I. INTRODUCTION

In a Notice of Inquiry in this Docket issued November 15, 2012 (NOI), the Federal Energy Regulatory Commission called for comments on possible changes to its regulations under the natural gas market transparency provisions of section 23 of the Natural Gas Act (NGA), as adopted in the Energy Policy Act of 2005.¹ The Commission is considering whether market participants should be required to report detailed transaction-specific information regarding every natural gas transaction that entails physical delivery for the next day or the next month. The Commission seeks comments on several related issues, including the scope of the reporting requirement, the type of information to be reported, the burden on reporting companies, and possible public dissemination of reported information. The Department of Justice’s comment focuses on the competitive effects of the public dissemination of reported information.²


The Department urges the Commission to carefully consider the potential adverse
effect of transparency on competition, as required by the NGA.\(^3\) It is widely understood
that transparency can have pro- and anticompetitive effects. Transparency can increase
efficiency in production, consumption, and investment, thereby lowering prices for
consumers. Transparency also can facilitate market monitoring by the Commission and
the public. However, transparency can increase the likelihood of an exercise of market
power by facilitating coordination among suppliers, thereby raising prices for consumers.
In general, the risks of coordination are greater when transparency involves the
dissemination of detailed transaction-specific information, as is contemplated by the
Commission in this proceeding.

If the Commission chooses to issue new rules requiring that market participants
report information concerning natural gas transactions, it can reduce the likelihood of
anticompetitive effects by maintaining the confidentiality of any reported firm- or
transaction-specific information. Alternatively, the Commission may be able to achieve
some of the benefits of transparency while reducing the likelihood of anticompetitive
effects by releasing firm- or transaction-specific information only in limited
circumstances, or by aggregating, masking, or lagging the release of such information.

\(^3\) “In determining the information to be made available under this section and the
time to make the information available, the Commission shall seek to ensure that
consumers and competitive markets are protected from the adverse effects of potential
collusion or other anticompetitive behaviors that can be facilitated by untimely public
II. BENEFITS OF TRANSPARENCY: MONITORING & EFFICIENCY

Market transparency can benefit the public by facilitating market monitoring and by promoting efficient production and investment decisions.

Transparency can facilitate market monitoring by the Commission or the public. The collection of market information, including firm- and transaction-specific information, clearly can help the Commission identify, remedy, and deter violations of the Commission’s regulations, including its market manipulation regulations. Moreover, public dissemination of such information can help the public identify such violations and bring them to the attention of the Commission.

Transparency also can increase short-run efficiency by providing appropriate signals to suppliers about how much to produce. Information about actual or expected prices are necessary for suppliers to make economically rational decisions about how much to produce and sell. Better information about market prices and the factors that affect prices allow suppliers to assess the profitability of production, making it less likely that “too much” or “too little” production will take place and that production will take place only when it covers costs.

Finally, transparency can increase long-run efficiency by providing appropriate signals to suppliers and potential suppliers about how much to invest. Information about future market prices allows suppliers to better assess the profitability of investing in productive capacity. Similarly, information concerning the conditions that affect future prices (e.g., expected supply and demand conditions) permits suppliers to better forecast expected prices and assess likely investment profitability. Such price signals help reduce
the risk that “too much” or “too little” investment takes place and that investment will take place only when it is expected to cover its costs.

III. COSTS OF TRANSPARENCY: COORDINATION

Although transparency clearly has benefits, it also can have costs. In particular, public disclosure of firm- or transaction-specific information may reduce competition by facilitating coordination among suppliers that can increase prices, thereby harming consumers. Such coordination can involve the formation of an agreement, which almost certainly would violate the antitrust laws, or mutual interdependence, which may not violate the antitrust laws.

Successful coordination – whether through an agreement or mutual interdependence – entails three critical tasks: (1) reaching terms of coordination that are profitable to the suppliers involved; (2) detecting deviations from the terms that would undermine the coordination; and (3) punishing such deviations. Certain market conditions – such as transparency, high concentration, impediments to entry, a homogeneous product, a low elasticity of demand, and small and frequent sales – may render a market vulnerable to coordination, making it easier for suppliers to perform the three critical tasks. 4 Each of these market conditions is discussed briefly below:

- Transparency. Transparency may increase the amount of information available to suppliers about actions taken by other sellers. The more detailed this information, the better suppliers will be able to determine whether their rivals are adhering to the terms of coordination. When such information is made available quickly to suppliers, they will be

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4 These are among the most commonly cited factors affecting the likelihood of coordination. Other such factors are discussed in U.S. Dep’t of Justice & Fed. Trade Comm’n, Horizontal Merger Guidelines § 7 (Aug. 19, 2010), available at http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf.
able to more quickly punish deviations from terms of coordination. And anticipating that
it will be easier to detect and punish deviations from the terms of coordination, suppliers
may find it easier to coordinate their actions.

- **High Concentration.** Fewer suppliers in a market may make it easier for
  suppliers to reach, and detect deviations from, terms of coordination, increasing the
  likelihood that terms will be reached. For example, in more concentrated markets the
  market share of a given supplier will, on average, tend to be larger; and the larger its
  share, the more a supplier will gain from an increase in price and the greater will be the
  incentive to reach terms of coordination. Moreover, if a supplier with a relatively large
  market share deviates from the terms of coordination by underpricing, the greater the
  effect on price and the more noticeable is the deviation.

- **Impediments to Entry.** The greater are impediments to entry, the less likely it is
  that coordination among existing suppliers will be disrupted by the prospect of
  competition from new suppliers, increasing the likelihood of coordination.

- **Homogeneous Products.** If suppliers offer products that are differentiated by
  quality, it can be difficult for them to reach terms of coordination; additionally, a supplier
  may deviate from terms of coordination by offering a higher quality product. By
  contrast, suppliers of a homogeneous product need to agree on only one price; and
  because they compete primarily on price, it is easier for suppliers to reach, and detect
  deviations from, terms of coordination.

- **Low Elasticity of Demand.** The less elastic is demand for a product, the higher
  the price that coordinating suppliers can profitably set, the greater the gains to
  coordination, and the more likely it is that suppliers will coordinate their actions.
• *Small and Frequent Sales.* The smaller are sales, the smaller the gains to a supplier from deviating from terms of agreement on any given sale. The more frequent are sales, the more quickly will other suppliers detect such a deviation. Hence, smaller and more frequent sales increase the likelihood of coordination.

**IV. MARGINAL EFFECTS OF TRANSPARENCY**

The costs and benefits of any new regulation that increases transparency likely will depend on the extent to which gas markets are vulnerable to coordination, as well as the degree to which the markets already are transparent to suppliers, consumers, and the Commission. To determine whether a new regulation is desirable, the Commission may wish to consider the *marginal* effect of the regulation on transparency; that is, the *change* in transparency, and the associated benefits and costs, brought about by the regulation. If the marginal costs (i.e., the increased risk of coordination) outweigh the marginal benefits (i.e., enhanced efficiency and market monitoring) of the additional transparency resulting from the regulation, then the regulation should not be implemented. If the marginal benefits outweigh the marginal costs, then it may be desirable to implement the regulation.

**V. SAFEGUARDS AGAINST COORDINATION**

The Commission may be able to reduce the costs of increased transparency arising from the dissemination of firm- or transaction-specific information by adopting certain practical safeguards. There are three types of safeguards that the Commission may wish to consider. First, and most obviously, the risks of coordination can be reduced by maintaining the confidentiality of any firm- or transaction-specific information reported to the Commission. This would eliminate the ability of suppliers to use such
information for purposes of coordination. Moreover, it still would permit the Commission to monitor markets. However, it would eliminate the benefits that transparency can have on efficiency, and on the ability of the public to monitor markets.

Alternatively, the Commission may be able to achieve some of the benefits of transparency while reducing the likelihood of coordination by releasing firm- or transaction-specific information only in limited circumstances. For example, rather than release all firm- and transaction-specific information it collects, the Commission could release such information only if it has reason to believe that market participants have violated its market manipulation rules. Or the Commission could release transaction-specific information if market prices exceed a threshold level that might indicate potential market manipulation concerns. Such limited release of transaction-specific information might deter suppliers from violating the Commission’s rules and help the public better understand the market, while at the same time reducing the likelihood of coordination.

Finally, the Commission may be able to more fully realize the benefits of transparency while reducing, at least in part, its potential anticompetitive consequences through three practical safeguards: aggregation, masking, and lagging. First, appropriately aggregated information makes it difficult for suppliers to determine whether others are abiding by terms of coordination; knowing that it is difficult to detect deviation from those terms, suppliers will be less likely to reach terms of coordination. Second, and for the same reason, appropriately masking firm- or transaction-specific information would hinder suppliers from using the information to reach terms or from detecting and punishing a deviation from terms of coordination. Even if it is deemed appropriate to disseminate firm- or transaction-specific information, masking the identity
of the parties to the transaction may deter coordination by undermining the usefulness of
the information to reach terms of coordination. Finally, releasing information with a
time lag will keep suppliers from immediately knowing whether others have abided by or
deviated from terms of coordination, increasing the likelihood that deviations will occur,
and thereby undercutting the likelihood and likely effectiveness of coordination.

Whether any of these safeguards are appropriate will depend on the relative
marginal benefits and costs of the dissemination of firm- or transaction-specific
information as contemplated by the Commission. The greater the marginal costs, in
terms of an increased risk of coordination, the stronger the case for limited or no release
of transaction-specific information. The greater the marginal benefits, in terms of
increased efficiency or more effective market monitoring, the stronger the case for a
broader release of transaction-specific information. However, such costs and benefits
cannot be evaluated in the abstract; rather, their evaluation requires a close consideration
of the structure and characteristics of natural gas markets, and of the marginal effect on
transparency of the specific regulation under consideration.

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5 However, in a market with a small number of suppliers, aggregating and
masking may not be sufficient to prevent suppliers from learning enough about their
rivals to substantially diminish the likelihood of coordination. In the extreme case of two
suppliers, masking and aggregating would not prevent each supplier from unmasking or
disaggregating the information to reveal the other supplier’s information. Hence,
aggregation or masking is effective only when there are a sufficient number of market
participants. In the case of a market with few suppliers, when aggregation or masking
may not be effective, it may be desirable to maintain the confidentiality of collected
information or increase the lag with which information is released to the public.
VI. CONCLUSION

As the Commission decides whether to issue new regulations regarding transparency, the Department urges it to consider carefully the characteristics of, and the existing degree of transparency in, natural gas markets to avoid unnecessarily increasing the likelihood of coordination among gas suppliers. It is particularly important that the Commission do so in the present proceeding. Unlike the Commission’s existing natural gas transparency regulations, which call for the collection and dissemination of aggregated information, the NOI contemplates the dissemination of disaggregated, transaction-specific information, which may increase substantially the risk of coordination.

If the Commission decides to issue rules calling for the collection of highly detailed information about these markets, it may be able to eliminate or reduce the likelihood that the rules will facilitate collusion by maintaining the confidentiality of any firm- or transaction-specific information it collects, or by disseminating such information only in limited circumstances. Alternatively, the Commission may achieve transparency’s benefits to a greater extent, while limiting its potential harm, by aggregating, masking, and/or lagging the release of such information.

Respectfully submitted,

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