

E. Market Behavior Rule 2(c)
(Prohibition Against Transactions
Relating to the Creation of Artificial
Congestion Followed by the “Relief” of
Such Artificial Congestion)

1. Commission Proposal

70. In addition to the prohibition against market manipulation set forth in proposed Market Behavior Rule 2, we also proposed, as a specific action or transaction that would be prohibited, “transactions in which an entity first creates artificial congestion and then ‘relieves’ such artificial congestion.”

2. Comments

71. Colorado Consumer Counsel, *et al.* argue that, in addition to the prohibition set forth in the proposed rule, the Commission should also address how all gradations of congestion will be managed in a wholesale market context and how market power, during periods of congestion, will be constrained.

72. Reliant asserts that the Commission’s apparent focus in Market Behavior Rule 2(c) is on market designs like those in California that do not use locational marginal pricing (LMP) as a tool to manage congestion. Reliant states that, if so, the Commission should clarify that its rule does not apply in LMP markets. EEI also questions the need and scope of the rule, noting that any transaction that would create “artificial congestion” would necessarily involve the submission of false information, as encompassed within the prohibition set forth in Market Behavior Rule 2(b). EEI and Pinnacle West also argue that the prohibition set forth in the rule should not apply to transactions that are consistent with an RTO’s or an ISO’s rules.

73. Reliant and EEI request that the Commission define what it means by “artificial congestion” because, in theory, this term could be construed to apply to (and thus be a sanction against) virtual transactions. Pinnacle West also requests clarification regarding the meaning of this term in this context.⁴²

74. The New York ISO also claims that Market Behavior Rule 2(c) requires clarification with respect to the day-ahead and real-time markets it operates. Specifically, the New York ISO claims that the proposed rule could be interpreted to prohibit changes in day-ahead schedules in response to changes in market conditions between the day-ahead and real-time markets, *i.e.*, to prohibit legitimate arbitrage between forward and real-time markets. Such a

prohibition, it is argued, would be harmful to these markets because it would restrict market participants from responding in a competitive manner to the forces of supply and demand. The New York ISO explains that, in practice, congestion that may exist in the forward market may not exist in the real-time market, where market participants are permitted to respond competitively to these changed conditions. The New York ISO concludes that Market Behavior Rule 2(c) should be read to permit such responses in the real-time market.

75. Commenters also assert that Market Behavior Rule 2(c) should be modified to incorporate an intent standard.⁴³ EPSA, *et al.* recommend that the prohibition apply to transactions in which an entity “intends to” first create artificial congestion and then relieve such artificial congestion.⁴⁴

3. Commission Ruling

76. We will adopt Market Behavior Rule 2(c), subject to the inclusion of an intent standard, as requested by commenters. As revised, Market Behavior Rule 2(c) will address, as a prohibited transaction:

Transactions in which an entity creates artificial congestion and then purports to relieve such artificial congestion (unless Seller exercised due diligence to prevent such an occurrence).

77. Commenters generally agree, as do we, that a Market Behavior Rule addressing market manipulation should include as an express prohibition transactions predicated on the creation and subsequent “relief” of artificial congestion. Experience has shown that in certain markets (including, in particular, markets that have not adopted an LMP market design) activities of this nature have been undertaken for the purpose of generating revenue without the occurrence of any corresponding economically substantive transaction.⁴⁵ Market Behavior Rule 2(c) makes clear that market manipulation of this sort, to the extent it can occur, has no legitimate business purpose and is therefore prohibited.

⁴³ See Comments of EPSA, *et al.* at Attachment B, pp. 3–4; Comments of Reliant at 10–11.

⁴⁴ See also Comments of Reliant at 10 (transactions in which an entity “intends first to create” artificial congestion and then “to purport to relieve” such artificial congestion); Comments of EEI at 15 (“intentionally engaging in transactions or scheduling resources that qualify for a congestion relief payment with the intent of profiting for relieving that congestion and canceling later is prohibited. This prohibition does not apply to transactions consistent with markets”).

⁴⁵ See Western Markets Report at VI at 26–30.

78. We agree with commenters, however, that Market Behavior Rule 2(c) should be revised to include an intent standard, *i.e.*, that the prohibition set forth in this rule should be predicated on a seller having knowingly committed the prohibited conduct. As we held, above, in addressing the use of this intent standard in the context of Market Behavior Rule 2(b), however, this due diligence exception will be applied only to the entity subject to this rule, *i.e.*, to the seller itself, not the individual acting on behalf of the seller who may have engaged in or otherwise authorized the prohibited conduct.⁴⁶

Moreover, we will find that the seller has knowingly violated this rule where the prohibited conduct is found to have occurred in the absence of adequate internal procedures designed to prohibit its occurrence.

79. Commenters also request clarification regarding the scope and definition of the term artificial congestion, as it will be interpreted by the Commission in the context of our rule. We will grant these requests and hereby clarify that artificial congestion, under our rule, will be understood to include all forms of congestion that may result from scheduling power flows in an uneconomic manner for the purpose of creating congestion (real or perceived).

80. Finally, the New York ISO seeks clarification that the prohibition set forth in Market Behavior Rule 2(c) is not intended to be applied in those cases where a market participant may be legitimately responding to changing circumstances relative to the day-ahead and real time markets. The New York ISO points out that from time-to-time, there may be a level of congestion in the day-ahead markets that is not present in real-time markets because market participants can respond to changing conditions. The New York ISO requests clarification that such real time responses to congestion that were anticipated in the day-ahead markets will not be prohibited under our rule. We will grant the requested clarification. The market responses addressed by the New York ISO reflect appropriate behavior which is reactive to the price signals emanating from the LMP congestion management system. Market conduct of this sort will not be characterized as a prohibited act under our rule.

⁴⁶ We make this same clarification, below, as it relates to Market Behavior Rule 3.

⁴² See also Comments of the New York ISO at 12–13.