

**American Electric Power Company, Inc. and**            )  
**Central and South West Corporation**                )       **File No. 70-9381**

**NOTICE OF APPEARANCE, PROTEST,  
COMMENTS, MOTION TO INTERVENE**

of the

**Ohio Consumers' Counsel  
West Virginia Consumer Advocate Division  
Indiana Office of Utility Consumer Counselor  
Missouri Office of Public Counsel  
Attorney General of Oklahoma  
Electricity Consumers Resource Council  
Industrial Energy Users - Ohio  
Public Citizen  
Ohio Partners for Affordable Energy,  
Citizens Action Coalition of Indiana  
Environmental Law and Policy Center  
Intervenors**

Pursuant to SEC Release No. 35-26989, 64 Federal Register 12391-96 (Mar. 12, 1999), the Ohio Consumers' Counsel, the West Virginia Consumer Advocate, Indiana Office of Utility Consumer Advocate, Missouri Office of the Public Counsel, Attorney General of Oklahoma, Electricity Consumers Resource Council, Industrial Energy Users - Ohio, Public Citizen, Ohio Partners for Affordable Energy, Citizen Action Coalition of Indiana, and the Environmental Law and Policy Center, through their undersigned counsel, hereby notice their appearance, move to intervene, protest this filing and file these comments concerning the merger of American Electric Power (AEP) and Central and South West (CSW).

The Ohio Consumers' Counsel (OCC), the West Virginia Consumer Advocate Division, the Indiana Office of Utility Consumer Advocate, and Missouri Office of Public Counsel are the statutory representatives of their respective states' residential utility consumers before state and federal regulatory

and legislative bodies, and the courts. Their interest in this case is in protecting consumers from immediate and long-term harm, as well as in retaining sufficient regulatory protections and structures to effectively protect consumers.

The Oklahoma Attorney General has the statutory responsibility to represent and protect the collective interests of all utility consumers of the state. Pursuant to this statutory authority, the Attorney General has standing not only before the Oklahoma Corporation Commission, but also before all state and federal courts and administrative agencies where the interests of Oklahoma utility consumers may be affected.

IEU-OH has 36 members with manufacturing facilities located throughout Ohio including the areas served by Ohio Power Company and Columbus Southern Power. IEU-OH's members spend about \$1.5 billion each year on electricity and natural gas to operate their Ohio plants and have been active participants in local, state, regional and federal proceedings related to policies and issues that affect the availability and price of energy and related services.

Public Citizen, founded by Ralph Nader in 1971, is a non-profit research, lobbying, and litigation organization based in Washington, DC. Public Citizen advocates for consumer protection and for government and corporate accountability, and is supported by over 120,000 members throughout the United States, with members in Texas, Oklahoma, Indiana, Michigan, Ohio, Kentucky, West Virginia, Tennessee and Virginia.

Ohio Partners for Affordable Energy is an organization formed to advocate for affordable energy policies on behalf of low and moderate income consumers and to provide a forum to facilitate the formation

of public and private sector partnerships to provide cost effective energy efficiency services to low and moderate income Ohio residents.

The Electricity Consumers Resource Council (ELCON) is an association of 34 large industrial consumers of electricity. Its members have facilities in most of the fifty states and throughout the world. They produce a wide range of products including aluminum, steel, chemicals, motor vehicles, computer chips,, petroleum, glass, paper, food products and rubber. These companies require an adequate and reliable supply of electricity at competitive prices.

The Citizens Action Coalition of Indiana is a 501.c.4 not for profit corporation with approximately 300,000 members and contributors, almost exclusively comprised of residential utility consumers of Indiana utility companies, including Indiana Michigan Power Company, dba. AEP Indiana.

The Environmental Law and Policy Center is a Chicago based regional environmental organization that provides technical and legal services to citizen groups throughout the Midwest, including in Michigan, Indiana and Ohio.

For the reasons provided below, the proposed merger must be rejected because it would result in numerous violations of Sections 10(c) of the Public Utility Holding Company Act (PUHCA). Acceptance of this Application will leave the public unprotected from holding company acquisitions that sacrifice operational efficiency for expansionism.

## **Introduction**

Section 10(c)(1) requires that the acquisition not be detrimental to the carrying out of Section 11(b)(1). Section 11(b)(1) requires each registered holding company to be limited to a "single integrated public utility system." There is an exception to this rule permitting retention of an additional system, but Applicants do not rely on this exception. The question, therefore, is whether the merged enterprise will be a "single integrated public-utility system."

Section 2(a)(29)(A) defines "single integrated public-utility system," as applied to an electric utility company, as

a system consisting of one or more units of generating plants and/or transmission lines and/or distributing facilities, whose utility assets, whether owned by one or more electric utility companies, are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation....

The purpose behind the incorporation of the integration standard into Section 10(c)(1), through Section 11(b)(1), through the reference in the former to the latter, is to prevent acquisitions that were motivated by acquisitiveness rather than efficiency. Before passage of PUHCA, a holding company might have owned utility companies scattered across the nation. PUHCA required the SEC to break up these companies and create a set of utility systems that controlled largely adjacent properties. To prevent recurrence of the pre-PUHCA structure, the acquisition tests of Sections 10(c)(1), 11(b)(1) and 2(a)(29)(A) require interconnection and integration of any post-acquisition segments.

The Applicants do not meet the acquisition tests, for multiple distinct reasons.

**First**, they propose to "integrate" their companies using a transmission contract for 250 MW with Ameren (the product of a merger between Union Electric and Central Illinois Public Service Company) through May 31, 2003. But as explained below, Applicants cannot create a "single integrated public-utility system" by connecting a 23,000 MW system and a 14,000 MW system with a 250 MW, one-way temporary transmission contract. See Part I.A.

**Second**, in an effort to reduce the market power they gain from use of the 250 MW interconnection, the Applicants propose to give up most of their use of the high voltage direct current (HVDC) interconnections linking Texas with Oklahoma. We explain below that in doing so, Applicants will render CSW's Texas assets fatally separated from the remainder of the post-merger system, thereby creating a separate violation of the "single integrated public-utility system" test of Section 2(a)(29)(A). See Part I.B.

**Third**, we explain that the merged company will separately violate Section 2(a)(29)(A) because it will not be "confined in its operation to a single area or region." See Part I.C.

**Finally**, a separate violation of Section 10(c) exists because the acquisition does not satisfy Section 10(c)(2), which requires each acquisition to "serve the public interest by tending towards the economical and efficient development of an integrated public-utility system." The Applicants cannot satisfy the "economical and efficient development" test by selling off generation used presently to integrate the system.

See Part II.

**I. The Merged Company Will Not Be Limited to a "Single Integrated Public-Utility System" as Required by Section 11(b)(1)**

**A. Applicants Cannot Create a "Single Integrated Public-Utility System" By Connecting a 23,000 MW system and a 14,000 MW System With a 250 MW, One-Way Temporary Transmission Contract**

**1. The Size of the Interconnection is Insufficient**

The Ameren transmission contract is for a very limited amount of capacity for a limited number of years. Connecting a 23,000 MW system with a 14,000 MW system by means of a 250 MW, one-way transmission contract does not constitute "integration" in the way Congress intended the phrase or in the way the SEC historically applied the statute. Integration means joint operations, not a token wire path. In none of the integration cases decided under the Act has the actual integration been so insignificant relative to the size of the merged company.

The merged company cannot be a "coordinated system." There are two systems. The components within each system are tied together through coordination agreements and some central dispatch. But there is no plan to coordinate the two previously separate systems through coordination and dispatch, except for insignificant amounts limited by the 250 MW interconnection. After the merger, therefore, there still will be two systems, not one. The Applicants make no pretense to being a single coordinated system after the merger. All that is "coordinated" is the transfer of a token amount of power between two huge systems.

The legal premise of Applicant's position (there is no factual premise) is that if one subsidiary of a holding company interconnects with one subsidiary of another holding company, the rest of each system comes along automatically and forms a single integrated system. But that cannot be true as a matter of law. Otherwise two companies could interconnect over a third by contract, and then each adjacent acquisition

made by each of the original two companies would necessarily produce a result that automatically satisfied the integrated public-utility system test. That is not the law. Interconnection alone does not equal integration.

## **2. Statutory Integration Cannot be Achieved With a Temporary Transmission Contract**

Applicants' Ameren contract right lasts only until 2003, leaving the merged company with no known way to interconnect, let alone integrate, its parts after the contract termination. But the Act requires that the interconnection plans must be in place at the time of the SEC's decision. Interpreting Section 2(a)(29)(A), the Commission has stated:

[S]eparate properties not interconnected must be capable of physical interconnection and of economic operation at the time the Commission considers the matter and not at some indefinite future time. The term 'normal conditions' mentioned in the definition does not refer to conditions which might possibly occur in the remote future and whose occurrence has not been foreshadowed by any facts shown in the record. General Public Utilities Corporation, 32 S.E.C. 807, 825 (1951). The Commission approves applications only after the plans for the interconnection either are certain or have been carried out. Thus in General Public Utilities, the Commission explained that its earlier rejection of the application was required since there were no immediate and concrete plans for interconnection. The Commission then approved the acquisition because the applicants had since built an interconnection. Compare American Gas and Electric Co., 32 S.E.C. 130 (1950) (finding Section 10(c)(2) satisfied where construction of interconnections would be completed within 20 months; no indication of blockages by other regulators).

General Public Utilities Corporation, 32 S.E.C. 807, 825 (1951).

A short-term agreement, followed by the mere possibility of construction, cannot satisfy the integration requirement. The SEC must find that arrangements will be in place throughout the life of the post-acquisition entity. A transmission agreement certainly need not last forever; but where it does not, the SEC has found that alternative or subsequent interconnection arrangements were certain. See, e.g., New

England Electric System, 38 S.E.C. 193, 198 (1958) (finding that "the necessary interconnections would be constructed forthwith if the present [transmission contract] arrangements with the non-affiliate companies were terminated" (emphasis added); Electric Energy, Inc., 38 S.E.C. 658 (1958) (acquiring companies had contractual use of necessary transmission facilities for the entire life of the acquired plant); Centerior Energy Corporation, 49 S.E.C. 472, 479 (1986) (transmission agreements had "no termination date and remain in effect as long as the [generation facilities at issue] are in existence); Northeast Utilities, 50 S.E.C. 427 (1990) (finding integration requirement satisfied where transmission contract was for at least ten years, and where companies were located within highly integrated power pool).

The Applicants have demonstrated no specific means of interconnecting their parts after expiration of the Ameren contract. Since they are purchasing "point-to-point" transmission service, FERC's Order 888 gives them no particular right to continue their transmission usage after contract expiration. Ameren's transmission capacity therefore will have to be made available on a first-come, first-served basis. There is no basis for assuming that any portion of the 250 MW, even if that quantity were sufficient to integrate the system, will be available to the merged company after expiration of the present contract. With the introduction of retail competition in the region, in fact, it is likely that there will be many other potential users of the 250 MW Ameren path, making it uncertain whether the Applicants will have any ability to continue even their symbolic interconnection effort.

As the case law cited above make clear, speculation about future integration is insufficient to satisfy the statute. In the recently affirmed WPL Holdings merger case, Madison Gas and Elec. Co. v. S.E.C., No. 98-1216 (D.C. Cir., Mar. 16, 1999), the Court of Appeals relied upon "Interstate's showing of a current transmission line contract and of an [alleged] plan to build two tie-lines of its own across the

Mississippi before the end of the contract term." Here, there is no comparable plan. There is only a temporary contract. The Commission, quite properly, has never found the requirement satisfied by a temporary contract only.

### **3. Applicants' Hopes for "ISOs" and Telecommunications Innovations Do Not Substitute for Real Integration**

Recognizing that their own plans fail to create an integrated system, the Applicants speculate about future regional developments, including the possible creation of an "independent system operator" covering the territory spanned by the merged company. There is no such independent system operator today, and no plans or efforts -- none -- to create one. In fact, AEP's ultimate refusal to participate in the Midwest Independent System Operator ("MISO") -- the only FERC approved regional transmission organization in the Midwest and the organization that AEP originally promoted -- means that the applicants' claims about the potential beneficial effects of these new institutions must not be allowed to create a false sense of security. Based on AEP's past MISO performance, it is clear that AEP's vague claims about its future intentions are hardly sufficient to protect the public interest or meet specific statutory requirements.

Even if such an effort were under way, the concept of "independent system operator" is too vague to be equated with the specific requirements of integration set forth in Section 2(a)(29)(A). The concept has no particular statutory or regulatory definition. It can be a central operator of transmission assets, whose control has been transferred to it by individual transmission owners. Or it can be a reviewer of transmission usage controlled by the transmission owners. It can have regional pricing plans which avoid the problem of multiple, duplicative and uneconomic transmission charges across multiple transmission systems (a so-called postage stamp or license plate rate), or it can require payment of multiple transmission

charges. It can have an independent staff and independent board, or its staff and board can consist of representatives from the various members. There is no set of requirements -- administrative, physical or economic -- that today define what is an "ISO."

An ISO is a paper organization until it develops real plans. Its ability to integrate the parts of a region depends entirely on those plans. But in the Application, "ISO" becomes a mantra -- a word to repeat when the law requires a substantive result and the Applicants are unable to supply it. The citation of the possible formation in the future of such an organization, without any specific features in place or even under discussion, cannot substitute for the real operational improvements which Section 2(a)(29)(A) demands.

The Applicants also attempt to fill the physical gap in their integration claim with literary allusions to the telecommunications revolution. All this eloquence means nothing if the only link is a 250 MW contract path. This fact is evident from the Application itself, which makes no verbal link between the discussion of telecommunications and the description of the contract path.

**B. By Giving Up Use of Its High Voltage Direct Current Ties Linking Texas With Oklahoma, CSW Will Render Its Texas Assets Fatally Separated From the Remainder of the System**

A separate violation of the "single integrated public-utility system" test occurs because CSW would reduce its use of interconnections that were constructed specifically for the purpose of integrating its utility subsidiaries. An acquisition cannot produce an integrated public utility system if it detaches a major part of the system. After providing some background on CSW's interconnection situation, we explain how Applicants' proposal effectively severs CSW's Texas portion from the rest of the system, rendering the Applicants unable to satisfy the integration test.

## 1. Background on the HVDC Ties

An understanding of this argument requires a summary of the history of the interconnection between two regions -- the Electric Reliability Council of Texas (ERCOT) and the Southwest Power Pool (SPP) -- and Applicants' role in that history.

CSW has four utility subsidiaries: two are located within ERCOT (Central Power & Light and West Texas Utilities), and two are located outside Texas in the SPP (Southwestern Electric Power Co. and Public Service of Oklahoma). For decades after the enactment of PUHCA, Texas was not electrically interconnected with the rest of the United States. Consequently, two of CSW's utility subsidiaries had no interconnection with the other two utility subsidiaries. Yet CSW existed as an SEC-approved holding company, obligated by statute to be an "integrated public utility system."

In the 1970s, municipal systems in Oklahoma brought to the SEC a complaint under PUHCA, asserting that CSW should face divestiture because of its decades-long failure to satisfy the integration requirement. The SEC set that matter for hearing. HCAR No. 19361 (January 30, 1976), as amended by HCAR No. 20031 (May 18, 1977). Faced with an obvious and multi-decade violation of the integration requirement, apparently tolerated by the Commission, CSW had to arrive at some means of satisfying the integration requirement. The result was the following:

- a. a decision to construct high voltage direct current (HVDC) interconnections between CSW's Texas and non-Texas segments. Direct current ties were chosen because the flows can literally be turned on or off, like a drawbridge, unlike the more traditional alternating current (AC) ties, in which power flows automatically. The use of DC ties allowed the company to limit Texas' electrical interactions with the outside world.
- b. the creation of a CSW Pool Agreement under which CSW would integrate its operations (with the extent of integration limited by the limitations of the HVDC ties), making use of the transmission capacity created and guaranteed by the HVDC ties.

- c. a finding by the SEC that the construction of the HVDC ties and the CSW Pool Agreement would result in CSW satisfying the integration requirement of PUHCA.
- d. Citation to and reliance on a special statement in the Federal Power Act stating that the construction of these ties will not make Texas utilities generally subject to the Federal Power Act. (Technically the Act authorized the FERC to order CSW to construct the HVDC ties, and stated that compliance with the FERC order would not subject CSW or any other utility in Texas to Federal Power Act jurisdiction, except for the limited purpose of determining the rates, terms and conditions for transmission use of the ties.) See "Order Requiring Interconnection and Wheeling, and Approving Settlement," Central Power and Light Company, Public Service Company of Oklahoma, Southwestern Electric Power Company, West Texas Utilities Company, 17 F.E.R.C. P61,078; 1981 FERC LEXIS 2508 (adopting a proposed order and finding, under Section 210 and 211 of the Federal Power Act, that compliance with the order would not make Texas Utilities or Houston Light and Power a "a "public utility", as that term is defined by section 201 of the Act, and subject to the jurisdiction of the Commission for any purpose other than for the purpose of carrying out the provisions of sections 210, 211, and 212 of the Act...."

As explained in the next section, the present Application would undo the integrating effects of the previous SEC approval order.

## **2. Applicants' Proposal in the Instant Case Would Undo the Integrating Effects of the HVDC Ties**

The Applicants are concerned that FERC will find that the merger will give them market power, particularly within ERCOT. As they have explained it, their 250 MW east-west transmission contract with Ameren (necessary so that they can appear to satisfy the PUHCA integration requirement) allows them to import 250 MW of power from AEP to CSW. This arrangement has the same effect, they say, as constructing a new 250 MW generator within CSW, and such construction would increase concentration levels for the merged company to a point which would cause FERC concern. The Applicants therefore have proposed various techniques for mitigating their market power.

One of the Applicants' mitigation proposals is to reduce their use of the HVDC ties. Applicants' witness Jones explains in his FERC (Supp. Testimony at 15-17) that they will

schedule their use of the two HVDC ties ... on a first-in-time basis for what are known as unplanned transactions in ERCOT and non-firm transactions in the SPP. This means that Applicants will stand in line with all other users to schedule the use of the ... HVDC ties between SPP and ERCOT to accomplish the central economic dispatch of the Applicants' post-merger system. In this way, the Applicants will have no advantage over other users for the hour-by-hour use of the ties to transfer energy between their SPP control area and their ERCOT control area. This waiver of priority will not apply to so-called planned transactions that are submitted to the ERCOT ISO or other transfers of firm capacity between the Applicants' SPP and ERCOT control areas, including the use of the North HVDC to export the output of the Oklaunion generation station to PSO and Oklahoma Municipal Power Authority in the SPP.

The waiver would remain in effect until the "earlier of the date on which an ISO of which the SPP operating companies are members begins to govern transmission access or the date on which the firm transmission reservation over the Ameren system ends. The current reservation [of Ameren capacity] will be in effect through May 31, 2003.

Id. at 16.

Although the proposal to share use of the HVDC ties certainly can reduce the Applicants' market power, it renders them unable to satisfy the integration test because it contradicts the premises of the SEC's finding that the construction of the ties enables CSW to satisfy the integration test. Specifically, the SEC found in its order in Central and South West, Release No. 22439, File No. 3-4951 (Apr. 1, 1982):

The record before FERC, and as supplemented in this proceeding, indicates that substantial savings are expected to be achieved in revenue requirements to ratepayers of the CSW subsidiaries from operation of the CSW system in an interconnected mode as a result of the planned interconnections between ERCOT and SWPP. The order issued by FERC finds, among other things, that the construction of the planned interconnection facilities "is in the public interest, will encourage overall conservation of energy and capital, will optimize the use of facilities and resources, and will improve the reliability of each electric utility system to which the order applies." The FERC order is a final order.

By ceding use of the HVDC ties to other entities, the Applicants alter the facts on which the Commission's decision in File No. 3-4951 was based. The Application therefore must fail.

We do not wish our argument to be interpreted as an argument for preserving Applicants' market power; rather, it is an observation that the Application must fail because the solution to Applicants' market power problem is a separate violation of the integration requirement.

**C. The Merged Company Will Not Be "Confined in Its Operations to a Single Area or Region"**

**1. The Applicants Cannot Meet the "Single Area or Region" Test of Sec. 2(a)(29)(A)**

The proposed entity will stretch west from Ohio across the Mississippi River and south to Texas, creating the largest electric holding company in the nation in terms of territory covered. If approved, the Applicants' proposal would obliterate any reasonable interpretation of the "single area or region" clause of Section 2(a)(29). Before this Application no credible person has ever suggested that Ohio and Texas are in a "single area or region."

**a. The Commission's Application of the "Single Area or Region" Standard**

The Commission's examination of the "single area or region" requirement has focused on such factors as size, industrial and business activity in the territories, marketing, transportation facilities, and basic geographical characteristics.

The size alone of the territory that is proposed to constitute an integrated system may be determinative of whether the "single area or region" standard is met. See Middle West Corp., Release No. 4846 (Jan. 25, 1944) ("[W]hen extremely large sections are considered .... distance alone may be

definitive."); Cities Service Power & Light, Release No. 4489 (Aug. 18, 1943) ("[T]erritory as vast as that covered by the States of Wyoming, Colorado, New Mexico and Arizona," spanning 900 miles from north to south, is not a single area or region under Section 2(a)(29)). See also PP&L Resources, Inc., Release Nos. 35-26905 (Aug. 12, 1998) (finding that a system will "operate in a single area or region" covering portions of Pennsylvania and Maryland where service territories of combining entities "are largely located in adjacent or nearby geographic areas and will in fact to a degree overlap").

When the size of the territory covered is not conclusive, various economic and business factors guide the assessment of what constitutes a single area or region. See Middle West, supra. Some of these factors include: industrial and business activity in the territories, marketing, transportation facilities, and basic geographical characteristics. In Middle West Corp., supra, the Commission assessed whether a group of utilities in the southwest could constitute a single area or region. The Commission observed that, in order to find a single region, it must conclude that a single area may consist of land stretching 400 miles north-to-south and 350 miles east-to-west. The Commission stated that "[i]n well-settled and economically developed territory such a finding might be impossible." Id. However, the Commission found the single area standard was met because

[t]he geographical characteristics of the territory encompassed by this sector of properties are fairly homogeneous. The area is more or less typical throughout, relying largely on oil and other minerals, agriculture, and relatively light industry for its subsistence. The rendition of satisfactory service in arid and sparsely-settled areas frequently requires the stretching of lines over long distances to connect small population centers with generating facilities strategically placed near suitable water and fuel supplies. In view of these facts we believe that the properties in question lie within a single area or region.

Id.

Discussing another set of companies in Middle West, the Commission emphasized that an area of more than 120,000 square miles is "enormous," such that "[i]t is only the nature of the area -- its sparse settlement, the difficulties of finding suitable generation locations because of water and fuel characteristics, the small sizes of communities widely separated and the necessity of stretching lines over long distances to accumulate load -- that would permit us to regard the territory served by these companies as embracing a single area or region." Id. (emphasis added). See also American Natural Gas Co., Release No. 15620 (Dec. 12, 1966) (accepting argument that service areas of Michigan, Wisconsin and Indiana utilities "are in a common economic and geographic region, taking into consideration such factors as industrial, marketing and general business activity, transportation facilities, and gas utility requirements"). As discussed next, the territory that would be occupied by the Applicants' proposed company fails the "single area or region" standard under any of the tests that the Commission has utilized.

**b. The Proposed Entity Will Not be Confined to a Single Region Regardless of How One Defines "Area" or "Region"**

Even considering technological and other industry advances over the past decades, it is difficult if not impossible to credibly assert that Texas and Ohio constitute the same area or region under any concept of those terms. Texas and Ohio are not by any standards "in a common economic and geographic region," American Natural Gas Co., supra, and the proposed entity would extend the total systems by hundreds of square miles. This expansion is far more than any of the previous cases in which the Commission has considered the distance by which a system territory would be increased as decisive for purposes of determining whether the "single area or region" requirement is met.

Most significantly, the merged entity fails the single region standard from the perspective of the industry. No power supply planners, no electric reliability technicians, no marketing strategists -- no one -- views Ohio and Texas as in the same region. For as long as anyone can remember, Texas has been grouped with Alaska and Hawaii as being its own region.

The chief reason that Texas is considered its own region is physical and regulatory. Until the 1980s, there was no physical interconnection (at least not one furnishing any commercial or reliability benefit) between utilities in Texas (excluding the relatively small portions of Texas located outside ERCOT) and those in other states. The reason has been the historic insistence by Texas utilities that Texas should be treated separately. This insistence has been accepted repeatedly by regulatory and political bodies. The Texas Public Utilities Commission regulates not only retail sales, but wholesale sales and the transmission of wholesale power, whereas wholesale sales and wholesale transmission occurring in every other state (other than Alaska and Hawaii) are subject to FERC's exclusive jurisdiction. Even the construction of the HVDC ties connecting CSW's ERCOT and non-ERCOT utility subsidiaries was accompanied by special legislation in 1978 preserving the state commission's exclusive authority over intra-Texas transactions, whether retail or wholesale. See below.

As a result of this physical gulf between Texas and the rest of the continental United States, a practice of "Texas is separate" has been entrenched in the industry. No reliability planning outside Texas takes into account resources or events inside Texas, and vice versa. Texas has its own reliability council, the Electric Reliability Council of Texas (ERCOT): the only reliability council in the continental U.S. confined to a single state and with the name of a state in its title.

Events since the 1980s have not changed these facts significantly. Although CSW did build high voltage direct current (HVDC) ties, Texas remains outside every credible dialogue concerning future regionalization of transmission planning and electric supply markets. The Energy Policy Act of 1992 recognizes this very fact. Subsection (k) of Section 212 is titled "ERCOT Utilities." The section states that

[a]ny order under section 211 requiring provision of transmission services in whole or in part within ERCOT shall provide that any ERCOT utility which is not a public utility and the transmission facilities of which are actually used for such transmission service is entitled to receive compensation ... on the transmission ratemaking methodology used by the Public Utility Commission of Texas.

Under this provision, FERC must base transmission service rates on "the rates for transmission services in ERCOT [based] on the ratemaking methodology that the Texas Commission uses." City of College Station, Texas, 86 F.E.R.C. para. 61,165 (Feb. 16, 1999). Texas is the only area of the country that is exempt from the ratemaking employed by FERC under the Federal Power Act and EPACT.

Even if Section 2(a)(29)(A) provided that an ISO could serve as a basis for finding that an expansive territory such as that proposed by Applicants was a single region, there is no such ISO, and no credible efforts to create one, by the Applicants themselves or by anyone else. This is why the Applicants are able only to emphasize the possibility of an ISO. In fact, the absence of an Ohio-to-Texas ISO, and the absence of any efforts to form one, is strong evidence that no one thinks of this territory as being part of a single region.

To assert now that Texas is in the same region as Ohio is to manufacture a result at odds with the statute and with reality. The Applicants want to define statutory terms to be consistent with their pecuniary

business strategy, but the purpose of the integrated system test was to put into the law objective protections for the public that were insulated from pecuniary strategies such as the Applicants'.

That AEP covers a region of seven states does not mean Applicants can play a numbers game by asserting that "'eleven' is not much bigger than 'seven.'" A simple look at the map shows that the "region" covered by AEP is not all of the seven states, but rather relatively closely connected territories in each of those states. The AEP system was largely the product of AEP's operating utilities' responsibilities as regulated public utility companies. Acquisitions were justified as means of minimizing costs, not as means of succeeding in the future competition. For example, the Commission justified the acquisition of Columbus and Southern Ohio Electric Company in 1978 on the grounds that "[t]hey fit together." American Electric Power Co., Release No. 20633 (July 21, 1978). The purpose and result of that acquisition was to include CSOE within a systemwide practice of joint planning and dispatch. Id. The acquisition of CSOE, today called Columbus Southern Power, was AEP's most recent acquisition of a utility subsidiary.

In contrast, the new proposed "region" covered by the merged company is not the product of past efforts to plan generation and transmission for the combined load, and there certainly is no plan to do so in the future (not with the miniscule interconnections between Texas and Oklahoma, and between AEP East and AEP West). The new proposed "region" is a product only of a desire of the two systems' corporate managers to increase the size and geographical scope of the enterprise.

The proposed entity would cover a territory comprising approximately one-fourth of the nation. The territory is well settled and highly developed. No factors make the "rendition of satisfactory service" difficult so as to support the need for an enormous system. Rather, as the Commission intimated in Middle West, the vast expanse of land covered without any ameliorating factors makes a finding of a single region

"impossible." As the Commission stated in Cities Service Power & Light, *supra*, the Applicants' proposal "would comprehend hegemonies of holding-company control so vast that (under the area or region standard) the Act would permit a few holding companies to divide the country."

**c. The Applicants' "Single Area or Region" Analysis Is Flawed**

The Applicants argue (Application at 62) that the terms "area" or "region" are capable of "flexible interpretation" and that the Commission may consider the "current state of the industry" to give the term "practical meaning and effect." They cite examples of integrated systems that span more than one state. They contend that "the concept of region is not constrained by geographical boundaries" nor by "regional designations which are part of the common vocabulary." *Id.* at 63. The Applicants argue that the proposed merger "represents a logical extension of the AEP System's existing territory in light of contemporary circumstances" and that "present realities" support a finding that a region can encompass four additional states more than AEP's seven-state region approved some 50 years ago. (App. at 64) They then claim that gas industry restructuring somehow supports their argument that Ohio and Texas should constitute a "single region." These arguments suffer from numerous flaws.

Nowhere do Applicants point to any specific evidence as to why AEP's operations in Ohio fall within the same region as CSW's operations in Texas. While they point out that, prior to the merger, the systems are separated at their closest point by "only" 150 miles, they fail to explain how that would support a finding that Columbus, Ohio and Corpus Christi, Texas are in the same "region." The question is not whether the systems constitute a single area by accounting only for the point at which they are closest, but rather whether the entire territory covered by the merged entity can constitute a single area. The utility subsidiaries of AEP and CSW are not adjacent and do not overlap, *see, e.g., PP&L Resources, Inc.,*

Release Nos. 35-26905 (Aug. 12, 1998), and Applicants point to no evidence as to why Texas -- historically and currently treated as its own area for purposes of reliability and regulation, see the previous section -- falls within the same region as Ohio.

Moreover, while it is true that the closest transmission facilities of AEP and CSW are separated by only about 150 miles, a far greater distance separates their service territories -- about 500 miles at their closest points.

The Commission must base any finding of a "single area or region" on substantial evidence. Applicants produce no evidence related to the factors the Commission has in the past considered important in determining whether the single region standard is met. They do not provide any specific information relating to how the proposed territory would constitute one region in terms of generation, fuel sources, marketing, transportation, community size, or any other factor the Commission has considered in the past.

The reason for the gaping hole in the Applicants' argument is obvious; as discussed in the previous section, by any industry or business measurement, Texas and Ohio are located in separate regions. Thus, without any concrete evidence as to why Texas and Ohio fall within the same region, Applicants are left with only vague assertions about the "increasingly competitive world," "contemporary circumstances" and "logical extensions" of existing territories, but no relevant evidence as to why the proposed entity would be "confined in its operations to a single area or region."

Furthermore, the Applicants' definition of a "single area or region" has no limits. Under Applicants' analysis, neither geographical boundaries, regional designations, business activities nor existing market structures determine what constitutes a single area for purposes of Section 2(a)(29). Rather, under

Applicants' reasoning, the key criterion is the future of electric industry restructuring, when "traditional boundaries will become more blurred and the contours of regional markets will change." (App. at 64)(emphasis added). Such a concept of region has no limitation and is left only to speculation about the future.

The closest the Applicants come to accepting any kind of limitation on what may constitute a single area is their proposal to apply the Commission's interpretation of Section 10(b)(1), which prohibits acquisitions that tend toward the "concentration of control" of public utility companies. This interpretation ignores Section 10(c)(1)'s requirement of a "single integrated public-utility system" and would delete Congress' explicit instruction that integrated systems be confined to "a single area or region."

The Applicants cite the Commission's decisions in Connecticut Yankee Atomic Power Co., Release No. 14968 (Nov. 15, 1963), and Vermont Yankee Nuclear Power Corp., Release No. 15958 (Feb. 6, 1968), as supporting their views on the interpretation of the "single area or region" standard. In particular, they cite to the statement in Vermont Yankee that "[i]n view of the existing state of the art of generation and transmission and the economic advantages of the proposed arrangement, Yankee may be deemed to be within the same area or region as each sponsor applicant...." If anything, however, the single sentence in each decision that references the single area standard demonstrates exactly why the proposed company cannot meet the standard. Both cases involve a combination of New England utilities and electric holding companies acquiring and financing a nuclear power plant. The reference to the single area standard was made in approving the joint acquisition of a single power plant by utilities who planned to benefit from its production, not a merger of two of the nation's largest utilities. The geographic territory covered by the participants in the nuclear plants was vastly smaller than the area proposed by Applicants, each utility was

a member of a single regional power pool (NEPOOL), and the acquisition of the plant itself was the product of regional planning for electric generation.

The Applicants rely on a flawed interpretation of Section 2(a)(29)(A). They focus, almost entirely, on the Commission's "flexibility" to take into account the current state of the industry. This argument is not available to them under the statute, because the "state of the art" parenthetical in Section 29(a)(29) pertains to the impairment requirement and not the "single area or region" standard. As explained next, the impairment clause and the single area clause are distinct requirements of Section 2(a)(29); and the parenthetical authorizing the Commission to account for the state of the art falls within the impairment clause, after the word "impair." However, even if one gives the Applicants the benefit of any doubt and considers the current "state of the art" in the electric industry, it is not credible to argue that Ohio and Texas fall within the same region, as discussed above.

The applicants cite the existence of the Mid-America Regulatory Conference, which includes regulators from Ohio and Texas, as evidence that the two states are in a "single region." (See Amendment 2 to Form U-1, fn. 19.) This is a joke. There is no evidence that the periodic gatherings of regulators from the Mexican border to the Canadian border have had any integrating effect on the physical operations covering that territory.

**2. Applicants' Effort to Merge the "Single Area or Region" Requirement Into the "Not So Large to Impair" Test Is a Misreading of the Statute**

The "single area or region" standard is a distinct criterion of an "integrated public-utility system" that the Applicants are required to meet. The requirement is one of the "four distinct standards that must be met before the Commission can find that an integrated public-utility system will result from a proposed

acquisition." Environmental Action, Inc. v. S.E.C., 895 F.2d 1255, 1263 (D.C. Cir. 1990) (citing In re Electric Energy, Inc., 38 S.E.C. 658, 668 (1958)).

The Commission has interpreted the "single area or region" language of Section 2(a)(29) as a distinct requirement of an integrated public-utility system for more than 50 years and to this day. See, e.g., United Light and Railways Co., Release No. 7951 (Dec. 31, 1947) (considering "whether those properties may be deemed to be located in a 'single area or region'" as a separate criterion under Section 2(a)(29)); Electric Energy, Inc., Release No. 13871 (Nov. 28, 1958) (holding that Section 2(a)(29) of the Act "requires that four separate standards be satisfied"; single area or region is third standard); American Electric Power Co., Release No. 20633 (July 21, 1978) (same treatment of the "single area or region" standard); Northeast Utilities, Release No. 35-25221 (Dec. 21, 1990) (observing that "the use of a third party cannot be relied upon to integrate two distant utilities" because under "section 2(a)(29)(A) ... 'integrated public utility system means . . . a . . . system confined in its operations to a single area or region . . .').

In fact, very recent Commission decisions confirm the agency's long-held view that the "single area or region" language in sec. 2(a)(29)(A) is a distinct criterion that the Applicants must meet in this case, in addition to the finding that local management and regulation will not be impaired. See NIPSCO Industries, Release Nos. 35-26975, (Feb. 10, 1999) (conducting separate analysis of whether "single area or region" standard of Section 2(a)(29) is met); Sempra Energy, Release Nos. 35-26971 (Feb. 1, 1999)(same); Conectiv, Inc., Release Nos. 35-26832 (Feb. 25, 1998) (also applying 4-part test).

The Applicants suggest, however, that because the word "and" is not included between the "single area or region" clause and the clause "not so large as to impair," the latter clause qualifies the single area

clause and together they constitute only one requirement. Under this construction, Applicants would only have to meet a three-part test and not the four-part test as called for by well-established precedent. Application at 52 n.9. The Applicants' argument is flawed for several reasons.

Perhaps the fact most damaging to the Applicants' argument is that the Commission and courts have explicitly and consistently followed the four-part test of an "integrated public-utility system" contained in clauses A and B of Section 2(a)(29), without deviation. See above. The interpretation calling for a four-part test has withstood the test of time, and Congress has acquiesced in that definition, for good reason: the "single area or region" requirement for an integrated public-utility system is readily apparent from a reading of the text of Section 2(a)(29)(A), particularly when viewed within the entire scheme of the Act.

The Applicants' attempt to combine the "single area or region" requirement with the impairment clause would cause significant confusion in the definition of an integrated public utility system. For example, it would render the "confined to a single area or region" clause entirely unnecessary, since the impairment clause could -- and in fact has always been interpreted to -- stand alone. It is well-established that statutes should not be read to render express language superfluous. See Ratzlaf v. United States, 510 U.S. 135, 140 (1994) (noting that courts "should hesitate" to adopt interpretations that would render other provisions of a statute superfluous or unnecessary).

Furthermore, that the "single area or region" clause is a separate criterion is evidenced by subpart (B) of Section 2(a)(29), which reads similarly to subpart (A) but includes the proviso that gas utilities "deriving natural gas from a common source of supply may be deemed to be included in a single area or region." This proviso clarifies, for gas utilities, what may constitute a single area. Because the proviso

guides the interpretation of the "single area" clause for gas utilities without mention of the impairment clause, it is clear that it is a separate criterion. To interpret subpart A differently than subpart B would produce an illogical result clearly not intended by Congress.

One may also turn to the A-B-C clauses of Section 11(b)(1), which provide the circumstances under which a registered holding company may own more than one integrated system, for additional guidance as to whether the "single area or region" clause is a distinct requirement under Section 2(a)(29). Similar to Section 2(a)(29), the A-B-C clauses refer, in clause A, to the economies of operation and, in clause C, to the impairment of "the advantages of localized management, efficient operation, and the effectiveness of regulation." Clause B requires that the additional systems be "located in one State, or in adjoining States, or in a contiguous foreign country." Clause B has been interpreted as requiring that all additional systems be located in a "single area" for the A-B-C exception to apply. Engineers Public Service Co. v. Securities and Exchange Commission, 138 F.2d 936 (D.C. Cir. 1943). The interpretation of clause B as requiring a "single area" is consistent with the "single area or region" standard of Section 2(a)(29)(A). Thus, the interpretation of clause B as requiring the additional system to be within the "single area" of the principle system -- with clause B obviously being a distinct criterion from clause C, which repeats the "impairment" clause of Section 2(a)(29)(A) -- is consistent with interpreting the "single area or region" clause of Section 2(a)(29)(A) as a separate criterion from the impairment clause in Section 2(a)(29).

Another problem with the Applicants' construction is that, taken to its logical end, it would also eliminate the second requirement of the established four-part test of an integrated public utility system. Since the requirement that the system "be economically operated as a single interconnected and coordinated system" and the requirement that the system be "confined in its operations to a single area or region" are not

separated by the word "and," the former phrase also would not be a distinct standard -- thereby turning what the courts and the SEC have interpreted for more than a half century as requiring a four-part test into not just a three-part but a two-part test. The logical result of Applicants' interpretation, then, would be to collapse three of the criteria recognized by the SEC and accepted by the courts into one criterion because of the absence of the word "and."

The Commission must reject the Applicants' suggestion of eliminating the "confined to a single area or region" requirement and view that suggestion for what it is: an attempt to evade a standard they cannot meet. The Applicants cannot meet the requirement that their operations be confined to a single area or region, and for that reason the Commission must reject their Application.

## **II. The Applicants Cannot Satisfy the "Economical and Efficient Development" Test of Section 10(c)(2) by Selling Off Generation Presently Used to Integrate the System**

Even if the post-merger entity could be a single "integrated public-utility system," the method by which Applicants would have achieved this status would violate Section 10(c)(2). It is not "economical and efficient" integration to divest generating plants that help make the present system integrated.

As noted above, Applicants have acknowledged that the effect of the 250 MW transmission arrangement is to increase CSW's market share, beyond levels that are acceptable under FERC's Merger Policy Statement. See Amendment #2, Item 9 (acknowledging that the 250 MW contract path produced "a few additional failures under the screening analysis ... for the Economic Capacity Measure in the SPP and ERCOT markets"). The Applicants therefore "propose to divest ownership of 550 MW of generation capacity (300 MW in the SPP and 250 MW in the ERCOT)." Id. These facilities are presently part of the generation configuration regularly dispatched to serve the combined load of CSW subsidiaries. They

represent investments made over the years to make the system integrated. Customers of the combined system have paid hundreds of millions of dollars for these units, for the purpose of achieving this integration.

Thus in the name of satisfying a statutory requirement of "economical and efficient development" of an integrated system, the Applicants would be selling off assets which were planned for, and used every day to serve, the integrated needs of the system. In short, Applicants would turn the statute upside down. The action which fails to integrate -- a token, temporary contract path -- is treated as integration; and what de-integrates -- the divestiture of plants crucial to the integrated joint dispatch of the CSW system -- is credited with assisting integration. The Commission cannot accept this result.

Even if the divestiture of the generation plants could somehow avoid violating the integration requirement on a physical basis, it will leave customers worse off on an economic basis. Customers who have paid "front-loaded" rates to finance the to-be-divested units are entitled to the low-cost output of these units in their later years, as a matter of symmetry and traditional ratemaking. Yet nowhere in the Application do the Applicants commit to hold the ratepayers of the CSW entities harmless from the loss of the economic benefits of these plants. An acquisition cannot "serve the public interest," as required by Section 10(c)(2), if it makes customers worse off.

That the statute never contemplated approval of this merger is evident from the series of moves Applicants attempt to avoid its provisions. Each statutory problem generates a separate solution, which solution itself creates a new statutory problem. Here is the sequence:

1. Because the Applicants are in two entirely separate regions, each with a generation system planned and operated completely independently of the other, there is no transmission system

common to both and no plan anywhere on earth to create one, so they created a token and temporary contract path, in the form of a 3-year contract, over Ameren, an intervening utility.

2. The rights to the 250 MW transmission facility produces a dangerous increase in the merged company's market share in the SPP and ERCOT markets. Realizing that the solution to one statutory failure (the integration requirement) would produce another statutory failure (undue concentration of control), they propose to divest key generation facilities.

3. But this final step, while possibly reducing the market power problem, creates another problem: the loss of integrating benefits for which ratepayers historically have paid.

## CONCLUSION

For almost 20 years, utility efforts to win Congressional repeal of the Public Utility Holding Company Act have failed. The Act largely stands as originally written. Utilities have also undertaken efforts to chip away at various provisions of the Act through merger applications and other filings on a case-specific basis. The Commission, citing its right to be flexible, has approved many utility consolidations that the Act's drafters likely would have rejected. However, flexibility has its limits. Certainly, such flexibility cannot go beyond the requirements of the law. Clearly, the facts in this case are beyond the pale. Under no permissible reading of the statute can the combined AEP-CSW system be deemed to be an "integrated public utility system." We respectfully urge the Commission to reject this Application.

Respectfully submitted, etc.

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April 6, 1999

**CERTIFICATE OF SERVICE**

The undersigned certifies that on April 6, 1999, it served a copy of the foregoing document on the Secretary of the Commission and on counsel for the Applicants.

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