

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION
103 FERC * 61,151

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell..

Communications with Commission-Approved Market Monitors Docket No. RT03-1-001

ORDER DENYING REHEARING

(Issued May 8, 2003)

I. BACKGROUND

1. On January 16, 2003, the Commission issued an order modifying the application of Rule 2201,[1] its rule on off-the-record or ex parte communications, as that rule applies to communications between Commission-approved market monitors and the Commission and its staff, and thereby treating such communications as exempt communications not subject to disclosure or notice.[2] The Commission based its decision on the view that these market monitors are practically an extension of, or a surrogate for, the Commission's own market monitoring and investigative staff. Because conversations between Commission staff are communications obviously not subject to Rule 2201, the Commission concluded that communications between the Commission and market monitors should be entitled to a similar degree of flexibility due to the similar tasks undertaken by market monitors.[3]

2. Six companies filed requests for rehearing in response to the January 16 Order.[4] They argue, inter alia, that the order violated various provisions of the Administrative Procedure Act ("APA"),[5] went beyond the scope of Rule 2201, and prejudiced the due process rights of the companies. As now discussed, the Commission denies rehearing.

II. DISCUSSION

A. The Administrative Procedure Act

3. The Electric Power Supply Association ("EPSA")[6] and the New England Consumer-Owned Entities ("NECOE")[7] argue that the exemption for ex parte communications with market monitors is the equivalent of a rulemaking.[8] Therefore, NECOE and EPSA assert that by not providing notice in the Federal Register or opportunity for public participation in modifying the application of Rule 2201, the Commission violated 5 U.S.C. * 553.[9] Both EPSA and NECOE argue that the January 16 Order does not fall within any of the exemptions to the notice and comment procedures.[10] Both companies specifically reject the notion that this order falls within the exemption for rules of practice and procedure, because they contend that it has a substantive effect as it alters the rights and interest of parties who appear before the Commission.[11]

4. NECOE's and EPSA's APA * 553 arguments are without merit. Rule 2201 provides that it "will apply to all contested proceedings, except that the Commission, may by rule or order, modify any provision of this subpart, as it applies to all or part of a proceeding, to the extent permitted by law." [12] Thus, Rule 2201 explicitly contemplates that the Commission could at a time after the promulgation of the regulations create specific exemptions to the general prohibition against off-the-record communications. [13] while the Commission initially used notice and comment procedures in adopting Rule 2201 in Order No. 607, such a process was not required for implementing the exception. Notice and comment procedures only apply to a rulemaking defined as an "agency process for formulating, amending or repealing a rule." [14] When an agency acts within the scope of a previous rule that unquestionably complied with the APA, then it is not engaging in rulemaking. [15] In establishing this exemption for communications with market monitors, the Commission acted within the regulations and guidelines set forth in Rule 2201, and did not amend Rule 2201. Therefore, the Commission did not engage in rulemaking within the meaning of the APA, and was not required to use notice and comment procedures.

5. Moreover, the APA generally requires an opportunity for notice and comment when an agency promulgates substantive regulations. Notice and comment are not required where a rule relates to agency personnel or agency organization, procedure or practice or when the agency for good cause finds that notice and public procedure are impracticable, unnecessary, or contrary to the public interest. [16] As the Commission has previously found, its ex parte rules and orders relate to the Commission's rules of practice and procedure. [17] Indeed, Rule 2201 is located in a section of the C.F.R. entitled "Rules of Practice and Procedure." [18] Thus, while the Commission chose to use notice and comment procedures to promulgate Rule 2201 in Order No. 607, because of the extensive changes to its ex parte regulations, it was not required to do so, and has amended the rule subsequently to codify a new exemption without using notice and comment procedures. [19]

6. The primary purpose of APA * 553 is "to ensure that agencies retain latitude in organizing their internal operations." [20] Furthermore, the "critical feature of a rule that satisfies the so-called procedural exception 'is that it covers agency actions that do not themselves alter the rights or interests of parties, although it may alter the manner in which the parties present themselves or their viewpoints to the agency.'" [21] while the January 16 Order may affect parties' ability to contest the presentation of viewpoints to the agency, it does not in and of itself alter parties' substantive rights. [22] Therefore, even if the January 16 Order had been subject to APA * 553, the Commission would not have been required to provide an opportunity for public comment.

7. NECOE further argues that permitting market monitors to make these ex parte communications violates 5 U.S.C. * 557(d), because market monitors are "interested parties" within the meaning of this provision. NECOE contends that market monitors who communicate with the Commission about a contested matter have a special interest in that proceeding, and hence fall within the broad definition of an "interested person." [23] To support this argument, NECOE, EPSA, and Reliant Resources, Inc. ("Reliant") claim that the Commission erred in determining that market monitors are independent from the interests of the Regional

Transmission Organization ("RTO") or Independent System Operator ("ISO").[24] Specifically, NECOE contends that the New England market monitor is not independent of the ISO New England, and the EPSC argues that the California market monitor is not an independent entity.[25] With the independent nature of these market monitors called into question, NECOE maintains that it has the impact of calling "into question the 'appearance' of 'open decision-making.'"[26]

8. NECOE's arguments regarding APA * 557(d) are groundless. When enacting this prohibition on ex parte communications, "Congress did not intend to erect meaningless procedural barriers to effective agency action." [27] This prohibition was intended to (1) prevent the appearance of impropriety and (2) to lead to fair decision-making.[28] Furthermore, this prohibition on ex parte communication was not meant to eradicate ex parte contacts that agency action sometimes demands.[29] Here, the off-the-record communications with market monitors are needed to enable the Commission to adequately oversee energy markets. Market monitors are not adversarial parties in these proceedings, but advisers to the Commission. Therefore, a Commission-approved market monitor's interest in the outcome of a particular proceeding does not make him an "interested person" as that term is used in APA * 706(d).

9. Along the same lines, while the market monitors may not be Commission employees, they serve as the functional equivalent of such employees. Market monitors are required, for example, to submit annual reports to the Commission, and report through the Commission's program offices any instances of misconduct by market participants.[30] Market monitors are also charged with reporting back to the Commission any problems and anomalies which they encounter so that the Commission may take appropriate action under the Federal Power Act.[31] Therefore, market monitors as the Commission's own staff play an important role in assisting the Commission in monitoring the everyday activities in certain power markets. Communications with market monitors are similar to communications between Commission staff, which give no appearance of impropriety, nor lead to biased decision-making.[32] As communications among Commission staff are exempt from APA * 557(d),[33] it follows that communications between their functional equivalent may also properly be considered to be exempt communications.

10. NECOE's and others' arguments regarding the market monitors' independence are misplaced. Challenges to the independence of any market monitor should be made in a specific proceeding involving that market monitor. The instant proceeding is not the appropriate forum to make such assertions. Moreover, in the January 16 Order, the Commission made no finding regarding the independence of the market monitors to which the order applied, nor did it base its decision on their independence from their respective RTO or ISO. Rather, the Commission limited the applicability of the exemption from the ex parte regulations to market monitors already approved by the Commission, provided they were not parties or otherwise participants in the relevant proceedings, and pointed out that issues of independence were being handled elsewhere.[34] Obviously a more ideal approach would be to have all independence issues resolved; however, on balance communications now between the Commission and the specified market monitors, within the noted limitations, are imperative to assist the Commission in its oversight of the energy markets. Under these circumstances, parties in contested

proceedings will not be unduly prejudiced.

11. NECOE contends that the Commission in the January 16 Order failed to explain how the Commission could meet its requirement under 5 U.S.C. * 706.[35] Specifically, NECOE argues that the Commission did not demonstrate how it will explain the ex parte communications it receives from market monitors in the formal record.[36]

12. As NECOE correctly notes, the January 16 Order expressly recognizes the requirements in APA * 706.[37] Its argument, however, highlights a fundamental misunderstanding of the role of market monitors in reaching Commission decisions. Market monitors are data collectors and "watchdogs" over the energy markets. Their sole duty is to report back to the Commission concerning what is going on in the markets. These communications will not negatively impact the fairness of the Commission's decision-making as they will simply provide background information on the current state of the markets. In this regard, as explained above, market monitor communications for all intent and purposes are similar to staff communications.

B. Scope of Rule 2201

13. Reliant, EPSA, and Dynegy Power Marketing, Inc ("Dynegy") maintain that the January 16 Order exceeded the scope of Rule 2201.[38] Specifically, EPSA and Dynegy argue that this rule only permits the rule barring ex parte communications to be "waived" on a case-by-case basis.[39] Dynegy also contends that modifications must be limited to a single identifiable proceeding or a set of proceedings.[40] Dynegy and EPSA further claim that the January 16 Order circumvents the Commission's own after-the-fact notice and disclosure requirements.[41]

14. As noted earlier, Rule 2201 specifically authorizes the Commission "by rule or order" to "modify any provision of this subpart, as it applies to all or part of a proceeding, to the extent permitted by law." [42] The Commission invoked this provision once before when it modified the application of Rule 2201 to permit State-Federal RTO Regional Panels to meet without public participation.[43] In the January 16 Order, the Commission acted in a similar fashion and modified the application of Rule 2201 to proceedings involving Commission-approved market monitors.

15. The parties' contention that the exemption must be done in a particular proceeding is in error. Thus, for example, the State-Federal Regional Panel Order was not limited to a specific proceeding or proceedings. Rather, it applied to all existing RTO proceedings as well as any proceedings that would be opened in the future. Otherwise, the purpose behind the order -- to facilitate discussions with state officials who have responsibilities related to the development of regional transmission organizations -- would have been frustrated. Likewise, here, the purpose behind liberalizing communications between the Commission and Commission-approved market monitors -- to ensure timely receipt of important market information -- would be impeded if the Commission was required to modify the application of Rule 2201 on a case-by-case basis.[44] The January 16 Order sets forth a policy of administrative practice. Requiring the Commission to repeat the policy for every relevant proceeding would be an administrative burden and a waste of resources. It could also thwart the market monitors' mission to

gather and report information in a timely and efficient manner.

16. Moreover, when determining the meaning of the Commission's regulations, unless the context indicates otherwise, "the singular includes the plural." [45] The term "proceeding" as used in Rule 2201 therefore includes "proceedings." In addition, there is no limitation in Rule 2201 that exemptions must be limited to identifiable proceedings. In these circumstances, the Commission acted within the scope of Rule 2201 in exempting proceedings involving designated market monitors from the general rule prohibiting off-the-record communications.

17. The Commission also acted appropriately in determining that subjecting communications between market monitors and the Commission to notice and disclosure under 18 C.F.R. * * 385.2201 (f) and (h) would frustrate the timely receipt of this information. As these procedures are not required by the APA, the decision of whether to apply these procedures to these particular off-the-record communications is clearly a matter of the Commission's discretion. Accordingly, not all exempt off-the-record communications are subject to notice and disclosure. [46] Furthermore, because market monitors are similar to the Commission's own staff, similar procedures may logically apply to the staff and the market monitors with respect to the notice and disclosure of these communications. The Commission's own staff is not subject to notice and disclosure and neither should be Commission-approved market monitors.

C. Due Process Concerns

18. As a final matter, EPSA, Dynegy, and NECOE raise due process concerns with the January 16 Order. [47] In particular, NECOE maintains that permitting these ex parte communications would be unfair to the parties, since they would have no way of finding out who submitted information on which the Commission is relying to make its decisions. [48] NECOE also contends that the "waiver" of Rule 2201 for the State-Federal RTO Regional Panel is not significant precedent for this exemption, because those parties were permitted an opportunity to respond to the ex parte communications. [49]

19. The Commission, as other agencies, is bound to reach decisions based on substantial evidence in the record. [50] That requirement, however, does not foreclose the Commission from developing internal rules of practice and procedure to handle off-the-record communications. Here, as discussed above, off-the-record communications between Commission-approved market monitors and the Commission and its staff are analogous to off-the-record communications between Commission staff and the Commission. The fact that the Commission has off-the-record communications with its own staff does not mean that it does not still have to base its decisions on substantial evidence in the record. The same is true with respect to off-the-record communications with Commission-approved market monitors. Both communications are merely "part of the way a decision maker gathers information." [51] If it were to rely on any particular communication, the Commission would be required to ensure the information was indeed part of the decisional record, or risk having its decision overturned in court. Thus, off-the-record communications of an advisory nature do not lead to due process violations. [52]

20. Furthermore, the Commission protected the due process rights of parties by ensuring that off-the-record communications are

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prohibited when the market monitor is a party or appears on behalf of a party in a proceeding.[53] The Commission is hence sensitive to situations where these off-the-record communications could undermine the integrity of the decision making process. In the other situations involving the five approved market monitors, such communications between those individuals and the Commission and its staff do not jeopardize the fairness of the proceedings.

The Commission orders:

For the reasons stated in this order, the requests for rehearing of the January 16 Order are denied.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

Footnotes

[1] 18 C.F.R. * 385.2201.

[2] Order Modifying the Application of Rule 2201 to Communications with Commission-Approved Market Monitors, 102 FERC * 61,041 (2003) ("January 16 Order"). The Commission identified five market monitors approved to date. See *id.* at P 1, note 1.

[3] *Id.* at P 10.

[4] Alabama Municipal Power Electric Authority, Dynegy Power Marketing Inc., Electric Power Supply Association, New England Consumer-Owned Entities, PPL Energyplus, LLC, and Reliant Resources, Inc.

[5] 5 U.S.C. * 553; 5 U.S.C. * 557(d); 5 U.S.C. * 706.

[6] PPL EnergyPlus, LLC adopts the arguments set forth in EPSA's request for rehearing. See PPL Request for Rehearing at p. 4.

[7] Alabama Municipal Electric Authority adopts the arguments set forth in NECOE's request for rehearing. See Alabama Request for Rehearing at p. 5.

[8] See EPSA Request for Rehearing at p. 7-13; NECOE Request for Rehearing at p. 8.

[9] APA * 553 requires an agency to publish notice of a proposed rulemaking in the Federal Register and to give interested persons an opportunity to comment on the proposed rule. See 5 U.S.C. ** 553(b), (c).

[10] APA * 553 states that the notice and comment provisions do not apply to interpretative rules, general statements of policy, or rules of agency organization, procedure, or practice. See 5 U.S.C. *553(A).

[11] See NECOE Request for Rehearing at p.16; EPSA Request for Rehearing at p.11.

[12] 18 C.F.R. * 385.2201(a) (emphasis added).

[13] See 18 C.F.R. * 385.2201(a). Generally, Rule 2201 prohibits off-the-record communications between Commission decisional staff and persons outside the Commission in contested on-the-record proceedings. There are nine codified exemptions to that prohibition. In addition, rulemaking and certain investigations are not considered on-the-record proceedings and thus do not fall within the scope of Rule 2201.

[14] 5 U.S.C. * 551(5).

[15] See *Vandermark v. Housing Authority of York*, 492 F. Supp. 359, 363 (M.D. P.A. 1980).

[16] See 5 U.S.C. * 553(b)(A) and (B).

[17] See Amendment to Rules Governing Off-the-Record Communications, Docket No. RM02-5-000, FERC Stats. & Regs. * 31,123 at p. 30,090 (2001) ("Order No. 623").

[18] See 18 C.F.R. Part * 385 (2002).

[19] See Order No. 623, FERC Stats. & Regs. * 31,123 at p. 30,090.

[20] *Aulenback, INC v. Federal Highway Administration*, 103 F.3d 156, 168 (D.C. Cir. 1997).

[21] *James V. Hurson Assoc. v. Glickman*, 229 F.3d 277, 280 (D.C. Cir. 2000) (quoting *Batterton v. Marshall*, 648 F.2d 694 (D.C. Cir. 1980); see also *City of Alexandria v. Helms*, 728 F.2d 643, 647-48 (4th Cir. 1984) (holding that notice-and-comment rulemaking is only required if the rule "makes a substantive impact on the rights and duties of the person subject to regulation."))

[22] See *American Hospital Assoc. v. Bowen*, 834 F.2d 1037, 1047 (D.C. Cir. 1987) (Mere impact on the substantive rights of parties is not enough to subject predominantly procedural rules to notice and comment procedures).

[23] See NECOE Rehearing Request at p. 12.

[24] See NECOE Rehearing Request at pp. 22-23; EPSA Rehearing Request at pp. 19-21; Reliant Rehearing Request at pp. 3-4

[25] See NECOE Rehearing Request at p. 22; EPSA Rehearing Request at p. 20.

[26] NECOE Rehearing Request at p. 13.

[27] *Profession Air Traffic Controllers Org. v. Federal Labor Relations Auth.*, 685 F.2d 547, 56-3-64 (D.C. Cir. 1982); see also H.R. Rep. No. 880 (Part I), 94th Cong., 2d Sess. at 20, reprinted in 1976 U.S.C.C.A.N. at 2202 (holding that "restrictions on off-the-record communications were not intended to cut an agency off from the general information it needs to carry out its regulatory responsibilities."))

[28] See *id.* at 563; see also *Portland Audubon Soc'y v. Endangered Species Comm.*, 984 F.2d 1534, 1539 (9th Cir. 1993)

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(holding that the APA was intended to "ensure that agency decisions required to be made on a public record are not influenced by private, off-the-record communications from those personally interested in the outcome.")

[29] See Texas Office of Pub. Util. Counsel v. Federal Communications Commission, 265 F.3d 313, 327 (5th Cir. 2001).

[30] See SMD NOPR, at p. 34,376.

[31] January 16 Order, 102 FERC * 61,041 at P 10.

[32] Ex parte communications between agency employees are exempt from * 557(d). See Hercules Inc. v. United States Environmental Protection Agency, 598 F.2d 91, 125 (D.C. Cir. 1978) (citing legislative history of * 557(d)).

[33] See 5 U.S.C. * 557(d).

[34] See January 16 Order, 102 FERC * 61,041 at P 11.

[35] See NECOE Rehearing Request at pp. 24-25.

[36] See id. at 24.

[37] See January 16 Order, 102 FERC * 61,041 at P 12 n. 25.

[38] See Reliant Rehearing Request at p. 6; EPSA Rehearing Request at pp. 5-7; Dynegy Rehearing Request at p. 4

[39] See EPSA Rehearing Request at p. 6; Dynegy Rehearing Request at 4.

[40] See Dynegy Rehearing Request at p. 4.

[41] See EPSA Rehearing Request at pp. 6-7; Dynegy Rehearing Request at pp. 7-8 (referring to 18 C.F.R. * 385.2201(f) and (h)).

[42] See 18 C.F.R. * 385.2201(a).

[43] See Order Announcing the Establishment of State-Federal Regional Panels to Address RTO Issues, 97 FERC * 61,182 (2001), reh'g denied, 98 FERC * 61,309 (2002), appeal dismissed sub num. Exelon Corp., et al. v. FERC, No. 02-1154 (D.C. Cir. Sept 20, 2002) ("State-Federal Regional Panel Order").

[44] A case-by-case approach would entail, for example a market monitor's filing a request to communicate with Commission staff in a particular proceeding. That request would be noticed and perhaps generate comments. The Commission would then need to issue an order. This process at a minimum would take several weeks, long after the market event which the market monitor must report or discuss with the Commission.

[45] 18 C.F.R. * 1.102(a); cf. Toy Mfrs. of America, Inc. v. Consumer Product Safety Com., 630 F.2d 70, 74 (2nd. Cir. 1980) (relying on 1 U.S.C. * 1 and the rule of construction that singular applies to several things to reject a statutory argument that "banning procedures were intended to deal with only one product at a time, and not with a broad range of products at the same time.")

[46] See 18 C.F.R. * 385.2201(e)(1)(I), (iii) and (viii).

[47] See EPSA Request for Rehearing, at pp. 22-24; Dynegy Request for Rehearing, at pp. 17-18; NECOE Request for Rehearing, at p. 18.

[48] See NECOE Request for Rehearing, at p. 18.

[49] See *id.* at pp. 26-27.

[50] See, e.g., *Pacific Gas & Electric Co. v. Federal Energy Regulatory Commission*, 306 F.3d 1112, 1115 (D.C. Cir. 2002).

[51] *Koster v. United States*, 231 Ct. Cl. 301, 309 (1982).

[52] See *Della Valle v. United States*, 231 Ct. Cl. 818, 821 (1983) (holding that *ex parte* recommendations of an advisory nature do not offend due process).

[53] January 16 Order, 102 FERC * 61,041 at P 11.