 U.S. 1, 5 (1958).

[3]. *See* Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).

[4]. *See* State Oil Co. v. Khan, 522 U.S. 3 (1997).

[5]. *See* Jefferson Parish Hospital District No. 2 v. Hyde, 446 U.S. 2 (1984).

[6]. *See* Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918) ("The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition."). *See also* State Oil Co. v. Khan, 522 U.S. 3

(1997) ("[M]ost antitrust claims are analyzed under a 'rule of reason', according to which the finder of fact must decide whether the questioned practice imposes an unreasonable restraint on competition, taking into account a variety of factors, including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint's history, nature and effect.").

[7]. California Dental Association v. Federal Trade Commission, 526 U.S. 756, 770 (1999) ("Quick look" appropriate in cases in which "the great likelihood of anticompetitive effects can easily be ascertained."). National Collegiate Athletic Association v. University of Oklahoma, 468 U.S. 85, 110 (1984) (A naked restraint "requires some competitive justification even in the absence of a detailed market analysis.").

[8]. United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966).

[9]. Town of Concord, Mass. v. Boston Edison Co., 915 F.2d 17, 21 (1st Cir. 1990).

[10]. Illinois v. Panhandle E. Pipeline Co., 935 F.2d 1469, 1481 (7th Cir. 1991).

[11]. Greyhound Computer Corp. v. IBM Corp., 559 F.2d 488, 498 (9th Cir. 1977), *cert. denied*, 434 U.S. 1040 (1978).

[12]. *See* Hoover v. Ronwin, 466 U.S. 558, 574 (1984).

[13]. *See* California Retail Liquor Dealers' Association v. Midcal Aluminum, Inc. ("Midcal"), 445 U.S. 97, 105 (1980).

[14]. *See* Eastern Railroad Conference v. Noerr Motor Freight, 365 U.S. 127 (1961); United Mine Workers of America v. Pennington, 381 U.S. 657 (1965).

[15]. *See* Silver v. New York Stock Exchange, 373 U.S. 341, 357 (1963). *See e.g.,* Otter Tail v. U.S., 410 U.S. 366 (1973) (Federal Power Act - no implied repeal); MCI Communications Corp. v. AT&T Co., 708 F.2d 1081 (7th Cir. 1983) (Federal Communications Act - no implied repeal); and U.S. v. National Association of Securities Dealers, 422 U.S. 694 (1975) (Securities and Exchange Act - implied repeal found).

[16]. *See* Ricci v. Chicago Mercantile Exchange, 409 U.S. 289 (1973).

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