Book Reviews

Regulating Mergers and Acquisitions of U.S. Electrical Utilities: Industry Concentration and Corporate Complication[1] by Scott Hempling

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Regulating Mergers and Acquisitions of US Electrical Utilities provides a unique analysis of the approval of mergers and acquisitions by energy regulators in the United States over the last forty years. There are hundreds of books dealing with the approval of mergers in competitive markets in over 100 years of competition law and anti trust law in Canada and the United States. In that sector the analysis is less complicated. There, mergers mean increased concentration which usually means less competition and higher prices. In regulated markets however the price is regulated, and price is not the concern.

Scott Hempling makes two fundamental points in this book. The first is that the expansion of a monopoly rate base often creates a greater consistent flow of revenue and that, Hempling claims, can help subsidize business activities in unregulated markets. The second, he argues, is that the "no harm" test which is used in both Canada and the United States in merger analysis is next to meaningless. By way of background, Hempling observes that since the 1980s in the United States a stream of mergers and acquisition has cut the number of local independent electric retail utilities in the US by more than half. This, he states, is not in the public interest.

Before we go further, we should outline the substantial experience this author brings to this book. Hempling is the author of three books[2] which energy regulators and counsel consider to be required reading. Scott Hempling has acted as counsel, arbitrator, and expert witness in various regulatory proceedings throughout the United States. For many years he has been a very popular professor at the Georgetown University Law Centre. He has lectured widely at energy conferences in Canada, the United States, and Europe.

He is no stranger to Canada. He has spoken three times at the Canadian Energy Law Forum. First at Salt Spring Island, British Columbia in 2011; then at Malbaie, Quebec in 2012, and Fox Harbour, Nova Scotia in 2014. Hempling has also authored nine articles in this journal. We should add that within a few months the *Energy Regulation Quarterly* will be 10 years old. Scott Hempling will be one of the few authors that has averaged one article a year over the decade.

There is a reason why Hempling has such a wide following. As we noted when we reviewed one of his earlier books Hempling is the Will Rogers of the energy regulation lecture circuit. He takes after his mentor, Alfred Kahn, the former chairman of the Economics Department at Cornell University. Kahn became best known when he was Chair of the Civil Aeronautics Board in Washington, DC. While in that job Kahn made the famous statement that he did not know one plane from another but it did not matter because they were only marginal cost with wings. Scott Hempling enjoys a similar turn of phrase and in his lectures sophisticated economic and legal concepts become long remembered catchy phrases.

This book is unique in that it carefully reviews over seventy merger transactions reviewed and approved by the Federal Energy Regulatory Commission (FERC). Scott Hempling's concerns with the FERC record in merger cases can be best summarized by three paragraphs on the subject in a recent ERQ article.[3] His position in this book can be traced to that article and that article can be traced to a significantly larger article on the same subject in the Energy Law Journal one year earlier.[4]

> Since the mid-1980s, mergers and acquisitions approved by the *Federal Energy Regulatory Commission* (FERC) have cut the number of independent retail electric utilities by more than half. These transactions have taken every possible form: horizontal, vertical, convergence, and conglomerate; operationally integrated and remote; domestic and international; publicly traded and going-private; debt-financed and stock-for-stock.
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> Accompanying this consolidation has been a complication. The conventional pre-1980s utility — local, pure play, conservatively financed — is being replaced by multistate and multinational holding company systems: corporate structures housing multiple, and sometimes conflicting, business ventures — structures that owe their finance ability and viability to their utility affiliates' monthly cash flow.
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> Under Section 203 of the *Federal Power Act*,[5] the FERC must find these consolidating and complicating transactions "consistent with the public interest".[6] Despite multiple policy statements, rules, and 70-plus transaction approvals, the FERC has never defined a "public interest" in terms of the industry's performance. Though the 1996 *Merger Policy Statement*[7] states a purpose of "encouraging greater wholesale competition", that purpose rarely appears in the FERC's actual merger orders. These orders require only "no harm", and no harm only to pre-merger competition — regardless of whether that pre-merger competition is effective or ineffective. Effective competition exists when a market's structure, and its sellers' conduct, pressure all rivals to perform at their best. By requiring only "no harm", and by applying that standard only to pre-merger competition, the FERC has invited and approved transactions whose contributions to performance are necessarily suboptimal. For 30 years, the Commission's merger decisions have disconnected the "public interest" from performance.
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> The Commission's deference to applicants' strategies is logical, and lawful, when the relevant markets giving birth to these transactions are effectively competitive markets. But when mergers involve retail monopolies, the relevant markets are not effectively competitive. Deference to transactions undisciplined by effective competition cannot be consistent with the public interest.

Scott Hempling's concern is really with the no harm test. Since 2005 Canada has used the no harm test in merger cases. More recently Alberta has used this test when it comes to approving construction of new transmission facilities. In that case the Court of Appeal had to determine whether the benefits of the new construction in the determination of whether the no harm test had been met was limited to past benefits and could not include future benefits.

In both Canada and the United States, the no harm test is part and parcel of the public interest test. Hempling points out that the FERC has never offered an adequate definition of that test. Nor have the Canadian courts. Both Canadian courts and American courts concede that it is very broad test and considerable discretion is granted to the regulator in both countries in determining if the public interest test has been met.

In conclusion we note that the regulator's role in approving mergers and acquisition is an important one. It certainly could be improved, as Hempling argues. This book is required reading for any serious energy regulator. The merger issue will become more important going forward. Today regulated utilities are being asked to adopt a number of new technologies in an effort to help decarbonize the electricity grid. Some of those new technologies will lead regulated utilities into competitive markets. A good example is EV charging where many policymakers believe the market should be competitive but at the same time they want the utilities to be involved to ensure that the EV charging networks expand fast enough to meet the dramatic increase in EV vehicles.

Scott Hempling's recent appointment as an Administrative Law Judge at FERC in June 2021 may mean that we will see fewer books and articles by him questioning regulatory conduct. However, no doubt his quick mind will be put to work in writing some very important decisions.

1. Scott Hempling, *Regulating Mergers and Acquisitions of U.S. Electric Utilities: Industry Concentration and Corporate Complication* (Chelthenham: Edward Elgar Publishing, Inc., 2020).
2. Scott Hempling, *Regulating Public Utility Performance: The Law of Market Structure, Pricing and Jurisdiction* (Chicago: ABA Book Publishing, 2021); Hempling, *supra* note 1; Scott Hempling, *Preside or Lead? The Attributes and Actions of Effective Regulators* (Washington: Scott Hempling, Attorney at Law LLC, 2013).
3. Scott Hempling, "Inconsistent with Public Interest: FERC's Three Decades of Deference to Electricity Consolidation" (2019) 7:2 Energy Regulation Q 33.
4. Scott Hempling, "Inconsistent with Public Interest: FERC's Three Decades of Deference to Electricity Consolidation" (2018) 39:2 Energy LJ 233.
5. *Federal Power Act*, 16 USC § 824b.
6. *Ibid*, § 203(a)(4).
7. See *Inquiry Concerning the Commission's Merger Policy under the Federal Power Act: Policy Statement*, 61 Fed Reg 68595 (1996).