

The Merger Violates FERC's Merger Standards

Citizen Power recommends that the Commission find that the proposed merger is contrary to the public interest. The evidence in the record clearly points to the legal conclusion that this merger is not in the public interest. This latest filing by the Applicants is simply another effort by Dr. Pifer to come up with a set of unrealistic assumptions and faulty analysis to manufacture a few implausible scenarios where the HHI numbers do not set off alarms. The latest untested analysis by Dr. Pifer again fails to demonstrate that the Applicants will successfully mitigate the anti-competitive dangers of the merger.

The Response of the Maryland Office of People's Counsel

Citizen Power has also reviewed the response of the Maryland Office of People's Counsel ("MOPC") and we are in full agreement with the analysis and recommendations made by the MOPC and Bruce Biewald. Citizen Power joins the MOPC in its positions and arguments.

New Arguments by Citizen Power

In addition to the points raised by the MOPC, Citizen Power raises the following four observations:

1. The Pennsylvania Public Utility Commission found that the proposed merger raised serious market power concerns.

It is important to note that in the one proceeding where the Commission's merger guidelines were addressed in a full hearing, the Pennsylvania Public Utility Commission.

In the final order in that commission's proceeding in this merger, the PA PUC concluded:

Based upon all of the evidence presented by the Applicants and the intervenors, the ALJ's concluded that the merger will substantially increase the market power of the Applicants in various relevant retail markets, including the ability to bid up their energy prices above market levels. No party, including the Applicants, disputed that the effect of the merger raises substantial market power concerns in certain relevant retail markets, and the record supports that finding. Based on the foregoing, the merger provides for an increase in the market power sufficient to require the application of section 2811(e)(2) of the Electric Competition Act, relating to the imposition of "such terms and conditions" as the Commission finds necessary to preserve competition in the retail electric markets.²

2. The Applicants' data and model present material facts which are very much in dispute.

²Pennsylvania Public Utility Commission Docket No. A-110150F.0015, Opinion and Order, entered May 29, 1998, pages 45-46.

A new model is being fed questionable assumptions and data to generate new results. Neither the witness, the new model and its inputs have been subjected to cross examination or competing testimony. The Pifer affidavit presents new analysis and information which are being seen for the first time. In the Pennsylvania proceeding, Dr. Pifer was compelled to admit that his bid-up analysis contained a serious modeling error and was flawed.³ That could be the case again in this new testimony.

3. The Applicants' own analysis shows the ISO fails to abate the market domination problem.

Dr. Pifer's affidavit includes the statement that:

The various forms that the MISO might take generally reduce market concentration, and eliminate market power concerns for some measures in the APS and Duquesne markets, but at current proposed transmission pricing and the present membership, the MISO alone does not eliminate the apparent increase in concentration resulting from the merger, particularly in the Duquesne destination market."⁴

More specifically, Dr. Pifer asserts that "... Applicants membership in the MISO does not have a mitigating effect on market concentration..."⁵ There are three reasons which the Applicants admit are responsible for this result.

The first is that the proposed MISO is considerably smaller than the ISO originally proposed or modeled by the Applicants.

³Pennsylvania Public Utility Commission Docket No. A-110150F.0015, Opinion and Order, entered May 29, 1998, pages 21-22.

⁴Affidavit of Dr. Howard G. Pifer III, June 5, 1998, page 2, lines 1-5.

⁵Affidavit of Dr. Howard G. Pifer III, June 5, 1998, page 8, lines 19-20.

The second reason is that the transmission pricing of the MISO does not eliminate pancaking. Membership in the MISO does little to reduce the impact of transmission charges.

The third reason is that neither APS nor Duquesne are contiguous to MISO. Even the Pifer scenarios which added AEP and First Energy to MISO (Case 2-A and Case 3-A) fail to give the MISO much of a mitigating impact.

4. The Applicants' proposal to divest control of 570 megawatts contains flawed assumptions and unrealistic scenarios.

Citizen Power objects to Dr. Pifer's treatment of the 570 megawatt slice for the following three reasons:

(a) Dr. Pifer assumes the 570 megawatts are sold in eleven blocks to eleven entities not currently in the market. The results are very different if the 570 MW slice is sold to only to one or two new market entrants or to entities already in the market. The results also change if the 570 MW slice is sold and wheeled to another market.⁶ None of these very plausible scenarios is presented or analyzed by the Applicants.

(b) The Proposed RFP gives the Applicants the ability to set a minimum price for the power. The impact of this is that the Applicants retain the ability to affect the price even with the divestiture of control. By saying they reserve the right

⁶The proposed RFP does not guarantee the 570 megawatts will remain in the market after it is sold.

to reject any bid below a certain price, the Applicants continue to exercise market power over this block to keep the price from dropping below the level they choose. This is the very problem with market control.

(c) The proposed divestiture is not scheduled to occur until January 1999, so the Commission is being asked to approve the merger before the merger agreement expires on October 5, 1998 without knowing who and how many entities will obtain control of the 570 MW slice and whether this transfer will be effective mitigation. Given the information before the Commission, it is unable to determine that the proposed merger is in the public interest.

The Biewald Bidding Up Analysis

The MOPC comments contain a bidding up analysis prepared by Bruce Biewald. Using the ELMO model which allows for a more nuanced analysis of bidding, Biewald determines that APS and Duquesne could separately bid up power by \$94 million (a 14% increase above market prices). The merger would provide APS and Duquesne will “substantially more market power” which would allow them to bid up power at a total cost to customers of \$210 million or a 30% increase.⁷ Even removing the 570 MW allows the Applicants to bid up power by \$177 million (or 26%). Citizen Power finds this analysis very persuasive of the dangers posed by this proposed merger.

⁷Affadavit of Bruce Biewald, June 22, 1998, ¶ 25.

Conclusion

Citizen Power asks the Commission to hold that the proposed merger is not in the public interest and to disapprove the merger. If the Commission wishes to consider new information and analysis in response to its May 7, 1998 letter, it must set the matter for hearing to address the material facts in dispute. The record in the Pennsylvania proceeding clearly shows that there are material facts in dispute and that the Commission may not approve this merger based on the facts now in the record or without the opportunity for the other parties in this proceeding to cross examine Dr. Pifer and to present testimony of their own on this matter.

Respectfully submitted,

Date: June 22, 1998

Roger E. Clark
Attorney for Citizen Power

Roger E. Clark, Esq. (Sup. Ct. No. 24852)
905 Denston Drive
Ambler, PA 19002-3901

phone: 215-643-2364
fax: 215-628-2630
e-mail: rclark@libertynet.org