IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 07-2499

FEDERAL TRADE COMMISSION,

Plaintiff - Appellant,

v.

EQUITABLE RESOURCES, INC., DOMINION RESOURCES, INC., CONSOLIDATED NATURAL GAS COMPANY, and THE PEOPLES NATURAL GAS COMPANY,

Defendants - Appellees.

ON APPEAL FROM A FINAL ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA DISMISSING PLAINTIFF'S COMPLAINT

REPLY BRIEF OF PLAINTIFF - APPELLANT FEDERAL TRADE COMMISSION

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INTRODUCTION AND SUMMARY

Pennsylvania has not clearly articulated any policy to displace competition with respect to the acquisition of one public utility by another. FTC Opening Brief ("FTC Br.") at 15-22. But that is what the antitrust state action doctrine requires -- a clear articulation by the legislature of a state policy to displace competition with respect to the *specific action* that is being challenged under the antitrust laws. Because defendants have failed to meet their burden of showing such a clear articulation, the state action exemption cannot apply to Equitable's acquisition of Peoples.

In their brief ("Def. Br."), defendants mistakenly contend that PUC approval of their acquisition equates with the clear articulation necessary to satisfy the first part of the test set forth in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980). Def. Br. at 19-25. But PUC approval cannot satisfy *Midcal* because clear articulation must come from the Pennsylvania legislature. Nor have defendants identified any provision of Pennsylvania law that clearly contemplates anticompetitive acquisitions by public utilities. *See* Def. Br. at 25-31. The provisions on which they primarily rely, 66 Pa. Cons. Stat. §§ 1102, 1103, *see* Def. Br. at 26, merely preclude acquisitions absent PUC approval, but in no way indicate that such approval is appropriate where an acquisition violates the antitrust laws. Also, although defendants contend that the "obvious role" of 66 Pa. Cons. Stat. § 2210 is limited to restricting acquisitions that have an anticompetitive effect on the market for the supply of natural gas, Def. Br. at 36-37, that limited role is "obvious" only by ignoring the actual wording of the statute. Because that provision precludes the PUC

from approving acquisitions that are "likely to result in anticompetitive or discriminatory conduct," it cannot possibly articulate a policy to displace competition. *Cf.* Def. Br. at 38-41. At most, it establishes the limited condition under which the PUC may approve acquisitions that would otherwise be anticompetitive -- when the PUC takes steps to assure that the competitive market is preserved, steps it has not taken here.

Defendants also fail to satisfy the second part of the *Midcal* test because they cannot show that there will be sufficient active supervision of the consequences of the acquisition. *See* Def. Br. at 47-54. Because the anticompetitive conduct and attendant consumer harm may not occur until well after initial approval of defendants' acquisition, Pennsylvania must, in order to displace the federal antitrust laws, provide continuing oversight of the firms' post-acquisition activities to ensure that they remain in accord with the state's regulatory policies. The fact that the PUC generally regulates certain aspects of utility conduct (such as maximum rates and minimum service standards) does not establish adequate state supervision because such regulation does not reach the specific anticompetitive conduct that the FTC has challenged.

Finally, if the FTC prevails in its appeal before this Court, it is both proper and necessary for this Court to enter an injunction pending completion of the district court's proceedings. Given that this Court has already enjoined the acquisition pending the outcome of this appeal, it makes little sense to require the FTC to seek temporary relief from the district court on a necessarily expedited basis.

ARGUMENT

I. THE STATE ACTION DOCTRINE DOES NOT EXEMPT DEFENDANTS' ACQUISITION FROM ANTITRUST SCRUTINY

A. Defendants fail to meet their burden with respect to the first part of the *Midcal* test

1. Defendants make the same mistake the district court made -- they contend that PUC approval of their acquisition constitutes clear articulation of a policy to displace the antitrust laws with a regulatory regime.[1] Def. Br. at 19-25. The antitrust laws are "[a] national policy of * * * pervasive and fundamental character," that are "essential to economic freedom." *FTC v. Ticor Title Insurance Co.*, 504 U.S. 621, 632 (1992). The "clear articulation" test allows state displacement of federal antitrust policy only where the state has unmistakably asserted its sovereign authority. Thus, clear articulation can only come from the state legislature (or the state's highest court), not from a state administrative agency. *Southern Motor Carriers Rate Conf., Inc. v. United States*, 471 U.S. 48, 62-63 (1985). This distinction is crucial because the state action doctrine "reflects Congress' intention to embody in the Sherman Act

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[1] Defendants, like the district court, repeatedly address the merits of the FTC's antitrust challenge. *See* Def. Br. at 1-2, 37, 38, 41-42. But whether the state action exemption applies is an issue that the courts must address antecedent to the merits. FTC Br. 25-28. Moreover, because this issue comes before this Court on defendants' motion to dismiss pursuant to Fed. R. Civ. P. 12(b)(6), this Court must assume the facts as pleaded in the FTC's complaint, not, as defendants incorrectly urge, the ones found by the PUC. *Krantz v. Prudential Invs. Fund Mgmt. LLC*, 305 F.3d 140, 142 (3d Cir. 2002). Thus, this is not the time to consider, for example, whether the acquisition was procompetitive or anticompetitive in its net effects.

the federalism principle that the States possess a significant measure of sovereignty under our Constitution." *Community Commc'ns Co. v. City of Boulder*, 455 U.S. 40, 53 (1982). This sovereign authority resides only with the federal government or with the states, not with subordinate state bodies. *Id.* at 53-54. Thus, the *Midcal* test seeks to assure that "*the legislature* contemplated the kind of action complained of." *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 44 (1985) (emphasis added; quotation marks omitted).[2] The PUC is not the legislature and neither its statements nor its actions can satisfy the first part of the *Midcal* test.[3]

The cases cited by defendants do not support their contention that the *Midcal* test is satisfied if the PUC, not the legislature, articulates a policy to displace competition. In *Southern Motor Carriers*, *see* Def. Br. at 23-24, the United States challenged, as a violation of the antitrust laws, agreements by common carriers in four states to submit joint rate proposals to state public service commissions. The

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[2] In *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 313 (1989), which does not involve the state action doctrine, the Court merely stated that the PUC is "essentially an *administrative* arm of the legislature" (emphasis added to the word that defendants twice omit from their brief, *see* Def. Br. at 10, 19). The case in no way suggests that, under the *Midcal* test, clear articulation of a *legislative* policy could come from a subordinate state agency. Similarly, neither *Keystone Water Co. v. Pennsylvania PUC*, 339 A.2d 873 (Pa. Commw. Ct. 1975), nor *Sayre v. Pennsylvania PUC*, 54 A.2d 95 (Pa. Super. Ct. 1947), involved the *Midcal* test. *See* Def. Br. at 10. Those cases merely involved direct review of PUC decisions, not issues of federalism.

[3] *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004), and *Credit Suisse Sec. (USA) v. Billing*, 127 S. Ct. 2383 (2007), *see* Def. Br. at 24 n.7, are irrelevant because they address the relationship between federal entities, not the issues of federalism that are inherent in the state action defense.

Court held that the state action defense shielded this joint conduct from the antitrust laws but cautioned that the defense "is available only when the challenged activity is undertaken pursuant to a clearly articulated policy of the State itself, such as a policy approved by a state legislature, or a State Supreme Court." 471 U.S. at 63 (citations omitted). Because clear articulation may come only from the legislature (or the highest court), the Court further cautioned that state administrative agencies "[a]cting alone * * * could not immunize private anticompetitive conduct." *Id.* at 62-63. In three of the states, the state legislatures had specifically authorized common carriers to submit joint rate proposals, and the state action defense clearly applied. *Id.* at 63.

In the fourth state, Mississippi, the public service commission, not the legislature, authorized joint rate submissions. However, the Mississippi legislature had authorized the public service commission to prescribe "just and reasonable" rates for intrastate transportation of commodities, and this meant that "intrastate rates would be determined by a regulatory agency, rather than by the market." *Id.* at 63-64. Once the legislature had prescribed this regime of rate regulation, the Court did not require that the legislature also expressly authorize every implementing detail. *Id.* at 64. "If more detail than a clear intent to displace competition were required of the legislature, States would find it difficult to implement through regulatory agencies their anticompetitive policies." *Id.*

In fact, the relevant holding of *Southern Motor Carriers* is that, where a state legislature clearly articulates a regulatory program that eliminates an aspect of

competition (*e.g.*, competition with respect to rates), that program is exempt from the antitrust laws, and that exemption extends to the implementing details of that program, details that the legislature clearly contemplates the agency to work out. But this does not mean, as defendants wrongly assume, that the PUC has *carte blanche* to articulate a displacement of other aspects of competition. In the present case, nothing in the statute indicates that the legislature contemplated anticompetitive utility mergers, and nothing in *Southern Motor Carriers* suggests that, absent clear articulation from the legislature, the PUC can provide that articulation.

Nor are defendants helped by this Court's decision in *Mobilfone of NE Pennsylvania, Inc. v. Commonwealth Tel. Co.*, 571 F.2d 141 (3d Cir. 1978). *See* Def. Br. at 19-20. *Mobilfone* was decided two years before *Midcal*, and this Court adopted a standard that differed from the one ultimately set forth by the Supreme Court. *Mobilfone* required the antitrust defendant asserting a state action defense to "show that the state has an independent regulatory interest in the subject matter of the antitrust controversy * * *." 571 F.2d at 144. But an "independent regulatory interest" would not pass muster under *Midcal* because it would not show a state policy to displace competition *with respect to the subject matter of the controversy*. Under *Midcal*, defendants must show, not just that Pennsylvania has a "regulatory interest" in acquisitions, but that it clearly contemplated approval of anticompetitive

acquisitions. *See Town of Hallie*, 471 at 42. That is a showing defendants cannot make.[4]

Nothing in *Yeager's Fuel, Inc. v. Pennsylvania Power & Light Co.*, 22 F.3d 1260 (3d Cir. 1994), holds that statements of the PUC may establish the clear articulation necessary to satisfy *Midcal*. *Cf.* Def. Br. at 21-22, 45. In *Yeager's Fuel*, this Court did not, as defendants mistakenly suggest, glean clear articulation from a report written by a bureau of the PUC. Instead, this Court looked to a state statute, and determined that certain energy conservation measures permitted by that statute displaced competition.[5] 22 F.3d at 1267-68. This Court looked to the PUC only for assistance in determining whether the utility's conduct came within the scope of the

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[4] *City of Pittsburgh v. West Penn Power Co.*, 147 F.3d 256 (3d Cir. 1998), is irrelevant to this case. *Cf.* Def. Br. at 20. That case did not involve the state action doctrine. Instead, this Court held that, where the two defendants had not competed in the past (unlike the situation here), and where it was not clear that the PUC would ever have permitted them to compete in the future, the withdrawal of a petition before the PUC, which, if approved would have resulted in competition, could not constitute antitrust injury. 147 F.3d at 263-265.

[5] Similarly, in *Independent Taxicab Drivers Employees v. Greater Houston Transp. Co.*, 760 F.2d 607, 610 (5th Cir. 1985), *see* Def. Br. at 21, the court concluded that the state had a clearly articulated policy to displace competition based on state statutes, not the decisions of an agency.

statute.[6] Thus, *Yeager's Fuel* is fully consistent with *Southern Motor Carriers* -- clear articulation must come from the state legislature, not from the PUC.[7]

Southern Motor Carriers is fully consistent with the approach that courts have taken to other aspects of state-federal relations, *i.e.*, the "clear statement" requirement that applies when Congress encroaches on areas of traditional state prerogative.[8] "'In traditionally sensitive areas, such as legislation affecting the federal balance, the requirement of clear statement assures that the legislature has in fact faced, and

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[6] Although the defendant in *Yeager's Fuel* did not, on appeal, pursue the state action defense with respect to "all-electric development agreements," *see* Def. Br. at 22 n.6, this Court did "conclude" that such agreements, which were outside the scope of Pennsylvania's law encouraging energy conservation, were not entitled to a state action defense. 22 F.3d at 1263; *see* FTC Br. at 20 n.8.

[7] In *California CNG, Inc. v. Southern California Gas Co.*, 96 F.3d 1193 (9th Cir. 1996), *see* Def. Br. at 20-21, 45, the court identified a regulatory regime that had been clearly articulated by the state legislature. *Cal. CNG*, 96 F.3d at 1197. Nonetheless, the court then charted the vicissitudes of the state utility commission's application of the program, and held that, when the defendant's conduct was not in accord with the commission, no defense was appropriate. *Id.* at 1197-1200. (In its *amicus* brief, the Commonwealth of Pennsylvania charts similar vagaries of the PUC's attitude toward competition. Pa. Br. at 13-18.) In so doing, the court not only ignored the holding of *Southern Motor Carriers* (that the policy to support a state action defense must come from the legislature), but also *City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 372 (1991), in which the Court warned that the state action defense does not make antitrust courts the reviewers of the decisions of administrative agencies.

[8] *See Will v. Michigan Dep't of State Police*, 491 U.S. 58, 65 (1989) (abrogation of Eleventh Amendment immunity); *Pennhurst State Sch. and Hosp. v. Halderman*, 451 U.S. 1, 16 (1981) (imposition of financial liability as condition of exercise of Congress's spending power); *Gregory v. Ashcroft*, 501 U.S. 542 (1991) (interference with qualifications standards for state judges).

intended to bring into issue, the critical matters involved in the judicial decision.'" *Will*, 491 U.S. at 65, quoting *United States v. Bass*, 404 U.S. 336, 349 (1971). Where the plain statement rule applies, moreover, that statement can only come from a sovereign authority -- Congress. Thus, in *California State Bd. of Optometry v. FTC*, 910 F.2d 976 (D.C. Cir. 1990), the FTC had interpreted its authority under the FTC Act to extend to the unfair or deceptive acts or practices of states. However, the court refused to defer to this interpretation. "The clear statement doctrine leaves no room for inferences. An agency may not exercise authority over States as sovereigns unless that authority has been unambiguously granted to it." *Id.* at 982. The same principle applies here in the other direction: the clear articulation needed to trump the fundamental federal policy of the antitrust laws must be based on unambiguous action by the state legislature, not on positions set forth by a subordinate agency.[9] *See Surgical Care Ctr. of Hammond, L.C. v. Hospital Serv. Dist. No. 1 of Tangipahoa Parish*, 171 F.3d 231, 234 (5th Cir. 1999) (referring to the state action exemption as a "doctrine of clear statement").

2. No provision of Pennsylvania law articulates a policy to permit anticompetitive utility acquisitions. In an attempt to satisfy the *Midcal* test,

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[9] In its *amicus* brief, the PUC ignores *Southern Motor Carriers*, and suggests that Pennsylvania "has given to the PUC sole authority to establish * * * a policy" to authorize anticompetitive acquisitions, thereby satisfying the first part of the *Midcal* test. *See* PUC Br. at 7; *see also* PUC Br. at 5 (arguing that this Court must defer to the PUC's evaluation of state action). Clear articulation may not be delegated, and, in any event, as discussed *infra*, there has been no such delegation.

defendants cobble together statutory provisions that merely relate to acquisitions. But a state displaces competition not by imposing regulatory requirements, but by authorizing conduct that is *inconsistent* with competition. *See* FTC Br. 21. First, 66 Pa. Cons. Stat. §§ 1102 and 1103, Def. Br. at 26, require that, before a public utility may acquire property, it must obtain PUC approval (§ 1102), and the PUC shall approve the acquisition only if it will "promote the 'service, accommodation, convenience, or safety of the public' in some substantial way." *City of York v. Pennsylvania PUC*, 295 A.2d 825, 828 (Pa. 1972) (interpreting the precursor of § 1103). Nothing in § 1102 or § 1103 suggests that, once an acquisition clears this public interest hurdle, it is freed from clearing hurdles imposed by other laws, including the antitrust laws. At most, § 1102 and § 1103 prescribe a policy that is neutral with respect to the antitrust laws. But clear articulation is not satisfied "when the State's position is one of mere neutrality respecting the * * * actions challenged as anticompetitive." *City of Boulder*, 455 U.S. at 55; *see McCaw Personal Commc'ns, Inc. v. Pacific Telesis Gp.*, 645 F. Supp. 1166, 1172 (N.D. Cal. 1986) (utility commission approval of an acquisition pursuant to a public interest standard is insufficient to demonstrate that the state intended to insulate the acquisition from the antitrust laws).[10] That is, defendants must show not just that the Pennsylvania

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[10] Defendants cite *Metro Mobile CTS, Inc. v. Newvector Commc'ns, Inc.*, 661 F. Supp. 1504 (D. Az. 1987), *aff'd* 892 F.2d 62 (9th Cir. 1989), Def. Br. at 40, 41, which rejects *McCaw*, and concludes that review pursuant to a public interest standard that "includes factors other than enhancing competition" clearly articulates a policy displacing competition. *Id.* at 1515. But *Metro Mobile* was based on the district court's belief that "[t]he theoretical underpinnings of state

legislature contemplated that public utilities would undertake acquisitions but that it clearly contemplated that the PUC could approve anticompetitive utility acquisitions.

Nor are defendants helped by § 1304, which prohibits public utilities from "maintain[ing] any unreasonable difference as to rates." *See* Def. Br. at 26. Even assuming that § 1304 provides the PUC with authority to prohibit the discounts that have been available to consumers who benefit from the competition between Equitable and Peoples, if the PUC had wanted to put a halt to discounts, it could have done so long ago, and it could have done so directly, independent of any acquisition.[11] It is absurd to suggest, as defendants do, that the authority to prohibit unreasonable discrimination in rates somehow constitutes authority to displace competition with respect to acquisitions merely because the competing parties offered discounts.[12]

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action immunity, federalism and the sovereignty of the states, require a more lenient analysis." *Id.* In fact, the opposite is true -- the state action defense is disfavored and is to be narrowly interpreted. *Ticor*, 504 U.S. at 635-636. Moreover, although *Metro Mobile* was affirmed, the Ninth Circuit specifically declined even to address that portion of the district court's opinion that discussed state action. 892 F.2d at 63.

[11] It is far from clear that § 1304 actually prohibits discounts -- apparently (despite § 1304) defendants have offered them for many years. *See also Building Owners and Managers Ass'n v. Pennsylvania PUC*, 470 A.2d 1092 (Pa. Commw. Ct. 1984) (merely charging different prices to different customers does not establish that a utility is charging unreasonable or discriminatory rates.)

[12] Even assuming that § 1304 prohibits discounts, that section and the other provisions of Pennsylvania law that authorize the PUC to regulate maximum public utility rates do not clearly articulate a policy to authorize anticompetitive acquisitions. Equitable and Peoples competed not only by offering discounted rates, but also by offering other benefits that are clearly outside the reach of

The first part of *Midcal* is not satisfied by a statutory provision that merely authorizes acquisitions. Thus, this Court should not rely on *FTC v. Hospital Bd. of Dirs. of Lee County*, 38 F.3d 1184 (11th Cir. 1994). *Cf.* Def. Br. at 26-29. In *Lee County*, the Eleventh Circuit held that the county hospital board's purchase of a private hospital was exempt from antitrust challenge pursuant to the state action doctrine. The court held that the mere grant of authority to acquire property was sufficient to authorize an anticompetitive acquisition. 38 F.3d at 1192. But corporations (or quasi-public entities, such as the hospital board in *Lee County*) only have such powers as are granted them by the states, and they are routinely given the power to contract, to acquire property, and to enter into joint ventures. If this were sufficient to authorize anticompetitive contracts, acquisitions, and joint ventures, then the first part of the *Midcal* test would be rendered virtually meaningless. *See* Phillip E. Areeda & Herbert Hovenkamp, IA *Antitrust Law*, ¶ 225b4 at 153 (3d ed. 2006) ("one would never infer from the mere fact that a corporation was authorized to enter into agreements that it was authorized to engage in price fixing").[13]

Pennsylvania's regulatory regime (*i.e.*, long-term contracts and guaranteed terms and conditions). *See* FTC Br. at 30-31.

[13] Neither *Omni Outdoor Advertising, supra*, nor *Town of Hallie, supra*, suggests that the fact that defendants cannot consummate the acquisition absent PUC approval satisfies the first part of *Midcal*. *Cf.* Def. Br. at 29 n.9. In *Omni*, the city's zoning ordinance provided a state action defense against an antitrust challenge asserted by a new entrant because "[t]he very purpose of zoning regulation is to displace unfettered business freedom in a manner that regularly has the effect of preventing normal acts of competition * * *." 499 U.S. at 373. As explained above, displacement of competition is not the "very purpose" of § 1102

In *Hammond*, *supra*, the Fifth Circuit, sitting *en banc*, properly rejected the approach taken in *Lee County*. That court concluded that a statute that gave the hospital district authority to engage in joint ventures did not constitute a clear articulation of a policy to authorize anticompetitive joint ventures because "[n]ot all joint ventures are anticompetitive. Thus, it is not the foreseeable result of allowing a hospital service district to form joint ventures that it will engage in anticompetitive conduct." 171 F.3d at 235. *Hammond* concluded that courts should "not infer such a policy to displace competition from naked grants of authority." *Id.* at 236.[14] So,

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and § 1103. Similarly, in *Town of Hallie*, the state authorized the defendant city to limit the areas in which it provided sewage treatment service. 471 U.S. at 41. The Court held that this statute clearly contemplated that the city would engage in anticompetitive conduct by refusing to permit unannexed towns to connect to the facility. *Id.* at 42. This statute was not neutral with respect to the anticompetitive consequences. *Id.* at 43. This is very different from the impact of § 1102 and § 1103.

[14] Defendants mistakenly contend that, in a brief filed in *Lee County*, the FTC conceded that state approval of a merger would satisfy the first part of the *Midcal* test. Def. Br. at 28-29. However, in the portion of the FTC's brief that defendants quote, defendants omit two case citations that explain the quoted portion by providing examples of the type of state approval that could constitute clear articulation. *See* Appx. 347 (Reply Brief for FTC in *Lee County* at 8). In the first of those cases, *Southern Motor Carriers*, state regulation of rates necessarily replaced the role of market forces in rate setting. *See supra*. In the second of the cases, *North Carolina ex rel. Edmisten v. P.I.A. Asheville, Inc.*, 740 F.2d 274 (4th Cir. 1984), North Carolina law required that, before one hospital could acquire another, it had to obtain a certificate of need. North Carolina had enacted the certificate of need program based, in part, on a finding that "the forces of free market competition are largely absent and government regulation is therefore necessary to control the cost * * * of health services." *Id.* at 277. Thus, it was

too, in this case, a statute that prohibits acquisitions that are not in the public interest should not be read to authorize anticompetitive acquisitions.

This Court, like the Fifth Circuit,[15] has also rejected the approach taken in *Lee County*. In particular, in *Yeager's Fuel*, this Court recognized that a statute that merely authorized a general category of conduct would not support a state action defense. 22 F.3d at 1267. Instead, this Court required that, to satisfy *Midcal*, the challenged anticompetitive activity must be a "foreseeable result" of what the statute authorizes. *Id.* at 1268. In this case, Pennsylvania law authorizes corporations such as defendants to acquire property, *see* 15 Pa. Cons. Stat. § 1502(a)(4), and § 1103 authorizes the PUC to approve acquisitions by public utilities that are in the public interest. This broad authority in no way indicates that the Pennsylvania legislature contemplated that the PUC would use such authority to approve anticompetitive acquisitions.[16] Thus, defendants' state action defense fails.

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clear that North Carolina intended its certificate of need program to supplant market forces. The FTC never suggested in its *Lee County* brief that any state regulatory regime that required approval of individual transactions would satisfy *Midcal* with respect to all actions of the regulated party.

[15] Defendants are not helped by *Martin v. Mem'l Hosp. at Gulfport*, 86 F.3d 1391 (5th Cir. 1996). *See* Def. Br. at 27. In *Hammond*, the Fifth Circuit explained that "any reading of *Martin* that finds immunity in a state legislature's general grant to its agency of authority to conduct its affairs is incorrect." 171 F.3d at 233.

[16] Defendants misunderstand the relevance of *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976). *See* Def. Br. at 30-31. Although *Cantor* suggested that the regulation of natural monopolies may provide a state action defense, 428 U.S. at 595-96, defendants ignore that, in the geographic market alleged in the FTC's complaint, natural gas distribution is *not* a natural monopoly because there has

3. Even if §§ 1102, 1103, and 1304 could, by themselves somehow be read to contemplate PUC approval of anticompetitive acquisitions, § 2210(b) specifically precludes such a reading. That section provides that, when the PUC reviews acquisitions, it must consider competition independent of other issues, and it must reject any acquisition that "is likely to result in anticompetitive or discriminatory conduct, including the unlawful exercise of market power * * *." § 2210(b). Far from displacing the antitrust laws with a regulatory regime, Pennsylvania law does the opposite -- it makes sure that, when the PUC approves acquisitions, it does not displace the protections of the antitrust laws.[17]

This Court should reject defendants' attempt to twist the wording of § 2210(b) and limit its application to the market for natural gas supply services. Def. Br. at 36-37. Section 2210(b) protects "retail gas customers." That term is broadly defined in § 2202 as "direct purchaser[s] of natural gas supply services or *natural gas distribution services* * * *." (Emphasis added.) Section 2210(b) also seeks to ensure that those retail gas customers are not prevented from reaping the benefits of a competitive "retail natural gas market." "Retail natural gas market" is not defined in

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been a long history of competition. The crucial holding of *Cantor* is that, even though the light bulb distribution program had been approved by a state commission pursuant to a public interest standard (just like defendants' acquisition), this did not shield the program from the antitrust laws. *Id.* at 594-595.

[17] Defendants can draw no support from *Sterling Beef Co. v. City of Fort Morgan*, 810 F.2d 961 (10th Cir. 1987), *see* Def. Br. at 29 n.9, because the statutory regime in that case had no provision similar to § 2210(b).

the statute. However, "natural gas supply services" is defined in § 2202, and is limited to the sale of natural gas -- it does not apply to natural gas distribution. Plainly, if the legislature had wanted to limit the application of § 2210(b), it could have done so by restricting the section's protections to customers for "natural gas supply services," or by limiting the section's application to the market for "retail natural gas supply services." Other sections of the statute have a more limited application. *See, e.g.*, § 2204(g) (mandating an investigation of "competition for natural gas supply services"); § 2207(e) (referring to "customers for all of the natural gas supply services"). Instead, however, the legislature gave § 2210(b) a broader scope, protecting direct purchasers of distribution services, and preserving competition in the retail gas market.

This Court should also reject defendants' attempt to interpret § 2210(b) in the light of what they refer to as the "one purpose" of Pennsylvania's Natural Gas Choice and Competition Act. *See* Def. Br. at 31. Although that act, of which § 2210(b) was a part, sought to create competition in the market for natural gas supply services, it does many other things. *See, e.g.*, § 2205(a) (maintaining the integrity of the distribution system); § 2206 (providing for consumer protection); § 2212 (regulating city natural gas distribution operations). Pennsylvania recognized that creating competition in the market for natural gas supply could lead to broad restructuring that would have an impact on many aspects of the retail natural gas market. Section 2210(b) protects customers from the anticompetitive aspects of such restructuring,

including acquisitions that have an impact on the market for gas distribution services. Moreover, reliance on the:

> "broad purposes" of legislation at the expense of specific provisions ignores the complexity of the problems [the legislature] is called upon to address and the dynamics of legislative action. [The legislature] may be unanimous in its intent to stamp out some vague social or economic evil; however, because its Members may differ sharply on the means for effectuating that intent, the final language of the legislation may reflect hard-fought compromises. Invocation of the "plain purpose" of legislation at the expense of the terms of the statute itself takes no account of the processes of compromise and, in the end, prevents the effectuation of [the legislature's] intent.

Board of Governors of the Fed. Reserve Sys. v. Dimension Fin. Corp., 474 U.S. 361, 373-74 (1986). Thus, defendants cannot invoke the "purpose" of legislation to narrow the scope of a broadly drafted specific provision.

Nor is there any merit to defendants' contention that § 2210(b) authorizes the PUC to approve anticompetitive acquisitions. *See* Def. Br. at 38-41. Defendants focus on the final clause of the section, which provides that the PUC shall not approve any anticompetitive acquisition "except upon such terms and conditions as it finds necessary to preserve the benefits of a properly functioning and competitive retail natural gas market." *See* Def. Br. at 39. But that clause does nothing more than give the PUC the power to do what reviewing agencies routinely do -- approve otherwise anticompetitive acquisitions if those acquisitions are modified to prevent the anticompetitive conduct. *See* FTC Br. at 23. Defendants, however, argue that § 2210(b) simply leaves it up to the PUC to determine the extent to which competition should be protected. Def. Br. at 40. If that were so, then § 2210(b) would impose no restriction at all, and would be rendered surplusage. This Court

should reject that interpretation. *See United States v. Cooper*, 396 F.3d 308, 312 (3d Cir. 2005), citing *TRW Inc. v. Andrews*, 534 U.S. 19, 31 (2001) ("[i]t is a well known canon of statutory construction that courts should construe statutory language to avoid interpretations that would render any phrase superfluous").

Defendants' interpretation of § 2210(b) is wrong because it takes the final clause out of context. That interpretation also ignores that a significant portion of that final clause appears twice in the section, and that the meaning of the clause can be derived from its first appearance. The critical sentence of § 2210(b) provides as follows:

> If the [PUC] finds, after hearing, that a proposed merger, consolidation, acquisition or disposition is likely to result in anticompetitive or discriminatory conduct, including the unlawful exercise of market power, which will prevent retail gas customers from obtaining *benefits of a properly functioning and effectively competitive retail natural gas market*, the [PUC] shall not approve such proposed merger, consolidation, acquisition or disposition except upon such terms and conditions as it finds necessary to preserve the *benefits of a properly functioning and effectively competitive retail natural gas market.*

(Emphasis added.) The "benefits" phrase, on which defendants' interpretation of § 2210 relies, appears first in a clause that is introduced by a comma and the non-restrictive pronoun "which." This means that "anticompetitive or discriminatory conduct" is equivalent to that which "will prevent retail gas customers from obtaining the benefits of a properly functioning and effectively competitive retail natural gas market." The second time the phrase appears, it must be given the same meaning. "'[I]dentical words used in different parts of the same act are intended to have the same meaning.'" *In re Federal Mogul-Global, Inc.*, 348 F.3d 390, 407 (3d Cir.

2003), quoting *Barnhart v. Walton*, 535 U.S. 212, 221 (2002). Far from bestowing on the PUC complete authority to "determine the form and extent of competition in regulated fields," *see* Def. Br. at 40, § 2210(b) authorizes the PUC to approve anticompetitive acquisitions only "upon such terms and conditions" that will prevent "anticompetitive or discriminatory conduct, including the unlawful exercise of market power."[18]

Thus, not only do defendants misinterpret § 2210(b), but even their interpretation does not constitute a clear articulation of a policy to displace competition. In the context of the clear statement doctrine, when a sovereign seeks to alter the usual balance between the states and the federal government, "it must make its intention to do so 'unmistakably clear in the language of the statute.'" *Will*, 491 U.S. at 65, quoting *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 242 (1985). This rule applies as well with respect to the state action doctrine. *See Cal. State Bd.*, 910 F.2d at 981. Defendants' interpretation of § 2210(b) is hardly "unmistakably clear in the language of the statute." Thus, it cannot satisfy the first part of the *Midcal* test.

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[18] Defendants complain that the FTC's interpretation of § 2210(b) would force the PUC to reject an acquisition that, according to the PUC, benefits Pennsylvania consumers. *See* Def. Br. at 37. But § 2210(b) gives the PUC the authority to modify an acquisition, and thereby both preserve competition and, to the greatest extent possible, still achieve any benefits that may result from the acquisition.

B. Defendants fail to meet their burden with respect to the second part of the *Midcal* test

Defendants further err in arguing that the PUC's review of the proposed transaction meets the second part of the *Midcal* test -- the requirement that the state actively supervise the challenged anticompetitive conduct. First, defendants wrongly argue that the PUC's initial review and approval of the proposed transaction alone satisfies the active supervision requirement. Even the district court did not adopt this untenable position. Defendants' argument ignores the reality that in the merger context the anticompetitive conduct and attendant consumer harm caused by the challenged transaction may not occur until after the fact. Section 7 of the Clayton Act, 15 U.S.C. § 18, protects consumers from potential anticompetitive activities by arresting anticompetitive transactions "in their incipiency." *See United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 362 (1963). If a state wishes to displace these antitrust protections, it is important that the state monitor the firm's post-merger activities to ensure that they remain in accord with the state's regulatory policies. *See P.I.A. Asheville*, 740 F.2d at 278.[19]

Defendants' argument is not aided by the cases they cite -- *Mobilfone*, *Yeager's Fuel*, and *Lee County*. *See* Def. Br. at 49. Neither *Mobilfone* nor *Yeager's Fuel*

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[19] The fact that the court in *P.I.A. Asheville* found that there was a total absence of post-merger supervision does not render the case inapposite, as defendants assert. Def. Br. at 53. The court in no way suggested that *any* degree of post-merger monitoring, short of a total absence of supervision, would satisfy the second part of *Midcal*. Indeed, that is clearly not the law. *See Patrick v. Burget*, 486 U.S. 94, 101 (1988) ("The mere presence of some state involvement or monitoring does not suffice").

involved a merger or acquisition, and the Court did not address what activities undertaken by the PUC would satisfy the active supervision requirement in the context of such a transaction. And the court in *Lee County* did not address the active supervision requirement at all, except to hold that, because the defendant was a "political subdivision" of the state, it was not required to show active state supervision. 38 F.3d at 1188.

There is also no merit to defendants' argument that the "extensive nature" of the state's regulatory scheme establishes that the PUC will monitor the aspects of the post-acquisition company's activities that may harm consumers. *See* Def. Br. at 50. The state's supervision must extend to the "particular anticompetitive acts" challenged in the antitrust action. *Patrick*, 486 U.S. at 101; *see A.D. Bedell Wholesale Co. v. Philip Morris, Inc.*, 263 F.3d 239, 262 (3d Cir. 2001) (state supervision must "reach the parts of the [agreement] that are the source of the antitrust injury"). It is far from apparent, however, that Pennsylvania's regulatory program reaches the post-acquisition company's activities that are of antitrust concern here. The regulations to which defendants refer relate principally to the establishment of maximum rates and minimum service standards. *See* FTC Br. at 30-31. But the post-acquisition activities that are of concern in this antitrust action relate to the elimination of benefits that defendants currently provide to customers that improve

upon regulated terms or are entirely unregulated.[20] Defendants fail to address how the state's regulatory scheme will provide for oversight of that conduct.

It bears repeating that the Supreme Court has articulated a rigorous standard for active state supervision, requiring not only that the state have general supervisory authority over the private actor, but also that the state have actually exercised this authority to ensure that private anticompetitive conduct accords with the state's policy goals. *See Ticor*, 504 U.S. at 638 (active supervision test not satisfied where "the potential for state supervision was not realized in fact"); *Patrick*, 486 U.S. at 101 (active supervision "requires that state officials have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy"). Defendants bear the burden of showing that the PUC has actually exercised supervisory authority over the particular anticompetitive acts challenged, *see Yeager's Fuel*, 22 F.3d at 1266, and that is a burden they have not met.

II. IT IS APPROPRIATE FOR THIS COURT TO ENJOIN DEFENDANTS' ACQUISITION PENDING COMPLETION OF THE DISTRICT COURT'S PROCEEDINGS

This Court should enjoin the acquisition pending completion of the district court proceedings for the same reasons that supported its entry of an injunction pending

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[20] The conditions in the PUC's order that require Equitable to file various reports following the acquisition are likewise unrelated to the harms this acquisition will cause. And, although the PUC order requires Equitable to implement a Service Quality Index, this is a temporary measure, which expires at the companies' next base rate proceeding. *See* Def. Br. at 52; Appx. 225 (ID at 72).

appeal: the FTC's likelihood of success on the merits and the balance of equitable considerations (including the likelihood of public harm and the lack of irreparable harm to defendants) justify a short injunction. Although defendants have promised to give the FTC three days' advance notice before they close the transaction, this is not an acceptable alternative to the relief to which the FTC is entitled. Defendants' proposal allows the FTC only three days to seek an injunction from the district court and, if the district court denies such relief, appeal that denial to this Court. Such a short period of time for two levels of judicial consideration would impose an intolerable burden on both courts. Moreover, contrary to defendants' suggestion, *see* Def. Br. at 55, consideration of the FTC's request for injunctive relief is squarely within this Court's judicial competence and authority.[21]

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[21] *See* 28 U.S.C. § 2106 (court of appeals "may affirm, modify, vacate, set aside or reverse any judgment, decree, or order, or require such further proceedings to be had as may be just under the circumstances"); *ICC v. Cardinale Trucking Corp.*, 308 F.2d 435, 438 (3d Cir. 1962) (this Court remanded to the district court "with the direction, pending the disposition [of the ICC's motion for a preliminary injunction] by it, to issue a temporary restraining order pursuant to the prayer of the plaintiff's complaint").

CONCLUSION

For the reasons set forth above and in the FTC's opening brief, this Court should reverse the district court's order dismissing the FTC's complaint, and enjoin defendants' acquisition pending resolution by the district court of the merits of that complaint.

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COMBINED CERTIFICATIONS

1) Bar membership -- Because this brief is filed on behalf of an administrative agency of the United States, there is no bar membership requirement.

2) Word count -- I certify that this brief complies with Fed. R. App. P. 32(a)(7)(B). It is proportionally spaced and contains 6880 words, as counted by the WordPerfect word processing program.

3) Service upon counsel -- I hereby certify that on August 17, 2007, I served this reply brief by e-mail on appellees and on *amici curiae* Public Utility Commission. I also served two copies of this brief on appellees and on *amici curiae* by express overnight delivery addressed to:

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