

# PRICE SQUEEZE IN A DEREGULATED ELECTRIC POWER INDUSTRY

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## I. INTRODUCTION

The electric power industry is in the midst of spectacular change.<sup>1</sup> Deregulatory efforts have moved the industry into a state of transition from a highly regulated era to one marked by increased competition.<sup>2</sup> This transition era has brought numerous procompetitive changes to the industry, including, for example, increased competition in wholesale and retail markets and a move away from cost-based ratemaking to market-based standards.<sup>3</sup> These changes are profoundly important for their impact on the application of antitrust principles in a deregulated electric power industry. This Comment examines the changes deregulation has brought on the applicability

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1. See, e.g., Paul L. Joskow, *Restructuring, Competition and Regulatory Reform in the U.S. Electricity Sector*, 11 J. ECON. PERSP., Spring 1997, 119, at 119 (“[D]ramatic changes are now taking place in the structure of electric power sectors around the world.”).

2. See *infra* Part II.

3. See *infra* Part IV.

of one antitrust claim important to the electric power industry—the price squeeze.<sup>4</sup>

Suppose a vertically integrated firm sells electricity at wholesale and retail.<sup>5</sup> Both the firm's wholesale and retail rates are regulated: the former at the national level by the Federal Energy Regulatory Commission (FERC), the latter by respective state public utility commissions. The vertically integrated utility services fifty towns in a given state. The distribution systems in forty of the towns are owned by the utility; in the others, the town itself owns the system. In areas where the town itself owns the distribution system, the town provides retail service to customers while purchasing the electricity wholesale from the utility; in areas where the utility owns the distribution system, it provides retail service at rates set by the state.

Suppose further that the integrated utility requests and receives a rate increase from FERC for the sale of electricity at wholesale but, for whatever reason, does not request (or does not obtain) a similar increase from the state commission for the sale of electricity at retail. As a result of the increase in wholesale rates, the towns providing their own retail service are forced to raise retail rates (which, in the case of municipalities, are not regulated) in order to continue to cover costs or maintain existing profit levels. Meanwhile, retail rates charged in the other forty towns do not rise. As a result, mobile firms and consumers take up residence in one of the towns where the utility provides retail service in order to take advantage of lower rates. The towns owning their own distribution systems suffer lost profits, perhaps to the point where it is difficult to cover costs.

The hypothetical just advanced evinces a common situational setting in the electric power industry. The allegation made against the integrated utility under such circumstances is one of antitrust injury based on the theory of price squeeze. The claim of price squeeze in the context of electric power has been examined by the courts<sup>6</sup> and well analyzed in the literature.<sup>7</sup> But these investigations of the price squeeze in the electric power context are dependent on characteristics of the industry that are no longer necessarily reflective of the setting that is increasingly facing antitrust courts and those concerned generally with the regulation of electric power. The electric power industry is in a state of transition from an era marked by traditional cost-of-service ratemaking and pervasive regulation to a deregulatory environment characterized by restructuring and a move to

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4. For a description of the price squeeze, see *infra* Part III.

5. The following hypothetical draws its facts from *Town of Concord v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990).

6. See *infra* Part III.

7. See John E. Lopatka, *The Electric Utility Price Squeeze as an Antitrust Cause of Action*, 31 UCLA L. REV. 563 (1984).

market-based ratemaking for wholesale transactions.<sup>8</sup> As wholesale deregulation becomes the norm, antitrust courts will have to reconsider the role of price squeeze claims in antitrust suits brought against integrated utilities.

This Comment takes a first cut at analyzing price squeeze claims arising in a deregulated electric power industry. Part II provides an introduction to the electric power industry, details some of the important structural deregulatory developments that have had an impact on the industry, and discusses the situational factors that give rise to a claim of price squeeze. Part III sets out a theory of the price squeeze. It explains that the factors giving rise to a claim of price squeeze generally are rarely of concern to antitrust courts and are often procompetitive; therefore, courts must be skeptical of the claim. Part III then extends the discussion of the price squeeze to the context of electric power specifically and examines the leading cases addressing the theory in the context of electric power. As this discussion shows, the courts, generally consistent with the theory of the price squeeze developed in the beginning of Part III, have been skeptical of the claim in the context of electric power. Part IV analyzes the application of the price squeeze claim in a deregulated electric power industry. Bringing together the restructuring of the industry and the deregulation of wholesale rates, Part IV attempts to juxtapose changes in electric power with an applicable approach to analyzing the price squeeze claim. Part IV further argues that prevailing on a theory of price squeeze in the electric power context will likely be even more difficult for plaintiffs as wholesale deregulation increasingly becomes the norm in electric power. Part V concludes the Comment.

## II. RESTRUCTURING IN THE ELECTRIC POWER INDUSTRY

### A. *Industry Basics*

The electric power industry can be divided into three parts: generation, transmission, and distribution.<sup>9</sup> Generation is the process of producing electricity.<sup>10</sup> The transmission system transfers the electricity from the generating facility.<sup>11</sup> The distribution system completes the transfer of electricity to the end user.<sup>12</sup> Traditionally, a

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8. See *infra* Part II.

9. See, e.g., FRED BOSSELMAN ET AL., ENERGY, ECONOMICS, AND THE ENVIRONMENT 654-57 (2000).

10. See *id.* at 654-55.

11. See *id.* at 656-57.

12. See *id.* at 657.

vertically integrated firm provided each of these services.<sup>13</sup> Vertical integration was the norm in the electric power industry because of the widely held belief that economies of scale—declining average costs over given periods of production—were present at the generation and distribution stages.<sup>14</sup> Because of the belief that electric power could be provided most efficiently in any given area by a single vertically integrated firm, the electric utility was viewed as a natural monopoly and was regulated as such by state agencies.<sup>15</sup> Under this regulatory regime, the electric utility was granted an exclusive service territory in exchange for having its prices set by state regulators.<sup>16</sup> Moreover, the utility agreed to provide service to any customer located within the relevant service jurisdiction.<sup>17</sup>

The electric power industry is in a state of transition from an era of pervasive regulation to one marked by increased competition. Technological innovation has led economists to suggest that the generation system has lost most of its economies of scale.<sup>18</sup> This recognition has led to efforts to open generation to competition.<sup>19</sup> Meanwhile, the transmission and distribution segments of the industry are still viewed as natural monopolies.<sup>20</sup> Thus, movements toward competitive reform in the industry have consisted in large part of attempts to deregulate price and remove barriers to entry in the generation sector.<sup>21</sup> Other procompetitive reforms in the industry include attempts at the state level to increase competition in retail markets, and attempts by both FERC and various state commissions to shift rate-making away from the traditional cost-of-service paradigm to one guided by market forces.<sup>22</sup>

The Federal Power Act<sup>23</sup> grants FERC regulatory authority over the transmission and wholesale purchase of electric power in inter-

13. See Suedeen G. Kelly, *Electricity*, in ENERGY LAW AND POLICY FOR THE 21ST CENTURY 12-7 (2000).

14. See David L. Kaserman & John W. Mayo, *The Measurement of Vertical Economies and the Efficient Structure of the Electric Utility Industry*, 39 J. INDUS. ECON. 483 (1991).

15. LEONARD S. HYMAN ET AL., AMERICA'S ELECTRIC UTILITIES: PAST, PRESENT, AND FUTURE 4 (7th ed. 2000).

16. See *id.*

17. See Jim Rossi, *The Common Law "Duty to Serve" and Protection of Consumers in an Age of Competitive Retail Public Utility Restructuring*, 51 VAND. L. REV. 1233, 1236 (1998) (noting that the common law and statutory-based "duty to serve" was primarily invoked as a condition on the utility's monopoly franchise).

18. See, e.g., PETER FOX-PENNER, ELECTRIC UTILITY RESTRUCTURING: A GUIDE TO THE COMPETITIVE ERA 4 (1997) (noting a general consensus); Matthew W. White et al., *Power Struggles: Explaining Deregulatory Reforms in Electricity Markets*, in BROOKINGS PAPERS ON ECONOMIC ACTIVITY: MICROECONOMICS 201, 202 (1996).

19. See Joskow, *supra* note 1, at 119.

20. See White et al., *supra* note 18, at 202.

21. See *id.*

22. See *infra* Part IV.

23. 16 U.S.C. §§ 791-828 (2000).

state commerce.<sup>24</sup> The Federal Power Act reserves most intrastate matters concerning the sale and resale of electric power to the states.<sup>25</sup> Pursuant to Congress's dual federalism-styled regulatory framework set forth in the Federal Power Act, ratemaking for the electric power industry has been, and continues to be, derived from two sources. Transactions concerning interstate wholesale purchases are governed by rates set by FERC, while intrastate transactions, including most retail transactions, are governed by rates set by the relevant state public utility commission. The rest of this Part discusses some of the ways rates are set by both FERC and state commissions and examines some of the changes currently taking place in both the federal and state regulatory spheres—changes that could have a dramatic impact on the way the price squeeze claim is analyzed.

### B. Ratemaking

Traditionally, state and federal regulators have required regulated utilities to offer consumers rates “that were just, reasonable, and non-discriminatory.”<sup>26</sup> In accord with the traditional economic understanding of natural monopoly, electric utility firms' rates were regulated to ensure those firms would not take advantage of their market dominance by reducing output or raising prices to supracompetitive levels.<sup>27</sup>

In the electric power industry, rates have conventionally been set based on cost of service.<sup>28</sup> The cost-of-service paradigm attempts to set rates at levels designed to mirror a competitive market by allowing the regulated firm to recover its cost of providing service along with a reasonable return on its capital investment. The derivation of cost-of-service ratemaking can be expressed by the formula  $R = O + (V - D)r$ , where  $R$  represents the regulated firm's revenue requirement,  $O$  the firm's operating costs,  $V$  the value of a firm's property,  $D$  the amount of depreciation applicable to  $V$ , and  $r$  the rate of return allowed by the regulator.<sup>29</sup>

24. *Id.* § 824(b)(1).

25. *See id.*

26. Joseph D. Kearney & Thomas W. Merrill, *The Great Transformation of Regulated Industries Law*, 98 COLUM. L. REV. 1323, 1331 (1998).

27. *See* Robin A. Prager, *Firm Behavior in Franchise Monopoly Markets*, 21 RAND J. ECON. 211, 211 (1990) (“The traditional solution to the natural monopoly problem is to impose some form of rate regulation.”).

28. *See* Peter Fox-Penner et al., *Competition in Wholesale Electric Power Markets*, 23 ENERGY L.J. 281, 281 (2002) (recognizing the historical dominance of cost-of-service-based ratemaking in the electric power industry).

29. CHARLES F. PHILLIPS, JR., *THE REGULATION OF PUBLIC UTILITIES: THEORY AND PRACTICE* 177 (3d ed. 1993). The formula is often expressed without reference to adjustment to total property value from depreciation. *See, e.g.*, BOSSELMAN ET AL., *supra* note 9, at 507 (expressing the formula as  $R = B(r) + O$ , where the only difference is that  $B$  repre-

In essence, the cost-of-service ratemaking process consists of three steps to be undertaken by the regulator.<sup>30</sup> First, the regulated firm's operating expenses must be calculated. A firm's operating expenses represent its variable costs.<sup>31</sup> These are a firm's largest contribution to the revenue requirement calculation and include expenses like fuel, wages, and maintenance costs.<sup>32</sup>

The second step is for the regulator to subtract the amount of depreciation from a firm's total capital investment. A firm's capital investment represents its fixed costs, or costs that do not vary with the level of production, and include, for example, the costs associated with building and maintaining operational facilities and acquiring and maintaining essential equipment.<sup>33</sup> To be included in this calculation, the claimed asset must be "used and useful" in providing the services that represent the firm's bases for being subject to regulation.<sup>34</sup>

The third step is to determine a fair rate of return for the firm. A fair rate of return is said to consist of determining a regulated firm's cost of capital.<sup>35</sup> The complexities of determining the appropriate rate of return, though, easily outweigh its definitional simplicity.<sup>36</sup> Notwithstanding the complexities of the process,<sup>37</sup> its objectives are relatively straightforward: "It should be fair to investors so as to avoid the confiscation of their property. It should also preserve the credit standing of the utility to enable it to attract new capital to maintain, improve and expand its services in response to consumer demand."<sup>38</sup> In short, as is the case with other aims of the ratemaking process, determining the appropriate rate of return should be done in a way that mimics the operation of market forces as closely as possible.

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sents capital investment—expressed as  $V$  in the original notation—unmodified by a discounting feature for depreciation).

30. See PHILLIPS, *supra* note 29, at 177 (noting that the cost-of-service "formula indicates that determining the total revenue required . . . involves three major steps").

31. See BOSSELMAN ET AL., *supra* note 9, at 507 (explaining that a firm's operating expenses "may vary with its level of production").

32. See PHILLIPS, *supra* note 29, at 177.

33. *Id.*

34. *Id.*

35. See, e.g., Claire Holton Hammond, *An Overview of Electric Utility Regulation*, in ELECTRIC POWER: DEREGULATION AND THE PUBLIC INTEREST 31, 50 (John C. Moorhouse ed., 1986).

36. See *id.* ("[D]etermining the appropriate rate of return is a formidable task embroiling commissions and utilities in time-consuming disputes.").

37. For a short but sufficiently detailed explanation, see Hammond, *supra* note 35, at 50-52.

38. PHILLIPS, *supra* note 29, at 178.

### C. Rate Structure

After a firm's rate of return is determined, the regulator must then allocate the cost-bearing function of the firm's revenue requirement amongst the firm's consumer classes.<sup>39</sup> This process is complicated, in part, by competing economic theories.<sup>40</sup> Complications have been furthered in recent years by rising rates and increased competition. As explained by one of the leading commentators on the regulation of public utilities, "[e]conomists . . . have contended that the traditional approach [to determining rate structure], based on average total or embedded cost, must be replaced with a marginal cost approach to ensure economic efficiency and promote conservation."<sup>41</sup> But even the marginal cost approach is not universally favored.<sup>42</sup> The economic debate over how best to formulate a firm's rate structure will not be addressed further, but it is useful to understand the general notion of rate structure.

### D. Wholesale Competition

Deregulation of the electric power industry has lagged behind deregulation of other industries, such as airlines, gas, and telecommunications.<sup>43</sup> Numerous factors led to the implementation of restructuring measures in the electric power industry. Following a period of declining prices, the industry began to see rising rates.<sup>44</sup> Specifically, "[t]he cumulative effects of inflation, oil price shocks, and fuel prices, as well as the onset of environmental regulation, led to consistent increases in the costs of producing power from traditional generation facilities."<sup>45</sup> Successful restructuring efforts in natural gas also encouraged the electric power industry to experiment with restructuring.<sup>46</sup>

#### 1. Toward Competition in Electric Power

Wholesale markets began transitioning to more competitive markets in 1978 with Congress's passage of the Public Utilities Regulatory Policy Act (PURPA).<sup>47</sup> Authorizing FERC to command wheeling

39. BOSSELMAN ET AL., *supra* note 9, at 556.

40. See Lopatka, *supra* note 7, at 577-85 (discussing these competing economic theories in some detail).

41. PHILLIPS, *supra* note 29, at 180.

42. See *id.*

43. See Elisabeth Pendley, *Deregulation of the Energy Industry*, 31 LAND & WATER L. REV. 27, 60 (1996).

44. See Rossi, *supra* note 17, at 1276.

45. *Id.*

46. See, e.g., Richard J. Pierce, Jr., *The State of the Transition to Competitive Markets in Natural Gas and Electricity*, 15 ENERGY L.J. 323, 324-25 (1994).

47. Public Utility Regulatory Policies Act of 1978, Pub. L. No. 95-617, 92 Stat. 3117 (codified as amended at 16 U.S.C. §§ 824a-1 to a-3, 824i-k, 2601-2645 (1994)).

for wholesale customers and suppliers was, perhaps, PURPA's most significant provision for advancing the electric power industry's restructuring efforts.<sup>48</sup> Ultimately, restrictive agency and judicial interpretations limited PURPA's impact on the competitive restructuring of the industry.<sup>49</sup> It has been suggested, though, that despite the constrictive interpretation of PURPA, its enactment may have had some procompetitive impact on the industry. For example, "the threat of compulsory wheeling may have nudged utilities to negotiate voluntary transmission agreements with other suppliers and wholesale customers."<sup>50</sup> Moreover, PURPA laid the foundation for independent firms to enter the generation market, providing competition for the traditional integrated provider.<sup>51</sup>

## 2. *The Beginning of Open Access*

The next significant boost to the electric power industry's restructuring efforts came in response to heightened concern for energy issues following the United States' involvement in Operations Desert Shield and Desert Storm, with passage of the Energy Policy Act of 1992 ("EPAAct").<sup>52</sup> Among other changes brought by the EPAAct,<sup>53</sup> Congress granted FERC greater authority to order wholesale transmission access.<sup>54</sup> Specifically, the EPAAct authorizes any electric power firm participating in wholesale markets "to apply to FERC for issuance of an order requiring a 'transmitting utility' to provide wheeling services, including any enlargement of transmission capacity necessary to provide the service requested by the applicants."<sup>55</sup> FERC, then, "is authorized to grant the application and order a transmission facility owner to provide the applicant with the requested service on fair terms."<sup>56</sup>

The EPAAct also responds to PURPA's limitations concerning opening power generation to competitive forces by encouraging independ-

48. BOSSELMAN ET AL., *supra* note 9, at 719 (describing this provision). The "wheeling" of electric power refers to its "transfer by direct transmission or displacement . . . from one utility to another over the facilities of an intermediate utility. . . ." *Otter Tail Power Co. v. United States*, 410 U.S. 366, 368 (1973).

49. BOSSELMAN ET AL., *supra* note 9, at 719. (noting the limiting effect of these interpretations and describing various decisions).

50. *Id.*

51. See FOX-PENNER, *supra* note 18, at 137.

52. Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776.

53. For an in-depth description of the changes effected by the EPAAct, see Jeffrey D. Watkiss & Douglas W. Smith, *The Energy Policy Act of 1992—A Watershed for Competition in the Wholesale Power Market*, 10 YALE J. ON REG. 447 (1993).

54. See Rossi, *supra* note 17, at 1279.

55. Watkiss & Smith, *supra* note 53, at 459-60 (citation omitted).

56. *Id.* at 460.



ent firms to enter the generation market.<sup>57</sup> Specifically, the EPAct “removed most of the restrictions on the type of generators that could sell deregulated wholesale power.”<sup>58</sup> In short, the various provisions of the EPAct “accelerated considerably” the transition to restructured, competitive wholesale markets initiated by PURPA.<sup>59</sup>

### 3. *Mandatory Open Access*

Progress toward restructuring brought about by PURPA and the EPAct culminated in the deregulatory agenda’s most significant regulation to date in the electric power industry—Order No. 888.<sup>60</sup> Order No. 888 initiated the unbundling process for transmission and generation assets and set in place a system for mandatory open access of transmission facilities.<sup>61</sup> The open-access requirement, in particular, has opened competition in wholesale markets, “because now a wider range of generators and utilities have access to a networked wholesale power grid.”<sup>62</sup> Other procompetitive benefits of Order No. 888 include the divestiture of generation assets by vertically integrated electric power firms, which has caused an increase in competition amongst firms to provide power at wholesale, and an increase in state movements to restructure retail electric power markets.<sup>63</sup>

### E. *Retail Competition*

Opening wholesale markets to competition is only part of the ongoing restructuring process in electric power. Retail markets—whose regulatory sphere is beyond the purview of federal regulators—are also the subject of intense debate in numerous states concerning whether, or to what extent, restructuring should take place.<sup>64</sup> Under a regime of retail competition, “the functional unbundling of transmission from generation and local distribution services would be ex-

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57. See BOSSELMAN ET AL., *supra* note 9, at 732. For a detailed description of the pre- and post-EPAct regulatory framework, see Watkiss & Smith, *supra* note 53, at 464-73.

58. FOX-PENNER, *supra* note 18, at 138.

59. TIMOTHY J. BRENNAN ET AL., A SHOCK TO THE SYSTEM: RESTRUCTURING AMERICA’S ELECTRICITY INDUSTRY 31 (1996).

60. Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities, Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996) (codified at 18 C.F.R. pts. 35, 385).

61. See Richard P. Bonnifield & Ronald L. Drewnowski, *Transmission at a Crossroads*, 21 ENERGY L.J. 447, 450 (2000); Joseph P. Tomain, *Electricity Restructuring: A Case Study in Government Regulation*, 33 TULSA L.J. 827, 841 (1998).

62. Rossi, *supra* note 17, at 1280.

63. JAMES H. MCGREW, FERC: FEDERAL ENERGY REGULATORY COMMISSION 178 (2002).

64. For a discussion of many of the issues being debated and state-specific examples of retail restructuring efforts, see CUSTOMER CHOICE: FINDING VALUE IN RETAIL ELECTRICITY MARKETS (Ahmad Faruqui & J. Robert Malko eds., 1999).

tended to separate the local distribution function from retail sales.”<sup>65</sup> Then end users, including residential consumers, would have the ability to purchase electricity from the retail firm of their choosing.<sup>66</sup>

Opening retail markets to competition consists primarily of state regulatory measures designed to mandate retail wheeling to allow supplying firms that own no transmission or distribution facilities in a given area to provide service to that area.<sup>67</sup> Integrated utilities still own transmission and generation facilities in most states and are generally unwilling to provide consumers with retail choice.<sup>68</sup> The goal of retail competition, though, is that every consumer will have a choice of retail providers and will be able to choose firms on the basis of competitive factors, such as price.<sup>69</sup>

Despite differing regulatory jurisdictions, retail and wholesale competition are generally seen as two parts of a competitive whole.<sup>70</sup> Generally, consumers do not currently have the option to select their retail providers.<sup>71</sup> Thus, despite the opening of wholesale markets—which presumably results in economic benefits to consumers—consumers will not realize the full range of benefits from competition until retail markets are subject to competition.<sup>72</sup>

Although nearly every state has at least considered opening retail markets to competition,<sup>73</sup> there are many difficulties involved with implementing retail competition.<sup>74</sup> Nowhere are these difficulties more evident than when examining the aftermath of the California

65. BRENNAN ET AL., *supra* note 59, at 41-42.

66. *See id.* at 42.

67. *See* MASAYUKI YAJIMA, DEREGULATORY REFORMS OF THE ELECTRICITY SUPPLY INDUSTRY 81 (1997).

68. *See* Rossi, *supra* note 17, at 1281.

69. *See* Richard D. Cudahy, *Retail Wheeling: Is this Revolution Necessary?*, 15 ENERGY L.J. 351, 351 (1994) (“Retail wheeling contemplates that every electric power customer should be given an opportunity to seek out the lowest cost source of power wherever it can be found.”).

70. *See* Rossi, *supra* note 17, at 1281 (“It is well-recognized that, in order to maximize the benefits of competition in wholesale power markets, retail access to competition for all customers will be necessary.”).

71. *See id.*

72. *See id.*

73. *See* BOSSELMAN ET AL., *supra* note 9, at 872 (“[M]ost . . . states have considered moving forward with retail competition, and many have already adopted competition plans.”). For a brief description of some of those plans, *see id.*

74. *See, e.g.*, Harry First, *Regulated Deregulation: The New York Experience in Electric Utility Deregulation*, 33 LOY. U. CHI. L.J. 911 (2002) (noting the difficulties New York has encountered while attempting to implement a program of retail competition). Regarding the Kansas plan, one scholar has noted:

In developing a plan, many legal and non-legal policy issues must be considered. When non-legal issues are decided, interested entities will be either satisfied or dissatisfied with the outcome. In contrast, when legal issues are decided, an outcome that is contrary to law or constitutional principles may invalidate the entire plan.

Sonnet C. Edmonds, *Retail Electric Competition in Kansas: A Utility Perspective*, 37 WASHBURN L.J. 603, 635 (1998).

electricity crisis.<sup>75</sup> But the crisis in California has not led to widespread abandonment of proposals to open retail markets to competition. Instead, the result of the crisis in California is that regulators have begun to study the situation to determine how to better implement retail choice programs in their own states.<sup>76</sup> Despite the potential costs of retail choice programs, their potential benefits will likely lead state regulators to continue considering various restructuring proposals for their respective states.<sup>77</sup>

### III. PRICE SQUEEZE

#### A. *Introducing the Price Squeeze*

A vertically integrated monopolist effectuates a price squeeze on second-level competitors, who are also purchasers of the first-level monopolized good, when the monopolist's first-level price is too high or second-level price too low for the competing firm to cover its costs.<sup>78</sup>

Because the vertically integrated firm is a monopolist at level one, the firm operating only in the level-two competitive market has nowhere else to turn for the necessary level-one input. Thus, the price at which the vertically integrated firm sells the monopolized good to a second-level competitor establishes a cost base for that competitor.<sup>79</sup> Likewise, the price at which the vertically integrated firm sells its second-level product sets an upper limit on the price its competitor can acquire for that product.<sup>80</sup>

The paradigmatic illustration of a price squeeze comes from the factual setting of the claim's seminal case, *United States v. Aluminum Co. of America (Alcoa)*.<sup>81</sup> Aluminum Company of America ("Al-

75. For a list of the difficulties experienced by residents of California in the wake of the crisis, see Jim Rossi, *The Electric Deregulation Fiasco: Looking to Regulatory Federalism To Promote a Balance Between Markets and the Provision of Public Goods*, 100 MICH. L. REV. 1768, 1768-69 (2002).

76. See Peter Navarro & Michael Shames, *Electricity Deregulation: Lessons Learned from California*, 24 ENERGY L.J. 33, 64 (2003) ("It is to the learned remembrance of the mistakes of California that must serve as lessons for those policymakers who continue to participate in the deregulation debate.")

77. For a good discussion of the various costs and benefits associated with retail choice programs, see FOX-PENNER, *supra* note 18, at 291-315.

78. See *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 18 (1st Cir. 1990); 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 767c, at 126 (2d ed. 2002).

79. See AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c, at 126 ("The price at which [the integrated firm] sells the monopolized raw material or intermediate product puts a floor under the costs of the second-stage producers . . .").

80. *Id.* (noting that the integrated firm's "selling price at the second stage puts a ceiling on the prices they can obtain").

81. 148 F.2d 416 (2d Cir. 1945). The *Alcoa* opinion—written by Judge Hand—is generally interpreted to stand for the proposition, as it relates to the issue of price squeeze, that a price squeeze is effectuated unlawfully by a firm with monopoly power when it

coa”), a vertically integrated firm, had monopolized the market for ingot, a good sometimes used to produce sheet metal.<sup>82</sup> Alcoa was the largest participant in the competitive market for the sale of sheet metal, but it also sold ingot to firms that would then produce sheet metal themselves, thus causing these firms to enter into direct competition with Alcoa.<sup>83</sup> The pricing scheme actually alleged in *Alcoa* is more complex than needed for a basic illustration of the price squeeze.<sup>84</sup> But consider the simplified hypothetical based on the facts of *Alcoa* used by then-Chief Judge Breyer in *Town of Concord v. Boston Edison Co.*:

Suppose, hypothetically, that Alcoa’s price for ingot was \$100 per ton; that the independents’ costs of fabricating ingot into sheet was \$50 per ton; and that Alcoa’s price for sheet was \$145 per ton. Under these circumstances, the independents, with ingot costs of \$100 and fabricating costs of \$50, would have no “room” to make a profit, for they could not charge more than \$145 for sheet without losing all of their business to Alcoa. Alcoa’s prices of \$100 for ingot and \$145 for sheet would squeeze the independents out of business.<sup>85</sup>

Although simple, this example illustrates the difficulties raised by a claim of price squeeze. As is clear from this definition and illustration of the price squeeze, there is nothing *a priori* anticompetitive about a squeeze. Instead, properly conceptualized, a price squeeze is merely a by-product of vertical integration, the result of which may be “adverse, neutral, or beneficial.”<sup>86</sup> The key, then, in analyzing any price squeeze claim is to unpack the situational and economic factors surrounding the allegation.

A price squeeze may signal a number of different market or private forces or circumstances in operation. As explained by Professors Areeda and Hovenkamp, “[a] price squeeze might reflect (1) an adverse change in cost or demand conditions, (2) the elimination of monopoly profits at the second level, (3) the monopolist’s increased effi-

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charges the independent competitor “higher than a ‘fair price’” for the first-level good or sets its second-level price too low to allow the independent firm to make “a living profit.” *Id.* at 436-38. Judge Hand’s test has been subject to a host of criticisms, the most obvious of which are that the “fair price” standard offers no meaningful guidance to courts and the difficulty in determining what, exactly, a “living profit” entails. *See, e.g., Town of Concord*, 915 F.2d at 25. For a more detailed criticism of Judge Hand’s test, see AREEDA & HOVENKAMP, *supra* note 78, ¶ 767d2, at 131.

82. *Alcoa*, 148 F.2d at 425 (finding Alcoa’s share of the ingot market to be at ninety percent).

83. *Id.* at 436.

84. For the pricing scheme alleged in *Alcoa*, see *id.* at 437-38.

85. 915 F.2d at 18.

86. AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c, at 126 (“[I]t is difficult to see any *competitive* significance apart from the consequences of vertical integration itself, which may be adverse, neutral, or beneficial.”).

ciency, (4) indirect price discrimination, or (5) predatory pricing.”<sup>87</sup> Only the last circumstance—price squeeze as a result of predatory pricing—is of great concern to antitrust courts considering a claim of price squeeze, and even it may be better conceptualized outside the framework of price squeeze.<sup>88</sup>

Three of the circumstances potentially leading to a price squeeze—change in cost or demand conditions, elimination of second-level monopoly profits, and increased efficiency by the integrated firm—are procompetitive in nature, and thus should not be condemned by antitrust courts.<sup>89</sup> Changes in the cost of producing ingot, for example, will necessarily squeeze second-level sheet metal producers where demand for sheet metal remains constant. Likewise, a large increase in demand for sheet metal would raise the demand—and thus price—for ingot. This set of market circumstances would effectuate a price squeeze on firms needing ingot for the production of end-product goods for which demand remained constant. When the market operates in search of competitive balance in this way, the resulting squeeze is of no concern to antitrust courts.<sup>90</sup>

The elimination of second-level monopoly profits is another possible procompetitive circumstance giving rise to a price squeeze. If the second-level firm is a monopolist, a price squeeze effectuated by the first-level monopolist on the second-level firm will be procompetitive in the sense that the price paid by the end user is likely to fall.<sup>91</sup> In this circumstance, the second-level firm has “no legitimate claim to insulate their monopoly profits from competition, notwithstanding the continuation of monopoly profits at the first stage.”<sup>92</sup> The first-level monopolist may be a legitimate target for antitrust attack, but the second-level monopolist equipped with only the claim of harm to its monopoly via price squeeze is in no position to initiate the challenge.<sup>93</sup>

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87. *Id.* (footnote omitted).

88. This approach is adopted from Professors Areeda and Hovenkamp, who note that price squeeze as a result of predatory pricing is the only one of the five circumstances giving rise to a price squeeze claim that “raises a question of unlawful conduct,” while arguing that even that claim should not be considered under the price squeeze rubric. *Id.* Instead, Professors Areeda and Hovenkamp suggest that the price squeeze as a predatory pricing claim should be analyzed under the jurisprudence of predatory pricing. *Id.*

89. *See id.* (stating that these three circumstances are “beyond reproach”).

90. *See id.* ¶ 767c1, at 127 (noting that such squeezes “are a normal and proper reflection of changed market conditions” and pointing out that “in such cases the ‘squeeze’ is what corrects the imbalance of supply and demand”).

91. *See* *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 24-25 (1st Cir. 1990) (discussing the benefit of reduced price to the consumer when a first-level monopolist squeezes a second-level monopolist).

92. AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c2, at 128.

93. *See id.* (“Whether society chooses to attack the first-stage monopoly is no reason to protect second-level monopoly profits from competition by the monopolist.”).

A third potential procompetitive justification for the existence of a price squeeze is that the integrated firm is simply more efficient than its second-level competitors.<sup>94</sup> This overall efficiency advantage may be the result of more efficient production of the second-level good, or it may simply reflect the firm's lower costs brought about as a result of vertical integration.<sup>95</sup> Regardless, the efficiency advantage most likely benefits consumers in the form of lower prices.<sup>96</sup>

A fourth possible circumstance giving rise to a claim of price squeeze is involvement by the integrated firm in price discrimination against its second-level competitors.<sup>97</sup> The price discrimination claim alleges price differentiation unrelated to cost.<sup>98</sup> A finding of price squeeze via price discrimination says little about whether the squeeze is harmful to consumers.<sup>99</sup> From an economic perspective, the key question when confronting a price discrimination claim is whether the monopolist's output increased or decreased as a result.<sup>100</sup> Whether antitrust courts condemn price discrimination, then, should depend on the outcome of that analysis. As Robert Bork noted:

If discrimination increases output, it tends to move resource allocation and value of marginal product toward that which would obtain in a competitive industry. A decrease in output has the oppo-

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94. See *Town of Concord*, 915 F.2d at 24.

95. See ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 243 (1993); AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c2, at 128.

96. One potential objection to the argument for not attacking this circumstance under the law of price squeeze is that the first-level monopolist may extend its monopoly to the second level and stifle progress in technological advances or productive efficiency. Professors Areeda and Hovenkamp respond to this claim by arguing that "such speculative losses, which may never materialize, are a poor trade-off for present efficiency gains." AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c3, at 128. This response is sound. If inefficient first-level monopolies develop as a result of an efficiency squeeze at level two, market forces should allow for correction via subsequent entry. If the firm engages in potentially illegal anticompetitive conduct, that conduct can, of course, be challenged in a normal antitrust proceeding. Eliminating competitively formed market efficiency gains out of fear that harmful anticompetitive conduct might result at some future time is not justification enough to forgo the presently obtained competitive benefits.

97. See Lopatka, *supra* note 7, at 588 (limiting the definition of price squeeze to a claim that represents "a form of price discrimination").

98. Professor Lopatka describes the price squeeze via price discrimination claim within the context of electric power as "the condition obtaining when the ratio of the private utility's wholesale price to its marginal cost of wholesale service exceeds the ratio of the private utility's retail price to its marginal cost of retail service." *Id.* (citation omitted).

99. See, e.g., Michael E. Levine, *Price Discrimination Without Market Power*, 19 YALE J. ON REG. 1, 36 (2002) ("[I]t is clear that price discrimination *per se* cannot be relied on in . . . any . . . industry as evidence of market power, which itself warrants intervention, and that attempts to stamp it out will ordinarily do more economic harm than good.").

100. See, e.g., BORK, *supra* note 95, at 395 (recognizing that the important economic question when price discrimination is alleged is "whether discrimination expands or further restricts the monopolist's output").

site effect. The impact of discrimination on output, therefore, may be taken as a proxy for its effect on consumer welfare.<sup>101</sup>

Because there is theoretical support for the proposition that price discrimination resulting from vertical integration serves procompetitive ends more often than not,<sup>102</sup> courts should look skeptically at any claim of price squeeze via price discrimination.<sup>103</sup>

The predatory price squeeze is the final variety of price squeeze and is the type of squeeze that is the greatest concern to antitrust courts wishing to promote competition. The predatory price squeeze draws from the concept of predation generally. Predatory pricing can be defined as pricing below cost in order to drive a competing firm from the market.<sup>104</sup> Pricing below cost is said to be rational from the

101. *Id.*

102. *See, e.g., AREEDA & HOVENKAMP, supra note 78, ¶ 756b5, at 16-17, ¶ 767c5, at 129.*

103. At least one court has recognized the tenuous nature of the price squeeze via price discrimination claim. Then-Chief Judge Breyer, while not precluding the possibility of recognizing such a claim, was skeptical of its potential to produce more anticompetitive harm than competitive good. *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 24 (1st Cir. 1990) (“[W]e believe that other arguments (such as those related to economic price discrimination) tend to be inconclusive in respect to anticompetitive effects.”)

104. *See HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE 335 (2d ed. 1999)* (“In its most orthodox form, ‘predatory pricing’ refers to a practice of driving rivals out of business by selling at a price below cost.”). It might be argued that an even less innocuous definition of price squeeze is available. Robert Bork, for example, has defined predation without using cost as a baseline. Instead, Bork defines predation “as a firm’s deliberate aggression against one or more rivals through the employment of [certain] business practices . . .” BORK, *supra* note 95, at 144. Under this definition, a simple lowering of prices (even if to a level still above cost) may be predatory pricing. It has even been explicitly argued that predatory pricing may occur absent pricing below cost. *See generally, Basil S. Yamey, Predatory Price-Cutting: Notes and Comments*, 15 J. LAW & ECON. 129 (1972). The classic response to this theory suggests that without some cost-based standard for analyzing the claim of predation, there is no way to determine what pricing strategy the monopolist should have adopted. *See, e.g., ROGER D. BLAIR & DAVID L. KASERMAN, ANTITRUST ECONOMICS 125 (1985)* (“Without some sort of cost-based standard, it is very difficult to determine whether this pricing is predatory because it is not clear how else the monopolist should behave.”). Nonetheless, I do not mean to reject the possibility of defining predation absent some conceptualization of cost as a baseline. Instead, my use of the term “cost” is simply designed to fall in line with the Supreme Court’s practice of using cost as a baseline when considering predatory pricing claims. *See Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222 (1993) (stating that “a plaintiff seeking to establish competitive injury resulting from a rival’s low prices must prove that the prices complained of are below an appropriate measure of its rival’s costs”).

In addition, by incorporating cost into this Comment’s working definition of predation, I do not mean to enter into the debate of which cost-based definition is best. Complicated arguments with respect to properly conceptualizing cost in predation claims abound. The seminal article on this topic, Phillip E. Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975), induced numerous responses. For a brief discussion, see W. KIP VISCUSI ET AL., *ECONOMICS OF REGULATION AND ANTITRUST 285-86 (2d ed. 1995)*. One interesting article proposing rejection of the cost-based models is Oliver E. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977). For a collection of the theoretical literature regarding the proper definition of predation, see James E. Meeks, *Predatory Behavior as an*

firm's perspective if it plans to recoup its short-term losses by charging monopoly prices after the target firm has exited the market or been sufficiently disciplined.<sup>105</sup> But the predatory price squeeze—unlike predation generally—need not involve pricing below cost.<sup>106</sup> Because of the potential complexities surrounding the situational factors present in a predatory squeeze, such a squeeze would be difficult to identify under anything but reasonably constant market conditions.<sup>107</sup> For example, without evidence that the integrated firm's price for its second-level good is below some measure of cost, alleged squeezes may simply represent the integrated firm's lower operating costs.<sup>108</sup> For these reasons, antitrust courts should be highly skeptical of any claim alleging predatory price squeeze.<sup>109</sup> If the analysis of price squeeze claims is lax, the result may harm the central goal of antitrust: to foster the growth of competition for the good of consum-

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*Exclusionary Device in the Emerging Telecommunications Industry*, 33 WAKE FOREST L. REV. 125, 127 n.7 (1998).

105. See HOVENKAMP, *supra* note 104, at 335. (“The predator’s intent—and the only intent that can make predatory pricing rational, profit-maximizing behavior—is to charge monopoly prices after rivals have been dispatched or disciplined.”); BORK, *supra* note 95, at 144 (arguing that predation “would not be considered profit maximizing except for the expectation either that (1) rivals will be driven from the market, leaving the predator with a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds inconvenient or threatening”). For an argument that firms may engage in predation more often than rational choice theory suggests, see Avishalom Tor, *Illustrating a Behaviorally Informed Approach to Antitrust Law: The Case of Predatory Pricing*, ANTITRUST, Fall 2003, at 52.

106. Professors Areeda and Hovenkamp offer a useful example:

Suppose a copper ingot monopolist has vertically integrated into copper pipe; that copper pipe is the only end product in which ingot is used; that the long-run marginal cost of fabricating pipe is \$35 but the short-run marginal cost for outputs somewhat below most efficient levels is \$25; and, finally, that the long-run profit maximizing price for ingot is \$65. The monopolist can raise the ingot price to \$75, hold the pipe price at \$100, and gradually monopolize without loss in short-term profits, provided that the monopolist can time the expansion of its fabricating capacity in such a way as to match the fall in output by competitors as they curb operations and, as their plants wear out, shut down altogether. In such “ideal” circumstances, the integrated monopolist can avoid short-run profit losses by capturing the independent fabricators’ return on investment. If there are several end products, however, the monopolist cannot conduct a “costless” squeeze without integrating forward into all of them.

AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c5, at 129 n.12.

107. *Id.* ¶ 767c5, at 129 (“[P]redatory price squeeze by an integrated supply monopolist is extremely hard to identify under other than relatively stable cost and demand conditions.”).

108. See HOVENKAMP, *supra* note 104, at 301 (“Most alleged price . . . ‘squeezes’ result because vertically integrated firms have lower costs than do independent firms who must rely on the market. The monopolist who reduces its costs by vertical integration will sell to the consumer at a lower price, and independent dealers will be unable to compete.”).

109. Cf. Oliver E. Williamson, *Delimiting Antitrust*, 76 GEO L.J. 271, 288-89 (arguing that predation claims generally should be “regarded with grave skepticism” until antitrust courts are better able to separate the “good and bad cases”).



ers.<sup>110</sup> Where there is anticompetitive conduct lurking under a claim of price squeeze, it is probably best addressed within the framework of more developed antitrust claims like predatory pricing and refusal to deal.<sup>111</sup>

### B. *The Electric Utility Price Squeeze*

In the electric power industry, the price squeeze claim “arises from the complex relationship between the supplier, the wholesale customer, the retail customer, and the federal and state regulators.”<sup>112</sup> Specifically, a price squeeze in the electric power industry may arise when a vertically integrated utility (operating in both wholesale and retail markets) sets wholesale rates higher than retail rates in relation to cost.<sup>113</sup> In such a case, independent firms that are wholesale customers of the integrated monopolist and competitors of the monopolist at the retail level may not be able to compete in the retail market.<sup>114</sup> Although electric power firms’ rates are regulated to some extent, a squeeze may arise due to actions of the differing bodies that set or approve the rates: FERC at wholesale and state regulatory commissions at retail.<sup>115</sup>

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110. On competition and consumer welfare as the central goals of antitrust, see BORK, *supra* note 95, and RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976).

111. See AREEDA & HOVENKAMP, *supra* note 78, ¶ 767c1, at 127, ¶ 787c3, at 312.

112. Lawrence J. Spiwak, *Is the Price Squeeze Doctrine Still Viable in Fully-Regulated Energy Markets?*, 14 *ENERGY L.J.* 75, 75 (1993).

113. See *id.* at 76.

114. *Id.*

115. See Lopatka, *supra* note 7, at 588 (“The possibility of a price squeeze arises because two agencies are examining a large amount of data, and each separately making hundreds of intricate calculations and subjective judgments.”); *City of Mishawaka v. Am. Elec. Power Co.*, 616 F.2d 976, 983-84 (7th Cir. 1980) (“Behind the rate applications there are differing regulatory procedures, differing tests and standards to be applied, and differing accounting principles to be used in the computations. At best, a utility may find itself in a legal and practical maze . . .”). Despite the fact that differing regulatory regimes set or approve rates in the electric power industry, there is some cross-comparison of rates. The Supreme Court has ruled that FERC, in determining whether a firm’s wholesale rates are just and reasonable, “must arrive at a rate level deemed by it to be just and reasonable, but in doing so it must consider the tendered allegations that the proposed rates are discriminatory and anticompetitive in effect” when considered in relation to retail rates. *Fed. Power Comm’n v. Conway Corp.*, 426 U.S. 271, 279 (1976). Professor Lopatka has proposed having one agency review both wholesale and retail rates to avoid the price squeeze in a fully regulated electric power industry. See Lopatka, *supra* note 7, at 601 (“The most effective way to eliminate both predatory and innocent but undesirable rate squeezes is to place jurisdiction over both wholesale and retail rates in a single agency.”). The possibility of price squeeze is aided by the fact that firms must often wait longer for retail rate approval. See *Am. Elec. Power Co.*, 616 F.2d at 983 (“[T]he wholesale rates under federal control go into effect automatically without agency approval, but the state retail rates must await state approval.”).

### C. *Electric Utility Price Squeeze Cases*

The modern landscape of the electric utility price squeeze was developed in two cases decided in the early 1990s: *Town of Concord v. Boston Edison Co.*<sup>116</sup> and *City of Anaheim v. Southern California Edison Co.*<sup>117</sup> This is not to say that the theory is well developed in the electric power context. The reality is that, although once frequently raised in cases concerning electric utilities, the price squeeze claim is surprisingly underdeveloped. The Supreme Court has yet to address the matter, and lower courts have provided relatively weak signals regarding the claim. Even the differences expressed in the two seminal cases concerning the electric utility squeeze are rather minor. One similarity, though, is strikingly clear. Courts are quite skeptical of allegations of price squeeze in the electric power industry.

#### 1. *Town of Concord*

Nowhere is judicial skepticism of the price squeeze claim clearer or more forcefully developed than in *Town of Concord*. In that case, defendant Boston Edison, a vertically integrated utility, sold electricity at wholesale to the plaintiffs, who were municipalities and their municipally-owned utilities.<sup>118</sup> The plaintiffs complained that increases in the defendant's wholesale rates obtained from FERC were not matched by retail rate increases; as a result, wholesale prices paid by the plaintiffs to the defendant rose over a three-year period while prices charged by the plaintiffs in retail remained constant, resulting in diminished profits.<sup>119</sup>

The First Circuit explicitly held that a government-regulated firm with fully regulated prices was not barred from requesting rate changes that might result in a price squeeze.<sup>120</sup> In effect, though, the First Circuit's reasoning all but foreclosed the possibility of finding a firm with fully regulated rates liable under section 2 of the Sherman Act<sup>121</sup> for effectuating a prize squeeze.<sup>122</sup> The court's initial reasoning

116. 915 F.2d 17 (1st Cir. 1990).

117. 955 F.2d 1373 (9th Cir. 1992).

118. *Town of Concord*, 915 F.2d at 20.

119. *Id.* at 20-21. Specifically, the plaintiffs alleged that the squeeze would result in their "mak[ing] less money." *Id.* at 21.

120. *Id.* at 19.

121. Liability for violation of section 2 of the Sherman Act is premised on a finding of market power in the relevant market and the existence of "conduct designed to acquire, maintain, or extend the monopoly." Lopatka, *supra* note 7, at 610. For a detailed discussion of how these principles apply in the context of electric power, see *id.* at 609-17.

122. One commentator has reported the opinion as having "held that price squeezes do not constitute [section] 2 violations in the regulated industry context." STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST LAW 83 (1993). Ross explains this characterization in a footnote: "Although the court limited its holding by saying that price squeezes would not 'normally' be exclusionary, its analysis effectively bars successful prosecution of [section] 2 claims of municipally-owned electric companies against integrated sources of wholesale power." *Id.*

noted that a fully regulated industry “diminishes the likelihood of ‘entry barrier’ harm, namely the risk that (1) prices will rise because (2) new firms will hesitate to enter a market and compete after (3) a squeeze has driven pre-existing independent competitors from the marketplace.”<sup>123</sup> Related to this argument against finding price squeeze liability in the electric power context, the court noted that regulators generally have authority to determine whether a new firm will enter the market.<sup>124</sup> If a firm is allowed to enter, the court continued, the regulators are unlikely to allow an integrated monopolist to drive the independent firm from the market by charging supra-competitive prices or refusing to deal.<sup>125</sup>

The First Circuit next displayed its skepticism of the price squeeze by touting a potentially procompetitive justification for the alleged squeeze. Specifically, the court noted that because “regulators try to set prices that reflect costs,” any squeeze effectuated by an integrated monopolist is likely to reflect that monopolist’s ability to operate more efficiently than its independent competitor.<sup>126</sup> Thus, the court concluded, “a rule preventing prices that create a squeeze will more likely discourage efficient operations and deprive consumers of prices that reflect lower costs.”<sup>127</sup>

The court’s reasoning, combined with its emphasis on potentially procompetitive explanations for an alleged squeeze, suggests that the First Circuit is not merely skeptical of price squeeze claims but also that the claim is all but foreclosed as the sole basis for finding a Sherman Act section 2 violation in a fully regulated industry. The court further hinted at this conclusion by stating that “a price squeeze in a fully regulated industry such as electricity will not normally constitute ‘exclusionary conduct’ under Sherman Act [section] 2.”<sup>128</sup> To be sure, the court was careful to include the modifier “nor-

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at 83 n.26. One might plausibly argue that this reasoning can be extended beyond the alleged squeeze involving municipally-owned utilities on one side to include any firm that is both a customer of the integrated firm in the wholesale power market and a competitor in the retail market.

123. *Town of Concord*, 915 F.2d at 25.

124. *Id.* at 26.

125. *Id.* As the court stated:

For another thing, factors related to regulation, such as the economic ability of a market to support new entry, or the legal requirement that a firm secure permission to enter, are likelier to determine new entry into a regulated industry than is a new entrant’s fear of a two-level monopolist’s enhanced retaliatory power. After all, should the regulator decide that new entry is warranted, it typically has the legal authority to prevent an existing “two-level” monopolist from improperly disadvantaging a new “second-level” competitor by, say, refusing to deal with it or by charging unreasonably high prices.

*Id.*

126. *Id.*

127. *Id.*

128. *Id.* at 28.

mally,”<sup>129</sup> but again, the reasoning makes clear that it would require rare factual circumstances before the court would find a firm liable for a Sherman Act section 2 violation on the theory of price squeeze.

## 2. City of Anaheim

In *City of Anaheim*, the Ninth Circuit concurred with the First Circuit’s skepticism of the price squeeze claim in a fully regulated industry such as electric power but rejected that court’s apparent foreclosure of the claim.<sup>130</sup> Rather than adopt the First Circuit’s dismissive and conclusive tone regarding the claim, the Ninth Circuit settled for protecting potentially procompetitive conduct in price squeeze cases by focusing its analysis on the question of whether the integrated monopolist had “specific intent” to engage in anticompetitive conduct.<sup>131</sup>

Despite providing more lenient rhetoric than the First Circuit in *Town of Concord*, the Ninth Circuit remained skeptical that such a claim could be proven in the face of the potential procompetitive justifications for an alleged squeeze.<sup>132</sup> And although numerous courts have remained open to the possibility of finding firms liable under a theory of price squeeze in a fully regulated industry like electric power,<sup>133</sup> the claim is almost uniformly looked upon with great skepticism.<sup>134</sup> So pervasive is this skepticism that it has led one commentator, after engaging in an extensive review of price squeeze cases arising in the electric power industry, to conclude that the claim, “[w]hile not outright abolished . . . appears to have lost much, if not all, of its bite.”<sup>135</sup>

129. The court even emphasized the modifier again: “[W]e have limited our holding by stating that ‘normally’ a price squeeze will not constitute an exclusionary practice in the context of a fully regulated monopoly, thereby leaving cases involving exceptional circumstances for another day.” *Id.* at 29.

130. See *City of Anaheim v. S. Cal. Edison Co.*, 955 F.2d 1373, 1378 (9th Cir. 1992) (“We . . . would be reluctant to hold that a mere showing that a squeeze developed would suffice to cause antitrust liability. However, we do not think that one must react as forcefully against the theory as the court did in *Town of Concord* in order to prevent that result.”).

131. *Id.* The court elaborated on how a plaintiff might meet its evidentiary burden under this standard, noting “that the specific intent need not be proved by direct admissions of wrongdoing. Rather, the actions of the utility, taken as a whole, can and should be considered.” *Id.*

132. The court in *City of Anaheim* did not itself find a violation of section 2 under the price squeeze theory. See *id.* at 1379.

133. See, e.g., *City of Kirkwood v. Union Elec. Co.*, 671 F.2d 1173 (8th Cir. 1982); *City of Groton v. Conn. Light & Power Co.*, 662 F.2d 921 (2d Cir. 1981); *City of Mishawaka v. Am. Elec. Power Co.*, 616 F.2d 976 (7th Cir. 1980).

134. Cases post-*Town of Concord* have echoed its great skepticism regarding the price squeeze claim. See, e.g., *City of Anaheim v. FERC*, 941 F.2d 1234, 1250-51 (D.C. Cir. 1991).

135. Spiwak, *supra* note 112, at 93.

#### IV. PRICE SQUEEZE IN A DEREGULATED ELECTRIC POWER INDUSTRY

This Part examines the claim of price squeeze in the deregulatory environment that has encapsulated the electric power industry in recent years. The first Section discusses the industry's move away from cost-of-service rate regulation for wholesale transactions to wholesale deregulation by allowing firms meeting certain conditions to leave the pricing of their wholesale electricity service to market-driven forces. The second Section introduces the doctrine of primary jurisdiction and describes the role it might play—in conjunction with the use of market-based ratemaking for wholesale transactions—in antitrust cases alleging price squeeze. This Part then addresses a potential objection to the use of the doctrine of primary jurisdiction in price squeeze cases arising in a deregulated electric power industry. Finally, this Part questions whether there is any role left for the claim in the context of electric power.

##### A. Market-Based Rates

Rate-of-return regulation has been subjected to a good deal of criticism. Chief among this criticism is the model of “regulatory bias” set forth by Harvey Averch and Leland Johnson.<sup>136</sup> In essence, Averch and Johnson posited that reliance on rate-of-return regulation would result in firms inefficiently substituting capital for other inputs.<sup>137</sup> Whether the “A-J Effect”, as Averch and Johnson's hypothesis has come to be called, is actually present in the electric power industry is subject to some debate.<sup>138</sup> Regardless, the lesson that has been drawn from discussion of the A-J Effect is that perva-

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136. Harvey Averch & Leland L. Johnson, *Behavior of the Firm Under Regulatory Constraint*, 52 AM. ECON. REV. 1052 (1962).

137. Averch and Johnson summarily stated the matter in the introduction to their paper:

[A] “regulatory bias” operates in the following manner: (1) The firm does not equate marginal rates of factor substitution to the ratio of factor costs; therefore the firm operates inefficiently in the sense that (social) cost is not minimized at the output it selects. (2) The firm has an incentive to expand into other regulated markets, even if it operates at a (long-run) loss in these markets; therefore, it may drive out other firms, or discourage their entry into these other markets, even though the competing firms may be lower-cost producers.

*Id.* at 1052. For a thorough but simplified economic analysis of the A-J effect, see VISCUSI ET AL., *supra* note 104, at 387-91.

138. See Hammond, *supra* note 35, at 53 (discussing empirical findings in support of and refuting the actual presence of the A-J Effect); VISCUSI ET AL., *supra* note 104, at 390 (noting the difficulty of testing the A-J Effect empirically and citing literature finding both the presence and absence of the A-J Effect in the electric power industry). If, in fact, the A-J Effect is present in the electric power industry, it may even have beneficial effects. See *id.* at 391 (suggesting that technological advancement might be one beneficial effect arising from the substitution of capital for other inputs).

sive regulatory schemes often fail in their attempts to facilitate industry operations as if they were subject to market forces.<sup>139</sup>

The potential inefficiencies associated with cost-of-service ratemaking have led federal and—to a lesser but growing extent—state regulators to experiment with different ratemaking methods. There is no statutory language at the federal level requiring regulators to partake in cost-of-service ratemaking. The Federal Power Act simply prescribes baseline standards requiring that rates be “just and reasonable”<sup>140</sup> and not “preferential.”<sup>141</sup> Taking advantage of the flexibility afforded by the just-and-reasonable standard, regulators have increasingly been experimenting with market-based ratemaking in an attempt to more closely mimic competitive markets in electric power.<sup>142</sup>

Despite the regulatory leeway provided by the just-and-reasonable standard, it is clear that FERC does not have the authority to simply leave the setting of rates entirely to market forces. In *Farmers Union Central Exchange, Inc. v. FERC*,<sup>143</sup> the D.C. Circuit rejected an attempt by FERC to subject oil pipeline ratemaking to competitive forces constrained by price caps set high enough to ensnare only flagrantly noncompetitive rates.<sup>144</sup> In addition to reaffirming the necessity of setting rates within the bounds set forth by the just-and-reasonable standard—bounds now clearly violated at the margin by relying on market-based rates subject only to high price caps—the D.C. Circuit made clear that FERC was imbued with responsibility under the Federal Power Act to actively monitor rates to ensure they remain within a zone of reasonableness.<sup>145</sup>

In the electric power industry, use of market-based ratemaking has proceeded incrementally. In *Citizens Power & Light Corp.*,<sup>146</sup> FERC approved market-based rates for a power marketer that owned

139. See Hammond, *supra* note 35, at 54 (suggesting that “the A-J debate is a further illustration of how extremely difficult it is to mimick [sic] the competitive market via regulatory fiat”).

140. 16 U.S.C. § 824d(a) (2000).

141. *Id.* § 824e(a).

142. There is some question in the literature as to whether the Federal Power Act can support market-based ratemaking by FERC. Compare Gerald Norlander, *May the FERC Rely on Markets to Set Electric Rates?*, 24 ENERGY L.J. 65 (2003) (concluding that FERC does not have authority under the Federal Power Act to engage in market-based ratemaking), with Michael J. Gergen et al., *Market-Based Ratemaking and the Western Energy Crisis of 2000 and 2001*, 24 ENERGY L.J. 321 (2003) (concluding that FERC does have authority under the Federal Power Act to engage in market-based ratemaking). This Article is agnostic on the legality of FERC engaging in market-based ratemaking under the Federal Power Act. All that matters for purposes of this Article is that FERC is currently using the market-based ratemaking standard in the electric power industry.

143. 734 F.2d 1486 (D.C. Cir. 1984).

144. *Id.* at 1507.

145. *Id.* at 1509-10.

146. 48 F.E.R.C. ¶ 61,210 (1989).

neither transmission nor generation facilities, lacked market power, and was not engaged in self-dealing.<sup>147</sup> In approving the use of market-based rates, FERC recognized potential procompetitive benefits and touted the likelihood that the rate-setting scheme would serve as an accurate proxy for operation in a competitive market:

Allowing Citizens Power the pricing flexibility it requests would undoubtedly permit it to respond quickly to changing market conditions and to be more effective. Pricing flexibility would also help to ensure that prices accurately reflect market conditions of scarcity or abundance and, to the extent it allows Citizens Power to succeed, it would further the Commission's statutory goals of promoting efficiency and coordination.<sup>148</sup>

Despite the purported efficiency gains in allowing for market-based rates, FERC recognized the potential for danger should a firm subject to market-based rates begin to engage in self-dealing or acquire market power.<sup>149</sup> To ensure the procompetitive benefits of market-based ratemaking were not usurped by anticompetitive tendencies, FERC levied three conditions on the approval of the new rate-setting standard. First, the firm in question was not allowed to own any transmission facility, affiliate with a firm that owned any transmission facility, or affiliate with a firm that held a franchised service area.<sup>150</sup> Second, the firm was to make filings regarding its contracts for the sale and purchase of generation and transmission contracts for review by FERC as a measure to ensure the firm was not obtaining significant market power.<sup>151</sup> Third, as an additional device to ensure against the obtainment of significant market power, FERC

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147. *Id.* ¶¶ 61,776-77. According to FERC, “[s]elf-dealing occurs when a marketer sells to or buys from an affiliate on terms that are more favorable than those that would be available to other market participants.” *Id.* ¶ 61,777.

148. *Id.* ¶ 61,777.

149. *See id.* (“While allowing pricing flexibility to Citizens Power can produce benefits, however, there are two potential abuses which we must guard against: self-dealing and the exercise of market power.”).

150. *Id.* ¶ 61,778.

151. *Id.* FERC was clear that guarding against the obtainment of significant market power was a primary concern. A host of conditions were placed on the filing documents pertaining to the contracts:

For each purchase contract and sale contract, Citizens Power should provide the following information: the buyer's or seller's name; a brief description of the service, including degree of firmness; the delivery points for each service; the price of each service; the quantities to be served or purchased; the contract's duration; the buyer's certification that it is paying a rate at or below its expected cost of alternative electric power; and any other attributes of the product being purchased or sold which contribute to its market value. Citizens Power shall file this contract information quarterly as to all contracts signed within the time period. Citizens Power must file this information within thirty days of the end of each quarterly period.

*Id.*

noted that the public would be allowed to file complaints against the firm alleging the existence of market power.<sup>152</sup>

FERC opened the door to widespread use of market-based rate-making in 1994, with its opinion in *Heartland Energy Services, Inc.*<sup>153</sup> In *Heartland*, FERC, for the first time, approved the setting of market-based rates for an affiliate of a vertically integrated utility with ownership over generation and transmission facilities.<sup>154</sup> *Heartland* also clarified the applicable framework for determining whether a particular firm is eligible to obtain rate approval based on market standards or maintain rates based on market standards:

The Commission's general standard is to allow market-based rates if the seller (and each of its affiliates) does not have, or has adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. In addition, the Commission considers whether there is evidence of affiliate abuse or reciprocal dealing. In evaluating specific transactions (*e.g.*, independent power producers selling their entire output under a long-term contract), the Commission examines the circumstances surrounding the transaction against these standards. In evaluating requests for open-ended, market rate authority, the Commission uses these same general standards but also implements reporting and periodic review requirements because it will not have the opportunity to examine the particular circumstances of each transaction.<sup>155</sup>

Thus, to obtain approval under the market-based standard, a firm must show that it does not have significant market power over transmission or generation. If the firm does have market power, it must mitigate that market power to a threshold degree acceptable to FERC. The firm must also not have erected any significant barriers to entry, or have engaged in any "affiliate abuse or reciprocal dealing."<sup>156</sup> Finally, firms are subject to continual oversight by FERC to ensure these standards are not violated.<sup>157</sup>

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152. *Id.* ¶ 61,779.

153. 68 F.E.R.C. ¶ 61,223 (1994).

154. *Id.* ¶ 62,060.

155. *Id.* ¶¶ 62,060-61.

156. *Id.* ¶ 62,060.

157. FERC required the following from *Heartland* to comply with the oversight of the market-based regime:

We thus direct *Heartland* to inform the Commission promptly of any change in status that would reflect a departure from the characteristics the Commission has relied upon in approving market-based pricing. These include but are not limited to: (1) ownership of generation or transmission facilities or inputs to electric power production other than fuel supplies; (2) affiliation with any entity other than WP&L that owns generation or transmission facilities or inputs to electric power production, or affiliation with another entity (other than WP&L) that has a franchised service area; or (3) business and financial arrangements in the United States, Canada, Puerto Rico, or Mexico involving



At first glance, it appears that the increasing use of market-based ratemaking in electric power will increase the likelihood that integrated firms will be able to successfully effectuate a price squeeze on rivals. This is because the market-based rates are not subject to the same type of regulatory scrutiny that cost-of-service regulation has been held to. But one key feature of the market-based ratemaking process suggests that it will be unlikely that firms will be able to take advantage of the differing ratemaking procedure to effectuate a price squeeze. In order for firms to have market-based rates approved, they must demonstrate an absence of significant market power. As long as regulators remain steadfast in keeping a watch on market power, firms are unlikely to be able to take advantage of relaxed ratemaking procedures in order to effectuate a price squeeze, because without market power it would be increasingly difficult to effectuate a squeeze. The opening of wholesale markets to competition also makes it less likely that an integrated firm will effectuate a squeeze. With open-access transmission now the norm in electric power, should a firm attempt a squeeze on a wholesale customer, that customer would have competitive options. For example, the squeezed firm might wheel power from another supplier or build transmission lines to another supplier.

### B. Primary Jurisdiction

The doctrine of primary jurisdiction is a judge-made rule of construction that allocates decisionmaking authority between federal courts and agencies when the two share jurisdictional authority.<sup>158</sup>

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Heartland or any entity affiliated with Heartland and the entities that buy from or sell power to Heartland. We also direct Heartland to notify the Commission if it sells to, purchases from, or obtains transmission from a utility that has any business relationship with any of Heartland's affiliates, including WP&L.

*Id.* ¶ 62,066. Since *Heartland*, FERC has granted the option of updated market analysis reports every three years subject to the understanding that FERC may require such a report at any time. See *Delmarva Power & Light Co.*, 76 F.E.R.C. ¶¶ 61,331, 62,584 (1996). Moreover, FERC now requires firms with rates set under the market-based standard to file quarterly reports on wholesale power sales made during the relevant period. Revised Public Utility Filing Requirements, Order No. 2001, 67 FERC Stats. & Regs. ¶ 31,127 (2002), *reh'g denied*, Order No. 2001-A, 100 FERC ¶ 61,074 (2002), *reh'g denied*, Order No. 2001-B, 100 FERC ¶ 61,342 (2002); see also Order No. 2001-F, 106 F.E.R.C. ¶¶ 61,060, 61,193 (2004).

On April 25, 2002, the Commission issued Order No. 2001, a Final Rule establishing revised public utility filing requirements. The rule requires public utilities to electronically file quarterly reports (Electric Quarterly Reports) summarizing specified pertinent data about their currently effective contracts (contract data) and data about wholesale power sales they made during the reporting period (transaction data).

*Id.* ¶ 61,060.

158. 1A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION, ¶ 245c, at 93 (2000) ("As a basic premise,

The doctrine of primary jurisdiction is temporal in nature rather than strictly authoritative with respect to ultimate decisionmaking power. Courts invoking the doctrine do so to delay action until the agency has had an opportunity to consider the issue; however, they retain the ultimate authority to decide the issue before them.<sup>159</sup> The principal jurisprudential basis for invoking the doctrine of primary jurisdiction is to promote uniformity by affording deference to expert agencies charged with oversight of the relevant regulatory regime.<sup>160</sup> By relying on the doctrine of primary jurisdiction, courts are able to take advantage of agency expertise, which better allows for the facilitation of “accommodation between the antitrust and the regulatory regimes.”<sup>161</sup> The doctrine is sufficiently broad, though, so as to allow courts to make differing determinations than the expert agency, should the facts before them so warrant.<sup>162</sup>

The potential applicability of the doctrine of primary jurisdiction to price squeeze claims in the context of electric power has long been recognized. Professor Lopatka, for example, has written that “[i]t is difficult to imagine a more appropriate case for the exercise of primary jurisdiction based on agency expertise than the utility price squeeze.”<sup>163</sup> He also noted that

a court may not be able to determine whether a price squeeze exists without expert assistance. Identification of a price squeeze requires an analysis of price and cost. With respect to most commodities, identical units manufactured by the same producer will have the same costs, so that identification of a squeeze will focus on price. The cost of electricity, however, varies on the basis of a

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the purpose of the ‘primary jurisdiction’ doctrine is to allocate decision-making power between two different departments of the federal government: the courts on the one hand and the regulatory agencies of the executive branch on the other.”).

159. See, e.g., Lopatka, *supra* note 7, at 607; Andrew G. Humphrey, Comment, *Anti-trust Jurisdiction and Remedies in an Electric Utility Price Squeeze*, 52 U. CHI. L. REV. 1090, 1105 (1985).

160. The Supreme Court noted:

Uniformity and consistency in the regulation of business entrusted to a particular agency are secured, and the limited functions of review by the judiciary are more rationally exercised, by preliminary resort for ascertaining and interpreting the circumstances underlying legal issues to agencies that are better equipped than courts by specialization, by insight gained through experience, and by more flexible procedure.

*Far E. Conference v. United States*, 342 U.S. 570, 574-75 (1952).

161. *Ricci v. Chi. Mercantile Exch.*, 409 U.S. 289, 307 (1973).

162. See Jim Rossi, *Lowering the Filed Tariff Shield: Judicial Enforcement for a Deregulatory Era*, 56 VAND. L. REV. 1591, 1650-53 (2003) (discussing the flexibility of primary jurisdiction, Rossi notes that it offers courts a promising way to confront the challenge of applying the antitrust laws in regulated industries while also recognizing its ability to leave key decisionmaking authority in the hands of courts).

163. Lopatka, *supra* note 7, at 607.

myriad of factors, and FERC is infinitely more adept at assessing these factors than a court.<sup>164</sup>

Courts have not consistently shared Professor Lopatka's enthusiasm for the applicability of primary jurisdiction to the electric power price squeeze claim. Some courts have found FERC's institutional expertise relevant in examining the claim of price squeeze.<sup>165</sup> Other courts, however, have refused to defer to FERC on the basis of agency expertise or notions of uniformity when examining the electric utility price squeeze.<sup>166</sup> The next Section examines the applicability of primary jurisdiction to the price squeeze claim in a deregulated electric power industry.

### C. Institutional Competence

As wholesale deregulation and open-access transmission become the norm in electric power, the price squeeze claim will take on a different shape than in the past. While the price squeeze has diminished as a viable cause of action in the electric power industry after *Town of Concord* and other unsympathetic judicial opinions rendered the claim, at best, a shot in the dark, deregulation may bring about an increase in price squeeze claims due to changing industry characteristics that distinguish present situational factors from those faced by courts analyzing the claim in a more fully regulated industry.<sup>167</sup> Where there is market power in transmission and market-based rates have not been implemented, or where deregulatory efforts are otherwise not in play, courts will most likely continue to adhere to the framework for analyzing the squeeze developed in cases like *Town of Concord*. Where deregulatory efforts are apparent, though, and the question before antitrust courts concerns a price squeeze brought about by wholesale rates set under FERC's market-based standard, antitrust courts will be faced with a new set of issues.

As discussed previously, before a firm is eligible for ratemaking under the market-based standard it must show that it does not have significant market power. Moreover, the petitioning firm—if its request is granted—must meet compliance standards and remain in a close working relationship with FERC so that the agency can determine whether the firm acquires significant market power post-rate approval—an event that would then render the firm an inappropri-

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164. *Id.* at 607-08 (emphasis and footnote omitted).

165. See Humphrey, *supra* note 159, at 1105.

166. See *City of Mishawaka v. Ind. & Mich. Elec. Co.*, 560 F.2d 1314, 1321-24 (7th Cir. 1977).

167. The United States Bankruptcy Court for the Northern District of California recently refused to find that Pacific Gas and Electric Company engaged in a price squeeze in the deregulated environment. See *In re Pac. Gas & Elec. Co.*, 295 B.R. 635 (Bankr. N.D. Cal. 2003).

ate benefactor of market-based ratemaking. If a firm's wholesale rates set under a market-based standard are challenged as part of a claim of price squeeze, a court may find invoking the doctrine of primary jurisdiction a useful measure to help guide it in determining whether a predatory price squeeze—that is, a price squeeze that antitrust courts should condemn—is at play. As a Sherman Act section 2 claim, antitrust liability for price squeeze is premised first on a finding of market power.<sup>168</sup> If the defendant firm does not have market power, it cannot be liable for price squeeze.

Because FERC approval of an application for market-based rates is conditioned on a finding that the firm does not have market power, and continued use of market-based rates is conditioned on ongoing evidence that the firm in question lacks market power, courts will most likely find it useful to invoke the doctrine of primary jurisdiction and defer, at least to some extent, to the agency's determination that the firm in question lacked market power. Presumably, under FERC's stated decisional guidelines for determining whether a firm is eligible to have its rates set using market-based standards, the agency makes detailed and credible findings of whether a particular firm possesses market power before allowing a firm to use market-based rates.

Recently, at least one commentator has questioned whether FERC enjoys the institutional competence to make a market power determination when considering a particular firm's eligibility for market-based rates. Using California's deregulation failures as a backdrop, this commentator has argued:

These “market-based” tariffs were new to FERC and dramatically different from the fixed “cost-of-service” tariffs with which FERC had the most experience. Indeed, FERC's cursory analysis of these new tariffs hints at the Agency's inexperience; it analyzed these applications solely by looking at the market share of each WEG, and being satisfied there was insufficient market share to manipulate the market, approved the applications. Unlike “cost-of-service” rates, FERC never evaluated a fixed number under its “just and reasonable” standard, but instead approved a process by which the WEGs would sell wholesale electricity in California.<sup>169</sup>

In addition to providing only a “cursory analysis” of market power during and after a firm's application for market-based rates, it may be that “FERC lacks meaningful experience with deregulated, competitive electricity markets due to its concentration on the highly

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168. See *supra* note 121.

169. Robert B. Martin, III, Note, *Sherman Shorts Out: The Dimming of Antitrust Enforcement in the California Electricity Crisis*, 55 HASTINGS L.J. 271, 298 (2003) (footnotes omitted).

regulated markets of the past.”<sup>170</sup> If so, courts will not want to blindly defer to the agency’s market power determinations. But the doctrine of primary jurisdiction is not premised on blind deference to the determinations of supposedly expert agencies. Conceptualized properly, the doctrine of primary jurisdiction can be invoked as a decision-making guide whereby courts use their accumulated judgment to glean that information deserving of deference and special consideration from uninformed and unsubstantiated findings. In the case of FERC’s review of market-based rate applications, it is quite unlikely that any existing inexperience or lack of expertise will continue far into the future. As FERC receives internal and external feedback and gains experience administering market-based rates, courts will increasingly be able to rely on its findings as valuable decisional guideposts.

#### D. Whither the Price Squeeze?

As a matter of economic theory, the claim of price squeeze as anti-competitive conduct is tenuous. A price squeeze may be grounded in procompetitive conduct or conduct otherwise not properly within the purview of the antitrust laws.<sup>171</sup> Antitrust courts must be cautious when examining the theory to ensure its application does not result in harm to competition and conduct generally beneficial to consumers. Given the complex economic underpinnings of the claim, the best option may be to abolish the theory as an antitrust cause of action where theories that have been better developed are able to serve as a framework of analysis for the conduct at issue. To the extent this is not possible or not likely in electric power, antitrust courts should continue to adhere to the skeptical approach to the claim advanced in *Town of Concord* and its progeny.

As wholesale deregulation and industry restructuring become the norm in electric power, antitrust courts will face new issues when examining the price squeeze claim. Perhaps of greatest interest is that a firm engaged in market-based ratemaking in wholesale transactions will have had to convince FERC that it lacks market power, and it will be required to continually show the absence of market power by making continuing filings with the agency. To the extent FERC’s market power determinations are accurate, the employment of market-based ratemaking forecloses the applicability of price squeeze as a Sherman Act section 2 violation.<sup>172</sup> Antitrust courts con-

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170. *Id.* at 306.

171. *See supra* Part III.

172. Other defenses may be available to defendant firms alleged to have effectuated a price squeeze. Although a complete discussion of how these defenses might apply in a deregulated electric power industry is beyond the scope of this Comment, examples of potential defenses include state action immunity and Noerr-Pennington immunity. *See Lopatka,*

sidering the claim of price squeeze effectuated by a firm engaged in wholesale transactions at market-based rates will want to take advantage of FERC's findings and determinations on the market power issue, and may do so by invoking the doctrine of primary jurisdiction as a measure of deference to FERC as an expert decisionmaking body on the issue of market power in the electric power industry. It has been suggested that FERC currently remains inexperienced in this mode. If so, courts will not want to blindly defer to FERC with respect to its market power determinations. As FERC gains experience with administering market-based rates, courts will find it easier to rely on FERC's findings and determinations. As deference to FERC increases over time, the price squeeze claim will likely lose much of its bite in cases concerned with wholesale rates set under market-based standards pursuant to approval and continual oversight by FERC.

## V. CONCLUSION

The transition from wholesale cost-of-service regulation to wholesale deregulation changes the landscape of applicability of the theory of price squeeze to the electric power industry. In the deregulatory environment, a firm must show that it does not possess market power before it is allowed to take advantage of the regulatory flexibility imbued by market-based rate-setting standards. If FERC's initial determination and continuing judgment that a firm lacks market power is accurate, it is unlikely that a firm using market-based rates in the sale of electricity at wholesale will be able to effectuate a price squeeze. As a matter of law, the familiar vehicle for bringing price squeeze claims—section 2 of the Sherman Act—requires first showing that a firm has market power in order to move forward with a substantive claim. Thus, an accurate showing that market power is absent appears to virtually foreclose a firm from being found liable for violation of section 2 of the Sherman Act under a theory of price squeeze.

Antitrust courts examining the theory of price squeeze where open-access transmission increases competitive options and wholesale rate deregulation suggests that the firm in question does not possess market power should embrace the doctrine of primary jurisdiction. Embracing the doctrine of primary jurisdiction assumes a degree of deference to FERC as an expert decision-making body that is able to analyze applicable structural and situational forces in the electric power industry to properly determine whether a particular

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*supra* note 7, at 617-35; Keith A. Rowley, Note, *Immunity from Regulatory Price Squeeze Claims: From Keogh, Parker, and Noerr to Town of Concord and Beyond*, 70 TEX. L. REV. 399 (1991).

firm has market power. To the extent FERC's experience and expertise in this mode have been accurately questioned, it should be remembered that the doctrine of primary jurisdiction does not require blind deference to the judgments of an agency. Courts ultimately retain final authority under the doctrine and presumably are able to appropriately discount an agency's findings if confronted with evidence that its decisionmaking processes or other situational factors make it prone to error. As FERC gains experience with implementing its market-based rate standards, it will likely produce judgments concerning the existence of market power that are of higher quality and of better use to antitrust courts considering the issue of price squeeze.

To the extent market power in transmission and continued use of cost-of-service ratemaking in this area remain prevalent, the skeptical approach to the price squeeze claim proffered by *Town of Concord* and its progeny remains the favored course of analysis to avoid chilling procompetitive conduct or preventing practices that are otherwise outside the scope of condemnation under the antitrust laws. But to the extent wholesale deregulation is relevant in future price squeeze cases arising in the context of electric power, courts should be even more skeptical of the claim given FERC's already existing determination that the firm in question lacked market power. Combined with the skeptical conceptualization of the price squeeze advanced by *Town of Concord* and its progeny, further justifications for skepticism of the claim advanced by theoretical work grounded in economics, and evidence that market power is nonexistent, the price squeeze claim is almost certainly a losing one in a deregulated electric power industry when a firm has been granted the ability, by FERC, to partake in the setting of wholesale rates using market-based standards. While recent developments in electric power do not signal the death of the price squeeze as a viable antitrust cause of action, it is increasingly unlikely that it will serve as a successful vehicle for plaintiffs in antitrust suits against electric power firms in an era of deregulation.

