UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Control and Affiliation for Purposes of Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act	Docket No. RM09-16-000

MOTION FOR LEAVE TO REPLY AND REPLY COMMENTS OF THE TRANSMISSION ACCESS POLICY STUDY GROUP, AMERICAN PUBLIC POWER ASSOCIATION AND NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

The Transmission Access Policy Study Group ("TAPS"), American Public Power Association ("APPA"), and National Rural Electric Cooperative Association ("NRECA") submit the following limited comments in reply to certain comments concerning the Commission's January 21, 2010, Notice of Proposed Rulemaking ("NOPR") in the above-captioned proceeding.[1] While reply comments have not been specifically requested by the Commission, no party will be prejudiced by the submittal of these reply comments, and they will aid the Commission in the resolution of the issues before it in this proceeding.[2]

TAPS, APPA and NRECA are compelled to respond to parties such as the Electric Power Supply Association ("EPSA") and the Financial Investors Energy Group ("FIEG") who seek modifications that would gut the Commission's proposed

[1] Control and Affiliation for Purposes of Market-Based Rate Requirements under Section 205 of the Federal Power Act and the Requirements of Section 203 of the Federal Power Act, , 75 Fed. Reg. 4498 (proposed Jan. 28, 2010), IV F.E.R.C. Stat. & Regs. ¶ 32,650. TAPS and APPA/NRECA each submitted initial comments in this proceeding on March 29, 2010.

[2] Similar to its treatment of answers to answers, the Commission permits reply comments that assist the development of the record and aid the Commission's understanding of the matters at issue. *Open-Access Same-Time Information System (OASIS) and Standards of Conduct*, 88 F.E.R.C. ¶ 61,100, at 61,239-40 (1999).

Affirmation-based behavioral commitment safeguards.[3] EPSA's and FIEG's requests show the need for the Commission to stick with its current case-by-case approach or adopt limitations on its proposed Affirmation-based approach such as the Federal Trade Commission's ("FTC") proposal that the Affirmation not be available to competitors of the issuing utility or those who control inputs to electric power generation. At a minimum, the Commission should adopt TAPS' and APPA/NRECA's proposed strengthening recommendations.

EPSA would retain the proposed certification-based approach but relieve the investor of the need to make any behavioral commitments whatsoever. This would frustrate or defeat the foundation of the Commission's proposal, *i.e.,* "*the Affirmation will require the investor to abide by commitments* to not take specific actions that would unduly influence the management of the utility, interfere with the operation of the utility's facilities, or request or receive non-public information." NOPR, P 34 (emphasis added). EPSA proposes an "alternative" certification that can be made by the stock issuing utility as opposed to the investor. Comments of the Electric Power Supply Association at 2, 7-11 (Mar. 29, 2010). Under EPSA's alternative, "a corporate officer of the issuer [utility or holding company]" would certify "to the best of the issuer's knowledge" the investor does not intend to act in a manner inconsistent with the proposed commitments**.** *Id.* at 9. EPSA's proposed "alternative" certification would defeat the Commission's commitment-based approach because the investor would commit to

[3] In addition to its initial comments, EPSA submitted reply comments in this docket on April 13, 2010, claiming a right to do so under Commission Rule 213. Rule 213 provides EPSA no right to reply because it only permits answers to pleadings, and "[p]leadings do not include comments on rulemakings." 18 C.F.R. § 385.202. If the Commission considers EPSA's reply it should also consider these reply comments.

nothing. There would be no meaningful assurance that the investor intended to be passive with respect to utility affairs and no way to discipline an investor who sought to exercise control notwithstanding the issuer's (*i.e.,* utility or holding company) belief that the investor would not do so.

EPSA, FIEG and others also seek the elimination or narrowing of the proposed restriction against the sharing of non-public information. EPSA Comments at 11-13; FIEG Comments at 7-8. According to FIEG, "it does not appear possible to certify that [an investor] will not receive [non-public] information" from the utility or holding company. FIEG Comments at 7. Permitting a purportedly passive investor[4] to receive non-public utility information could result in the sharing of all manner of market information[5] between competitor utilities. The Commission should not countenance such a result because it would be contrary to the Commission's declared "task of ensuring that investment in a public utility does not, in fact, create opportunities … for the investor or the public utility to engage in anti-competitive conduct." NOPR, P 36.

FIEG opposes the NOPR's proposed requirement that the Affirmation be made by a senior executive officer, that it bind affiliates, employees, officers, directors and

[4] The Commission should be aware that Wall Street's understanding of what it means for an investor to hold stocks for investment purposes only may differ radically from the Commission's understanding. Defendant Harbinger Capital Partners Offshore Manager, L.L.C. argued in Delaware state court that planning to use acquired shares in support of a takeover attempt was not inconsistent with a stated intent to hold the shares for an investment purpose, and "that it is widely believed in the community of hedge funds who frequently file [SEC] Schedule 13Ds that one need not disclose any intent other than an investment intent until one actually makes a [takeover] bid." *NACCO Industries, Inc. v. Applica Inc.*, No. 2541-VCL slip op. at 46 (Del. Ch. Dec. 22, 2009), *available at* http://www.davispolk.com/files/uploads/MA/harbinger.nacco.applica.12b6.ruling.12.09.pdf. The court held that detailed allegations that the fund had been in secret negotiations with the takeover target and was planning to "take it private" were sufficient to plead the falsity of the fund's stated investment-only intent.

[5] 18 C.F.R. § 35.36(a)(8) (definition of market information including illustrative and non-exhaustive examples).

investors, and that it be made upon personal oath. FIEG argues that the size and compartmentalization of large global financial institutions is a good and sufficient reason for not imposing personal responsibility – on the part of anyone – for the initial and ongoing accuracy of the Commission's proposed passive investor commitments.

> [I]f a signatory must sign under oath individually, that person will be potentially subject to personal liability for matters unknowable to her and beyond her control. If Form 519-C is not revised, FIEG anticipates material problems in having it executed as signatories will be required to feel confident that they are making accurate representations to a government agency and will resist potential personal liability for matters beyond their knowledge and control.

FIEG Comments at 7. FIEG fails to explain how an institution can make an accurate, binding and ongoing commitment to the Commission, if there is *no person* within the organization who is capable or willing to do so. The financial institutions seek to shield their officers and directors from liability and responsibility by means of institutional certifications (made by low-level employees), and leave the Commission to enforce behavioral commitments based on challenging theories of collective institutional knowledge and intent or the painstaking ferreting out of proof of actual personal knowledge and involvement.

The FTC, consistent with the comments of TAPS and APPA/NRECA,[6] questions the adequacy of FERC's proposed behavioral approach, and in particular raises concerns flowing from "the potential diminution in the acquirer's and the issuer's *incentives* to compete." FTC Comments at 3. The FTC shows that this can arise from acquiring a share interest in a competitor's revenue stream. *See Id.* at 20-22. *See also* Kwoka

[6] Including the expert declaration of Professor John E. Kwoka, Jr., attached to APPA/NRECA Comments.

Declaration at 8-9 (also showing anticompetitive problems arising from partial acquisition incentive alignment).[7] The FTC proposes a significant additional structural safeguard if the Commission goes forward with the proposed Affirmation-based approach in order to protect against the potential anticompetitive effects resulting from the adverse incentives associated with partial acquisitions. The FTC recommends that the Affirmation not be available to competitors or those who control inputs to electric power generation.

Specifically, the FTC (Comments at 22) proposes that the Affirmation be modified to state that:

> Neither the reporting person nor any of its employees, officers, or investors competes in the same product and geographic markets as the issuer.
>
> Neither the reporting person nor any of its employees, officers, or investors owns, controls, or is affiliated with an entity that owns or controls "inputs to electric power production" (as defined in 18 C.F.R. § 35.36(a)(4)) serving the same product and geographic markets as the issuer.

TAPS, APPA and NRECA agree with the FTC that its proposal "would address the [adverse] incentive effects … at their core." *Id.* at 23.

In light of the foregoing, TAPS, APPA and NRECA urge the following:

- None of EPSA's or FIEG's suggestions (or other kindred recommendations) should be adopted and their statements make clear the risks associated with the Commission's behavioral Affirmation-based approach: investors claim that institutional size and compartmentalization may make it difficult for them to comply with their commitments, and devoting resources to implementing the Affirmation-based approach serves little to no purpose if investors (as opposed to

[7] In its reply, EPSA seeks to dismiss the problem of incentive alignment as apparently limited to "non-controlling investments." EPSA Reply Comments at 6. EPSA misses the point: a competitor who owns almost 20% of another competitor has aligned its revenue interest with its competitor, and thus may be substantially incented to seek to control the aligned competitor's business practices, by contract or otherwise.

issuers) are unwilling to file and be held accountable for abiding by the requisite certifications.

- EPSA's and FIEG's proposals highlight the benefits of the Commission's current case-by-case review, or adopting the FTC's recommended structural safeguard prohibiting the Affirmation-commitment based approach where the investor is a competitor or owns or controls inputs to electric power production in the same product and geographic markets. The FTC safeguard, if implemented, would go a long way towards furthering the Commission's pro-competitive and pro-infrastructure goals while removing the incentives for improper conduct that will otherwise exist under the Commission's proposed approach.

- EPSA's and FIEG's statements show that, at a minimum, the Commission needs to adopt TAPS' and APPA/NRECA's strengthening suggestions[8] in order to insure that the Affirmation commitments are taken seriously and are enforceable.

[8] In its Reply Comments (at 12), EPSA incorrectly states that "[t]here is no practical difference between an investor that has filed an Affirmation and then determined that it no longer wishes to abide by the terms of that Affirmation and an investor who never filed an Affirmation in the first place." The investor who files an Affirmation gets to acquire a substantial ownership interest in a utility or utility holding company and to do so free of other regulatory requirements. EPSA's skewed perspective underlines the need for the Commission to either stay the course with its current approach of case-by-case review or significantly strengthen its proposed Affirmation-based approach.

Respectfully submitted,

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