

prevent anticompetitive bidding behavior.⁸

11. In the November 20 Order, however, we also noted that this potential for market manipulation was not limited to the California market.⁹ In fact, the potential for market abuse and the exercise of market power may exist in any region where the evolution towards a competitive market is not yet complete; or where the design structure of the market is otherwise ill-equipped to promote competition; or where the supply/demand imbalance causes the market to be in disequilibrium.¹⁰ In the November 20 Order, therefore, we proposed to apply to all public utilities authorized to sell energy and ancillary services at market-based rates, the same conditions we had applied to market-based rate sellers in the western markets.

Hearing Procedures and Responsive Pleadings

12. The November 20 Order established paper hearing procedures to address the Commission's proposed tariff provision, with interested entities invited to file comments and reply comments. Numerous responsive pleadings were filed. In addition, a public conference was convened in this proceeding on March 11, 2002, to discuss issues raised in the comments and reply comments. Comments on the technical conference were filed on March 22, 2002.

Staff's Investigation of Market Manipulation in the Western Markets

13. Commission Staff addressed a broad range of market power issues and the need for market behavior rules, in its investigation of the Western energy markets, in Docket No. PA02-2-000.¹¹ In Staff's Initial Report, issued in August 2002, Staff made a number of findings regarding, among other things, the possible misconduct by Enron Corporation (Enron) and its affiliates, and the use, by Enron and its affiliates,

of the so-called Enron trading strategies.¹² These trading strategies, Staff found, included efforts to game the market in ways that were either fraudulent or otherwise anticompetitive. Moreover, Staff found that similar trading strategies were being utilized by a broad cross-section of the industry.

14. Subsequently, in the Western Markets Report, Staff recommended that the Commission condition all electric market-based rate tariffs and authorizations and all natural gas blanket marketing certificates on specific market behavior rules.¹³ Staff proposed that market-based rate sellers be required by their tariffs to: (1) Provide complete, accurate, and honest information to any entity that publishes price indices; (2) retain all relevant data and information needed to reconstruct a published price index for a period of 3 years; (3) explicitly prohibit the use of false information as a condition for granting all market-based rate authorizations; (4) require that data sent to firms publishing price indices be provided by the risk management office of the company, not the trading desk or a trader, and be certified by the chief risk officer; (5) ban any form of prearranged wash trading and prohibit the reporting of any affiliate trading activities through industry indices; (6) require that sellers who use trading platforms use only those trading platforms that agree to provide the Commission with full access to trade reporting and order book information for the trading systems and agree to adhere to appropriate monitoring requirements; and (7) prohibit the submission of false information or the omission of material information to the Commission or to an entity such as an independent system operator, a regional transmission organization, or an approved market monitor.

Discussion

Procedural Issues

15. A number of entities request rehearing of the November 20 Order.

However, rehearing may not be sought in this case until the Commission issues a final decision or other final order.¹⁴ Because the November 20 Order initiated an investigation and thus was not a final order, we will not consider requests for rehearing of the November 20 Order. However, we will treat these requests as comments to the degree they are relevant to our current proposal.

Proposed Tariff Revisions

16. Consistent with the findings and recommendations of the Western Markets Report and the comments filed in this proceeding, we propose new market behavior rules applicable to all market-based rate tariffs and authorizations. As set forth in the Attachment to this order, these market behavior rules would prohibit market manipulation and more clearly outline sellers' responsibilities and duties with respect to communications to regulatory authorities and market operators. Should a seller be found to have engaged in the transactions or behavior prohibited under our proposed market behavior rules, it would be subject to disgorgement of unjust profits obtained in contravention of the seller's tariff, and appropriate non-monetary remedies such as revocation of seller's market-based rate authority and revisions to seller's code of conduct.

17. As noted above, in proposing these market behavior rules we have attempted to strike a careful balance. On the one hand, it is essential, for all the reasons outlined in the November 20 Order and in the Western Markets Report, that our market behavior rules be clear and enforceable. Market conduct which is anticompetitive or which constitutes an abuse of market power must be prohibited and made subject to remedial action under the circumstances outlined herein. On the other hand, transactions and practices which are consistent with the normal operation of supply, demand, and true scarcity, or which otherwise have a legitimate business purpose, should neither be discouraged nor impeded. Further, while our proposal is designed to give the Commission and interested parties an enhanced ability to undertake effective enforcement and to require appropriate remedies, we understand that market participants need some level of certainty, that is, they need to know that they will not be exposed to open-ended uncertainty. Our proposal attempts to balance these two valid concerns by proposing appropriately-tailored complaint procedures and by

⁸ November 20 Order, 97 FERC at 61,975, citing *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service, et al.*, 95 FERC ¶ 61,115, order on reh'g, 95 FERC ¶ 61,418 (2001).

⁹ *Id.* at 61,975-76.

¹⁰ In addition, sellers may have the opportunity to exercise market power even in markets which are typically (and on most occasions) competitive. For example, extreme supply or demand conditions to which the market cannot quickly adapt, such as the loss of significant hydropower capacity because of drought, or force majeure events such as a major transmission line outage could provide opportunities to exercise market power even in a market that is normally workably competitive.

¹¹ Staff's investigation was initiated pursuant to our February 13, 2002 order in Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices, 98 FERC ¶ 61,165 (2002).

¹² See Initial Report on Company-Specific Separate Proceedings and Generic Reevaluations; Published Natural Gas Price Data; and Enron Trading Strategies: Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices, Docket No. PA02-2-000 (August 2002).

¹³ The Final Report also recommended that several entities participating in the California market (including Enron) be required to show cause why their authority to sell power at market-based rates should not be revoked by the Commission in light of their apparent involvement in market manipulation and gaming activities. Orders directed to these issues were subsequently issued by the Commission on March 26, 2003. See *Enron Power Marketing, Inc., et al.*, 102 FERC ¶ 61,316 (2003); *Reliant Energy Services, Inc., et al.*, 102 FERC ¶ 61,315 (2003).

¹⁴ See Rule 713 of the Commission's Rules of Practice and Procedure, 18 CFR 385.713 (2003).