UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

AMERICAN ELECTRIC POWER COMPANY, INC. — Administrative Proceeding
File No. 3-11616

STATEMENT OF POSITION
AND NARRATIVE SUMMARY OF EVIDENCE AND LEGAL THEORIES OF
THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION
AND THE AMERICAN PUBLIC POWER ASSOCIATION

In accordance with the scheduling order of October 6, 2004, the National Rural Electric Cooperative Association (NRECA) and the American Public Power Association (APPA) submit this statement of position and narrative summary of the evidence and legal theories on which they will rely in this proceeding. By order of September 17, 2004, APPA and NRECA are parties to this proceeding under Rule 210(b)(1)(i) of the Commission's Rules of Practice.[1]

Statement of Position

Section 9(a)(1) of the Public Utility Holding Company Act (the Act) makes it unlawful for a registered holding company "to acquire, directly or indirectly, any securities or utility assets or any other interest in any business"[2] absent Commission approval under section 10 of the Act.[3] The United States Court of Appeals for the District of Columbia has vacated the Commission's

[1] 17 C.F.R. § 201.210(b)(1)(i).

[2] 15 U.S.C. § 79i(a)(1).

[3] 15 U.S.C. § 79j.

order of June 14, 2000, approving American Electric Power Company's (AEP) acquisition of the common stock of Central and South West Corporation (CSW) and the interests in the assets and businesses of CSW's subsidiary public-utility companies.[4] Neither AEP nor the Commission sought further review of the court's order. Without a Commission order approving AEP's acquisition of CSW, however, the acquisition is unlawful under the Act, the requisite legal approval for the merger of AEP and CSW has not been obtained, and the merger remains pending.[5] Hence, as sections 9 and 10 of the Act require, AEP is now before the Commission again proposing that it be allowed to acquire CSW. There can be no presumption favoring the proposed acquisition as a *fait accompli*. AEP made a deliberate decision in choosing to consummate the merger with CSW pending judicial review; it should not now be relieved of the risk it undertook voluntarily. Rather, AEP bears the burden of proof under the Act to justify its proposed acquisition of CSW. If AEP does not satisfy that burden, the Commission should not approve the acquisition and should require the divestiture of the CSW companies—just as the Commission represented to the court of appeals that it would do if the merged company did not comply with the Act's requirements.[6]

The Commission should not approve the proposed acquisition. Section 10(c)(1) requires that the Commission not approve an acquisition that "would be detrimental to the carrying out of the provisions of section 11."[7] Thus, section 10(c)(1) prohibits approval of an acquisition by a

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[4] *National Rural Electric Cooperative Ass'n v. SEC*, 276 F.3d 609 (D.C. Cir. 2002), *vacating and remanding American Electric Power Co.*, Holding Company Act Release No. 27186 (2000).

[5] This uncertain state of affairs—now nearly three years old—raises a host of potential legal issues, both in this proceeding and more generally.

[6] 276 F.3d at 615-16.

[7] 15 U.S.C. § 79j(c)(1).

registered holding company that would not be permissible under section 11(b)(1) of the Act.[8] Under section 11(b)(1), the utility properties of a registered holding company are generally limited, with certain exceptions not relevant here, to a "single integrated public-utility system."[9] Section 2(a)(29)(A) defines an integrated public utility system, as applied to electric utility properties, to mean:

> a system consisting of one or more units of generating plants and/or transmission lines and/or distribution 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 operations, and the effectiveness of regulation . . . . [10]

AEP's narrative summary submitted on November 15, 2004, does not show that the merged company is an "integrated public-utility system" under this section. First, AEP does not show that the merged company is "physically interconnected or capable of physical interconnection" such that its assets "under normal conditions may be economically operated as a single interconnected and coordinated system." Second, AEP does not show that the merged company is "confined in its operations to a single area or region ... not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operations, and the effectiveness of regulation . . . ."

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[8] 15 U.S.C. § 79k(b)(1). *See New Century Energies, Inc.*, Holding Co. Act Release No. 35-26748, 1997 WL 429612 (S.E.C. Aug. 1, 1997); *Electric Bond and Share Co.*, 33 S.E.C. 21, 31 (1952).

[9] 15 U.S.C. § 79k(b)(1).

[10] 15 U.S.C. § 79b(a)(29)(A).

The Court of Appeals' Order and the Scope of the Remand

These are the very two issues that led the court of appeals to vacate and remand the Commission's earlier order.[11] The court found that "the Commission failed to explain its conclusions regarding the interconnection requirement" and "failed to justify its finding that the proposed acquisition will satisfy the single-area-or-region requirement."[12]

As to the former, the court found that "the Commission's acceptance of a unidirectional contract path to 'interconnect' AEP and CSW" was unexplained.[13] The court noted that "interconnection" of utility assets under the Act "seems, on its face, to require two-way transfers of power."[14] The court noted further that "PUHCA itself requires that the interconnected system be one 'which under the normal conditions may be economically operated as a single interconnected and coordinated' whole."[15] Thus, the court concluded that "[a]bsent some explanation from the Commission, we cannot understand how a system restricted to unidirectional flow of power from one half to the other can be operated in such a manner."[16]

The court also found that "the Commission failed to follow its own prior reasoning regarding interconnection of distant utilities"—decisions in which the Commission "has clearly indicated that a contract path cannot alone integrate distant utilities."[17] The court found the

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[11] 276 F.3d at 610, 619.

[12] *Id.* at 610.

[13] *Id.* at 615.

[14] *Id.*

[15] *Id.* (citing 15 U.S.C. § 79b(a)(29)(A)).

[16] *Id.*

[17] *Id.*

Commission's prior statements "sufficiently explicit to obligate the Commission to provide some rationale for its current contrary view."[18]

As to the single-area-or-region requirement, the court found that the Commission's earlier order "cannot withstand even the most deferential review," because the Commission "failed to make any evidentiary findings on the issue" and "erroneously concluded that a proposed acquisition that satisfies PUHCA's other requirements also meets the statute's region requirement."[19] The court found that the Commission had thus essentially read the single-area-or-region requirement out of the Act, by concluding that satisfying the other integration requirements meant the utility system necessarily operated in a single area or region. In particular, the court found that the Commission's "analysis conflicts with PUHCA's express requirement that an electric utility system be 'confined in its operations to a single area or region . . . not so large as to impair . . . the advantages of localized management, efficient operation, and the effectiveness of regulation.'"[20] The Commission had applied this requirement by reading the word "single" out of the Act.[21] The court concluded that "[t]he Commission may have some legitimate basis for concluding that AEP's service territories in Indiana, Kentucky, Michigan, Ohio, Tennessee, Virginia, and West Virginia fall in the same 'region' as CSW's service territories in Arkansas, Louisiana, Oklahoma, and Texas, but we cannot find it in the record before us."[22]

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[18] *Id.*

[19] *Id.* at 617.

[20] *Id.* (citing 15 U.S.C. § 79b(a)(29)(A) (ellipsis in original)).

[21] *Id.* at 618.

[22] *Id.* at 618-19.

Narrowly construing the issues on remand, AEP contends in its narrative summary that the court "affirmed the Commission's basic conclusion that contract rights may suffice to meet the 'physical interconnection' requirement . . . ."[23] But, as noted above, the court did not affirm the Commission's conclusions that contracts rights are sufficient in this case. To the contrary, the court held that the Commission had departed without explanation from its clear policy that contract rights may not be used to integrate two distant utilities. Thus, on remand, the Commission must make the factual findings and provide a reasoned explanation as to why AEP and CSW—which the court correctly noted are "distant" from one another—can be integrated by using the transmission facilities of other non-affiliated utilities that stand between them.

By vacating and remanding the Commission's order—instead of simply remanding the case for further clarification without *vacatur*—the court of appeals found that the Commission's order was so deficient that it could not be rectified simply by clarification or explanation of the Commission's reasoning. A court remands without vacating the agency's order when the court is "unsure and [wants] . . . clarification of [the agency's] position and the rationale therefor.".[24] That course is generally appropriate when "there is at least a serious possibility that the [agency] will be able to substantiate its decision" and when vacating the agency's order would be "disruptive."[25] Accordingly, by vacating the Commission's order, the court of appeals did not find a serious likelihood that the Commission would be able to substantiate its earlier decision

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[23] Narrative Summary of the Case Submitted by American Electric Power Company, Inc., p. 4 (Nov. 15, 2004) (AEP Narrative) (citing 267 F.3d at 614-15).

[24] *Checkosky v. SEC*, 306 U.S. App. D.C. 144, 23 F.3d 452, 465 (D.C. Cir. 1994) (Silberman, J. concurring). When "deciding whether to vacate an agency's decision pending further explanation," the District of Columbia Circuit considers "the seriousness of the order's deficiencies . . . and the disruptive consequences of an interim change that may itself be changed." *A.L. Pharma, Inc. v. Shalala*, 314 U.S. App. D.C. 152, 62 F.3d 1484, 1492 (D.C. Cir. 1995) (internal quotations omitted).

[25] *Allied-Signal, Inc. v. United States Nuclear Regulatory Comm'n*, 300 U.S. App. D.C. 198, 988 F.2d 146, 151 (D.C. Cir. 1993).

permitting AEP's acquisition of CSW and did not find that it would be too disruptive to deprive AEP of the necessary legal approval for the acquisition in the interim.

While AEP in its narrative summary characterizes the issues on remand as "narrowly defined" by the court of appeals,[26] these issues were serious, went to the fundamental basis for the Commission's approval order, and warranted vacating the order. The Commission's order of August 30, 2004, instituting the hearing in this proceeding thus recognized that "further supplementation of the record is required for us to address the issues identified in the Court's opinion and to determine on remand whether the combined AEP and CSW systems meet the relevant standards of sections 10(c)(1) and 11(b)(1) of the Act and in particular, what specific facts about AEP and CSW's electric systems and the geographic area covered by their systems are relevant to the required determinations."[27]

As shown below, however, much of the evidence summarized by AEP in its submission appears irrelevant to these determinations. Moreover, AEP's narrative summary suggests an attempt to so narrow the relevant issues that the Commission would have to—once again—read those requirements out of the Act.

Narrative Summary of NRECA and APPA's Evidence and Legal Theories

The proposed acquisition should not be approved under section 10 of the Act. The Act was written to protect utility customers, investors, and the public against the undue aggregation of economic power of large, multi-jurisdictional public utility holding companies.[28] The

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[26] AEP Narrative, p.4.

[27] *American Elec. Pwr. Co.*, Release No. 35-27886 at 3 (S.E.C. Aug. 30, 2004).

[28] *See, e.g., American Elec. Pwr. Co.*, Release No. 35-20633, 1978 WL 19453 at *6 (S.E.C. July 21, 1978) ("The statute was enacted against a background of unbridled and unsound expansion of utility holding companies controlling utilities scattered from coast to coast .... Holding companies were piled on top of holding companies

statutory presumption is against large mergers. Allowing AEP to acquire CSW and form the largest holding company in the country would set a dangerous precedent and effectively end enforcement of the Act. Approval of the acquisition—especially now, after the virtual collapse of the merchant generation sector that was supposed to provide competition to incumbent monopolists like AEP and CSW—would signal to the industry that the Commission is prepared to rubber-stamp mergers of any size, regardless of the Act's clear purposes of limiting the size of holding companies, simplifying their structures, and maintaining their effective regulation to protect consumers, investors, and the public. This proposed acquisition would aide and abet the very harms the Act was intended to prevent. It would (and indeed, its initial approval did) herald the re-formation of the vast holding companies that the Act was designed to dismantle and prevent from recurring.

As explained below, the proposed merger fails to meet the integration requirements of the Act. The proposed merged company would not be an "integrated public-utility system." Its assets would not be "physically interconnected or capable of physical interconnection." Its operations would not be "confined to a single area or region."

A. Interconnection

The proposed acquisition does not satisfy the requirement the merged entities' assets be physically interconnected or capable of physical interconnection. AEP has not shown why its unidirectional contract path will effect the required interconnection consistent with the Act and Commission precedent.

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resulting in highly leveraged structures of extraordinary complexity.") (citing S. Rep. No. 621, 74th Cong., 1st Sess., 55 (1935)).

1. Unidirectional contract path

It appears from AEP's narrative summary that the company has not undertaken and does not plan to undertake the one easy step that would solve part of its dilemma: buy a bi-directional contract path. (Although even then, the Commission would still have to explain why such a path is sufficient to integrate distant utilities.) Instead, AEP states that the company intends to rely on (1) a unidirectional, east-to-west contract path of unknown size and term; (2) *non-firm* transmission in the reverse direction over that same indeterminate path; and (3) open-access transmission service over third parties' transmission systems from west-to-east.[29] These three strategies, however, are insufficient to meet the court's concerns. Indeed, AEP is creating new difficulties for itself and the Commission.

In its prior application to the Commission, AEP relied on a temporary, four-year transmission contract for 250 megawatts, which provided for power transfers in only one direction (east to west). By its terms, that contract path has now expired. Apparently seizing on the court's finding that neither the 250-MW size nor the four-year term was insufficient on its face,[30] AEP now provides no description of the path capacity or the contract term on which it currently relies. But the court's opinion did not grant AEP such license. Without some knowledge of the capacity and term of the agreement, it is impossible to determine whether the AEP and CSW utility assets are "physically interconnected or capable of physical interconnection" such that its assets "under normal conditions may be economically operated as a single interconnected and coordinated system." The interconnection requirement under the

[29] AEP Narrative Summary, p. 9.

[30] 276 F.3d at 614.

Act, while distinct from the coordination requirement, cannot be read in isolation. A one-megawatt unidirectional path would not suffice, it is safe to say.

AEP also relies on the fact that its "firm reservation also includes the option for AEP to reverse the flow from west to east on a non-firm basis at any time at no additional charge."[31] Such non-firm point-to-point transmission service is an unreserved, interruptible service that is available only if not pre-empted by requests for reserved, firm service or by prior requests for non-firm service. The "reversibility" that AEP describes is a feature of any firm, point-to-point transmission service provided under a FERC-regulated open-access tariff. While AEP does not state definitively that its contract path is provided under such a tariff, the fact is that such non-firm service is nothing distinctive or new. In fact, AEP could seek to obtain such non-firm service (if and when it is available), even without having its unidirectional contract path; the only thing the contract path provides is that AEP does not have to pay an additional charge for the additional non-firm service, if it is available. In short, the "reversibility" feature adds nothing to AEP's ability to integrate the AEP and CSW assets.

That brings us to the third item AEP has identified in its narrative summary—the general availability of open-access transmission service west-to-east over the transmission systems of intervening utilities. Again, this is nothing new or distinctive to AEP and CSW: nearly any two utilities in the country could make the same claim of integration. If the mere availability of open-access transmission service is sufficient to integrate two (distant) utilities, then the interconnection requirement of the Act indeed becomes a nullity. None of the Commission precedent cited by AEP in its narrative summary stands for that broad proposition.

[31] AEP Narrative Summary, p. 5.

Moreover, despite AEP's assurances, the availability of open-access transmission service is uncertain, and its price may be uneconomic to integrate distant utilities. The price and availability of service matter. With the advent of locational marginal pricing regimes under FERC policies, the pricing and availability of transmission service is becoming less and less certain for long-term arrangements—which is exactly the kind of service that AEP posits it will have even without buying a firm contract path or building a line. While AEP states that it will provide data showing the availability of non-firm transmission service, the quality of that data and inferences that may be drawn from it remain to be seen.

Moreover, by relying on non-firm, west-to-east transmission service under open-access transmission tariffs (whether in conjunction with AEP's east-to-west contract path or not), AEP is essentially asking the Commission to adopt arguments that the court of appeals already considered and rejected. In its brief to the court of appeals, AEP asserted that "the need for interconnection was primarily" east-to-west, but noted that AEP had also provided for west-to-east transactions.[32] Thus, AEP "determined that there would be adequate transmission capacity available on a non-firm basis to accommodate economic transfer from CSW to AEP [west-to-east transfer]."[33] As AEP argued before the court, "contrary to Petitioners' Brief, west-to-east transfers are available and are 'economically feasible' – it was simply more efficient to handle such transfers on a non-firm basis."[34]

Accordingly, the court—at the time of its decision—was aware that AEP and CSW had available to them both a 250-MW contract for an east-to-west connection and non-firm

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[32] Brief of Intervenor, No. 00-1371, p. 31.

[33] *Id.*

[34] *Id.*

transmission options for a west-to-east connection. Nonetheless, the court determined that the interconnection path between AEP and CSW was unidirectional contract path but could not "understand how a system restricted to unidirectional flow of power from one half to the other" satisfied the Act's statutory interconnection requirement.[35] If the court of appeals thought there was any merit in AEP's argument that these non-firm arrangements satisfied the Act's interconnection requirement, it would not have had to vacate the Commission's order in those terms.

The case that AEP has summarized in its narrative mirrors that before the court of appeals. AEP invites the Commission to adopt the same rationale that the court has already rejected. Indeed, AEP appears to invite the Commission to adopt even more far-reaching rationales, which would dispense with the need for a contract path altogether and rely on the (uncertain) availability of open-access transmission service to constitute interconnection under the Act. The court has already warned the Commission that it may not read a statutory provision "so flexibly as to read it out of the Act."[36] The Commission should not commit the same error in the same case twice.

2. Consistency with Prior Precedent

The court also cited the Commission's failure "to follow its own prior reasoning regarding interconnection of distant utilities."[37] The court agreed with NRECA and APPA that

[35] 276 F.3d at 615.

[36] *Id.* at 618.

[37] *Id.*

"the Commission has clearly indicated that a contract path cannot alone integrate distant utilities" and was "obligate[d] ... to provide some rationale for its current contrary view."[38]

While AEP asks that the Commission "disavow" its prior holdings,[39] there is no reason for the Commission to do so now simply to accommodate AEP. If the Commission did, it would effectively allow nearly any two utilities to claim they now meet the interconnection requirement of the Act. AEP's acquisition of CSW is exactly the type of consolidation that Congress enacted the Act to prevent or reverse.

A long contract path may be a sign that two utilities are not in a single area or region, as AEP argues.[40] But the length of a contract path—like the capacity or term or firmness of the contract service—is directly relevant to the Act's interconnection requirement. The length of the contract path has both physical and economic dimensions, either of which can prevent the utility assets from being interconnected so that they may be economically coordinated. A long path is more easily interrupted. It is also generally more expensive. These considerations are relevant to determining whether two utilities are physically interconnected or capable of physical interconnection so that they may be economically coordinated. Thus, the court of appeals has affirmed the Commission's prior determination that the term "economically" in section 2(a)(29)(A) of the Act imposes a requirement "that facilities, in addition to their physical interconnection, be consolidated so as to take advantage of efficiencies."[41]

AEP claims that the advent of FERC-regulated regional transmission organizations (RTOs) will eliminate rate pancaking and thus diminish the economic barrier presented by a long

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[38] *Id.*

[39] AEP Narrative, p. 10.

[40] *Id.*

[41] *City of New Orleans v. FERC*, 969 F.2d 1163, 1168 (D.C. Cir. 1992).

contract path. But as shown below, AEP and CSW cannot be integrated by means of an RTO tariff—they will require service using multiple, additive transmission rates of multiple RTOs for the foreseeable future.

AEP claims that the distance between AEP and CSW is less than the distance between other utilities that the Commission has permitted to merge. NRECA and APPA do not concede that point. In particular, AEP does not explain what measure of distance it will employ and why it is relevant under the statute. Moreover, the cases AEP cites[42] are distinguishable on other grounds as well—*e.g.*, the availability of a single RTO tariff (*Exelon*), or the promise to build a transmission line (*New Century Energies*). Utilities may be "distant" for more reasons than simply measuring the distance between the two nearest pieces of utility equipment. By any reasonable measure, AEP and CSW are distant from one another. Accordingly, AEP and CSW have not shown that they are sufficiently interconnected under the Act by a contract path.

B. The "Region Requirement"

In its opinion, the court of appeals made clear that, in order to win approval of its merger with CSW, AEP must demonstrate, independent of the other requirements of section 2(a)(29)(A) of the Act, that the merged company will be "confined in its operations to a single area or region." AEP acknowledges this requirement in its narrative summary in this case.[43] Nevertheless, AEP is unable to identify the single region in which the merged company will allegedly operate. This is hardly surprising, for the territory of the merged company stretches from southern Michigan – near the Canadian border – all the way to the Mexican border. AEP's

[42] AEP Narrative, p. 10.

[43] AEP Narrative, p. 11.

inability to identify a single region encompassing Canton, Ohio and Brownsville, Texas is not surprising—there is no such region.

Instead, AEP identifies two "considerations" it wishes the Commission to keep in mind. It then invents four theories which it urges the Commission to rely upon to conclude that the entire area covered by the merged company, however large in land area and however varied in geography, economics, and population density, can somehow be labeled a single region. None of AEP's theories or "considerations," however, can overcome the simple fact that the service territories AEP seeks to merge are not located in a single region.

AEP first urges the Commission to keep in mind that the Act requires consideration of "the state of the art."[44] Significantly, the language quoted by AEP is actually in reference to the Act's "localization" requirement, rather than the "region" requirement.[45] Moreover, while AEP refers to consideration of "changes in engineering and technology,"[46] it cites to no specific technological advances, nor does it explain how electrical engineers could make Michigan and Texas part of the same region. Essentially, AEP urges the Commission to repeat the same mistake regarding the region requirement already noted by the court of appeals:

> The Commission applies the requirement as if it did not include the word "single" but instead read: "confined to an area *or areas* not so large as to impair . . . ." Technological improvements may well justify ever-expanding electric utilities, but PUHCA confines such utilities to a "single" area or region.[47]

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[44] *Id.* at p. 13.

[45] Specifically, section 2(a)(29)(A) of the Act requires that the merged company operate in a region "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."

[46] AEP Narrative, p. 14.

[47] 276 F.3d at 618.

AEP's second consideration is that the Commission interpret section 2(a)(29)(A) as a whole and in light of the overall purposes of the Act.[48] NRECA/APPA agree wholeheartedly. The purpose of the Act is to prevent the abuses that can occur "when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties,"[49] and the Commission should indeed keep this purpose in mind in considering AEP's application.

AEP next provides four separate rationales upon which it urges the Commission to find that the merged company's operations are confined to a single area or region. Viewed most generously, AEP's arguments may prove at most that, as compared with the situation that prevailed in 1935, when the Act was passed, there is increased contact of various sorts between the different regions in which the AEP and CSW systems are located. These arguments do not – can not – relocate Brownsville, Texas into the same region as the Great Lakes.

First, AEP claims that trade flows and infrastructure demonstrate that the area served by the combined company is a single area or region. AEP points to "road networks, waterways, pipelines, telecommunications systems and other facilities that have developed considerably over the past 70 years to lower the cost of both transportation and communications and to facilitate trade...."[50] Here AEP confuses the lowering of barriers to trade and communications between regions with the creation of regions. It is indeed a great boon to trade and transportation that interstate highways (for example) run unimpeded from coast to coast. Yet New York and San Francisco, lying at opposite ends of Interstate 80, are not in a single region, however much that

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[48] AEP Narrative, p. 14.

[49] Section 1(b)(4) of the Act.

[50] AEP Narrative, p. 15.

highway may facilitate contact between the different regions through which it passes. Indeed, many of the same developments in transportation and communications have facilitated growth in trade internationally, not just between regions of this country. Nevertheless, the fact that Wal-Mart purchases a significant volume of goods from China does not put Beijing and Bentonville, Arkansas in a single area or region.

Next, AEP claims that the entire Eastern interconnection should be treated as a single region. No precedent supports the notion that the entire Eastern Interconnection is a single area or region, as that term is used in section 2(a)(29)(A) of the Act. Nor would AEP prevail if this theory were accepted, for it seeks approval for an entity that would not operate entirely in the Eastern Interconnection. In fact, as AEP itself is forced to acknowledge, the CSW utilities operate partly in the Eastern Interconnection and partly in the electrically distinct and separate Electric Reliability Council of Texas ("ERCOT"). While it is true that the prior operation of CSW, partly in ERCOT and partly in the contiguous Southwest Power Pool, Inc. ("SPP"), was determined to nevertheless be in a single area or region, it hardly follows that ERCOT must therefore be determined to be in the same region as Ohio or Michigan. In any event, making this second argument undercuts the logic of AEP's first argument, because the electrical isolation of the portions of the company in ERCOT would prevent AEP from taking advantage of the advances in trade flows and infrastructure that AEP itself touts. Regardless of advances in technology and engineering, flows between the portion of CSW in ERCOT and the rest of CSW—much less AEP—will remain extremely constricted. Thus, to the extent the Commission agrees with AEP that trade flows are an important indicator of the existence of a single region, it must find that the merged company will not in fact operate in a single area or region.

AEP's third argument is that the area encompassed by contiguous RTOs with existing or contemplated robust Joint Operating Agreements ("JOAs") is effectively a single area or region. This argument fails on several fronts. First, the very name "Regional" Transmission Organization indicates that each RTO is a separate region, and that contiguous RTOs are contiguous regions. Under FERC's Order No. 2000, an RTO "must serve an appropriate region" that is sufficient in scope and configuration to permit it "to maintain reliability, effectively perform its required functions, and support efficient and non-discriminatory power markets."[51] While FERC also directs RTOs to develop inter-regional coordination and appropriate mechanisms to "ensure the integration of reliability practices within an interconnection and market interface practices among regions,"[52] those arrangements by definition are "among regions," and FERC recognizes that inter-regional coordination arrangements between RTOs are complex, difficult efforts. AEP's reliance on the inter-regional coordination process is unwarranted since regional cooperation is uncertain at best. Additionally, AEP fails to provide any criteria for what constitutes a "robust" JOA, or to explain how an agreement between transmission operators to exchange operational information, and to jointly manage transmission congestion, operates to change regional boundaries. At most, such an agreement may facilitate trade in one commodity – electricity – between neighboring regions.

Moreover, it is not clear that a "contemplated" JOA – which is all that exists today between SPP and its neighbor to the northeast, the Midwest Independent Transmission System Operator, Inc. ("MISO") – can even do that. Indeed, given the significant differences that

[51] 18 C.F.R. § 35.34(j)(2) (2004).

[52] 18 C.F.R. § 35.34(k)(8).

currently exist between SPP and MISO as to what form such a "seams agreement" should take,[53] it may be an overstatement to say that even a "contemplated" agreement exists between those organizations.

Additionally, while AEP in its Narrative sings the praises of RTOs as expanding regional boundaries and helping to create a single region of the entire eastern United States, the fact is that AEP itself has a less than ironclad commitment to RTO membership. In fact, AEP's two subsidiaries located in the SPP region[54] have given notice, as required by the SPP Membership Agreement, of their intent to withdraw from the SPP.[55] AEP can hardly be permitted to point to the existence (or, in the case of SPP, conditional existence) of RTOs as permanently changing the regional boundaries of the entire country when AEP itself insists on keeping open the option of its utility subsidiaries not to participate in RTOs.

More fundamentally, however, AEP is simply incorrect in positing that changes in operations among electric utilities can, in and of themselves, create single regions within the meaning of section 2(a)(29)(A). If that were the case, the region requirement would be a nullity, for the very act of combining ownership and operation of two companies' electric facilities would be sufficient to demonstrate the existence of a single region. Clearly what the statute requires is a determination that the service territories to be served are within a pre-existing single

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[53] Regarding SPP's proposed JOA, MISO has stated "the proposed JOA is primarily deficient because it fails to include the key provisions governing congestion management and flowgate coordination, which the Commission has recognized as the *raison d'etre* for a 'seams' agreement." Motion to Intervene, Motion to Reject Compliance Filing, Protest and Request for Hearing of the Midwest Independent Transmission System Operator, Inc. filed in FERC Docket No. ER04-1096-000 (August 23, 2004) at 2.

[54] Public Service Company of Oklahoma and Southwestern Electric Power Company.

[55] The giving of such notice by AEP was noted by the FERC in *Southwest Power Pool, Inc.*, 106 FERC ¶ 61,110 at P 67 (2004).

geographic region, not merely that the electric utilities serving them, including RTOs where applicable, are interconnected, or have transmission contracts approved by FERC.

Finally, AEP argues that the region requirement can be considered met because the service territories of the utilities with which the original AEP is directly interconnected (so-called "first tier" interconnected utilities) are contiguous to the service territories of the utilities with which the original CSW was directly interconnected. Essentially, AEP argues that the mere showing that the merging utilities are separated by no more than two wheeling transactions, without more, suffices to prove the existence of a single region. Thus, although the court of appeals has already instructed this Commission that a finding that the merging utilities are physically interconnected or capable of interconnection is insufficient to justify a finding that the merged company will operate in a single area or region, AEP now urges the Commission to find that the region requirement is met if the merging utilities are within two wheeling transactions of being physically interconnected. AEP's argument simply cannot be reconciled with the court's determination.

AEP acknowledges that, where the Commission has looked to the effect of a proposed merger upon the merging companies and the companies with which they are directly interconnected, it has done so in the context of section 10(b)(1) of the Act, which looks to the effects of a proposed merger upon competition. AEP's claim that, if the merging companies and those interconnected with either of them are the appropriate region for purposes of applying section 10(b)(1) of the Act, they must also be a single area or region for purposes of section 2(a)(29)(A) of the Act, simply urges the Commission to once again treat the region requirement as duplicative of other requirements, rather than as an independent, substantive condition that

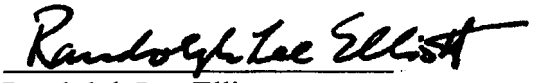
must be met in addition to the Act's other requirements. The court of appeals has already rejected such a reading of the Act.

Thus, based upon AEP's own preview of the evidence it intends to present, it is clear that the Commission will have no choice but to find that AEP has failed to meet its burden of demonstrating that the merged company will be "confined in its operations to a single area or region."

Conclusion

The proposed acquisition does not satisfy the Act's integration requirements. The proposed merged company would not be an "integrated public-utility system." Its assets would not be "physically interconnected or capable of physical interconnection." Its operations would not be "confined to a single area or region." The proposed acquisition should not be approved.

Respectfully submitted,



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