

103 FERC ¶ 61,016

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Fact-Finding Investigation into Possible Manipulation of Electric and Natural Gas Prices Docket No. PA02-2-005

ORDER PROVIDING FOR SUBMISSION OF BRIEFS

(Issued April 2, 2003)

1. In this order, we provide an opportunity for interested persons to provide comment on Commission Staff's interpretation, contained in Chapter VI of its Final Report on Price Manipulation in Western Markets (Docket No. PA02-2-000 March 26, 2003)(Final Report), of the California Independent System Operator's (ISO) and California Power Exchange's (PX) Market Monitoring and Information Protocol (MMIP).
2. This order benefits customers by providing a forum where this issue may be addressed and resolved.

Background

3. In an order issued by the Commission on February 13, 2002, in Docket No. PA02-2-000, we directed Commission Staff to investigate whether Enron Corporation (Enron), including any of its affiliates or subsidiaries, or any other entity participating in the wholesale energy markets in the West, had manipulated prices for electricity or natural gas or otherwise exercised undue influence over wholesale electricity prices, since January 1, 2000.¹

¹See Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices, 98 FERC ¶ 61,165 (2002) (February 13 Order). The February 13 Order, of
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4. Pursuant to the directive of the February 13 Order, Commission Staff undertook a comprehensive fact-finding investigation, encompassing both data gathering and data analysis of physical and financial transactions in and out of the California bulk power marketplace and related markets during 2000-2001.

5. In August 2002, Commission Staff released its Initial Report on potential manipulation of electric and natural gas prices in these markets, which included both findings and recommendations regarding, among other things, the possible misconduct by Enron and three of its affiliates, and the appropriateness of using publicly-reported natural gas price data in calculating potential refunds in the California Refund Proceeding.² Commission Staff expressly noted in this Initial Report, however, that its investigation into certain matters was ongoing and that other areas of inquiry and recommendations not addressed in its Initial Report may be included in its Final Report.

6. In Commission Staff's Final Report,³ Commission Staff notes that a number of entities, either individually or with others, appeared to have used what has been described as the Enron trading strategies.⁴ In addition, in Commission Staff's Final Report, Commission Staff notes that its market-level review of spot market clearing prices and its review of unit-specific, average monthly bid data provided by the ISO and PX, as well as

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course, was not the beginning point of our investigation into the justness and reasonableness of the rates of public utility sellers into the Cal ISO and Cal PX markets. For a general recitation of this procedural history, including the series of events and circumstances giving rise to the California energy crisis, see *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Services*, et al., 97 FERC ¶ 61,275 (2001).

²Initial 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).

³Final Report on Price Manipulation in Western Markets (Docket No. PA02-2-000 March 26, 2003).

⁴Final Report at VI-1, VI-11 - VI-44.

other evidence only recently reviewed, reveals what appears to be a pattern of economic withholding and inflated bidding in the ISO and PX short term energy markets for the period May 1, 2000 to October 2, 2000.⁵

7. Commission Staff's Final Report also describes the ISO's and PX's filed tariffs, and in particular the MMIP found in both tariffs.⁶ The Objectives section of the MMIP outlines its underlying purpose:

This Protocol (MMIP) sets forth the workplan and, where applicable, the rules under which the ISO will monitor the ISO markets to identify abuses of market power, to ensure to the extent possible the efficient working of the ISO Markets immediately upon commencement of their operation, and to provide for their protection from abuses that have the potential to undermine their effective functioning or overall efficiency in accordance with Section 16.3 of the ISO tariff.[⁷]

8. Part 2 of the MMIP goes on to identify what are termed "Practices Subject to Scrutiny." Among these practices are "gaming" and "anomalous market behavior." Gaming is defined at Section 2.1.3 of the ISO's MMIP as follows:

⁵Final Report at VI-1, VI-45 - VI-54.

⁶In this regard, the Commission Staff's Final Report describes the history of the MMIP. It states that the ISO and PX each initially submitted its MMIP (along with other protocols) for informational purposes only on October 31, 1997. The Commission, however, found that the protocols, including the MMIP, "govern a wide range of matters which traditionally and typically appear in agreements that should be filed with and approved by the Commission." The Commission accepted the protocols, including the MMIP, for filing, and directed the ISO and PX each to post the protocols on its Internet site and to file its complete protocols pursuant to Section 205 of the FPA within 60 days of the ISO's and PX's Operations Date (that date ultimately was April 1, 1998). The ISO and PX each made that compliance filing on June 1, 1998. Accordingly, the MMIP has been part of the ISO's and PX's filed tariffs since 1998. Final Report at VI-9 - VI-10.

Because both the ISO and the PX have substantially similar MMIPs, we refer below, for convenience, only to the ISO's MMIP.

⁷MMIP 1.1.

[T]aking unfair advantage of the rules and procedures set forth in the [Cal] PX or [Cal] ISO Tariffs, Protocols or Activity Rules, or of transmission constraints in periods in which exist substantial Congestion, to the detriment of the efficiency of, and of consumers in, the [Cal] ISO Markets. "Gaming" may also include taking undue advantage of other conditions that may affect the availability of transmission and generation capacity, such as loop flow, facility outages, level of hydropower output or seasonal limits on energy imports from out-of-state, or actions or behaviors that may otherwise render the system and the ISO Markets vulnerable to price manipulation to the detriment of their efficiency.

9. Anomalous market behavior is defined at Section 2.1.1 of the ISO's MMIP:

"Anomalous market behavior" . . . is . . . behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or as behavior leading to unusual or unexplained market outcomes. Evidence of such behavior may be derived from a number of circumstances, including:

* * *

unusual trades or transactions;

pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions, e.g., prices and bids that appear consistently excessive for or otherwise inconsistent with such conditions; and

unusual activity or circumstances relating to imports from or exports to other markets or exchanges.^[8]

⁸MMIP 2.1.1.5 further provides that:

The Market Surveillance Unit shall evaluate on an ongoing basis, whether the continued or persistent presence of such circumstances indicates the presence of behavior that is designed to or has the potential to distort the operation and efficient functioning of a competitive market, e.g., the strategic withholding and redeclaring of capacity, and

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10. The Commission Staff's Final Report concludes that the conduct at issue here, identified above, falls within the definitions of gaming and/or anomalous market behavior identified in the ISO's and PX's MMIP,⁹ which, as noted, is part of the ISO's and PX's tariffs. Commission Staff contends that the MMIP puts market participants on notice regarding their rights and obligations in the marketplace. It serves as the "rules of the road" for market participants. According to Commission Staff, market participants cannot reasonably argue that they were not on notice that the conduct referred to above adversely affected the efficient operation of the ISO and PX markets and would violate, i.e., is prohibited by, the MMIP.

11. The MMIP, Commission Staff indicates, also contemplates that these rules will be enforced or otherwise carried out, when necessary, whether by the Market Surveillance Unit, in the form of monitoring and reporting, or by the appropriate body or bodies (including this Commission), in the form of corrective actions.¹⁰ MMIP 2.3 and its several subparts address how the ISO, including the Market Surveillance Unit, is to respond to market participants engaging in any of the suspect practices delineated in the MMIP. While the MMIP outlines intermediate steps (such as arranging for alternative dispute resolution or proposing language changes to the tariff), ultimately, the MMIP directs the Market Surveillance Unit to refer matters to this Commission for enforcement.¹¹ In other words, Commission Staff explains, the MMIP contemplates that, while the ISO may try to correct misconduct on its own, the Commission is to be "the court of last resort" for misconduct committed by market participants, including the

⁸(...continued)

whether it indicates the presence and exercise of market power or of other unacceptable practices.

⁹Final Report at VI-6 - VI-11. Commission Staff's Final Report goes on to recommend that such violations warrant disgorgement of profits. Final Report at VI-1, VI-10 - VI-11.

¹⁰Sections 2.3, 3.3.4, and 7.3 of the MMIP outline the procedures to be followed by the ISO and the PX when a market participant is found to have engaged in any of the suspect practices delineated in the MMIP. While the MMIP empowers the ISO and the PX to resolve these matters without recourse to the Commission (by arranging for ADR, imposing sanctions and penalties, or proposing language changes to their respective tariffs), ultimately, if these remedies will not suffice, the MMIP directs the Market Surveillance Unit to refer matters to the Commission for enforcement.

¹¹MMIP 3.3.4.

"gaming" and "anomalous market behavior" misconduct defined in the MMIP. Moreover, Commission Staff notes that, while Part 2 of the MMIP enumerates suspect practices, MMIP 7.3 authorizes the ISO to impose "sanctions and penalties" or, as particularly relevant here, to refer matters to the Commission for appropriate sanctions or penalties. While the Commission's role, in this regard, may be triggered by the referral procedures outlined in the MMIP, Commission Staff states, the Commission also possesses the authority to enforce a rate schedule on file even in the absence of a referral; the Commission is authorized to enforce a tariff with or without the assistance of a complaint or a referral.

12. Based on its interpretation that the MMIP is a prohibition on certain market behaviors and that the MMIP is incorporated in tariffs on file with the Commission, and its determination that certain market participants, either individually or with others, appear to have engaged in market manipulation (including the Enron trading strategies and economic withholding and inflated bidding), Commission Staff recommends that the Commission issue orders to show cause why profits should not be disgorged.

Discussion

13. The Commission will provide that any interested person may submit a brief, double-spaced and no more than 30 pages, on Commission Staff's interpretation, contained in Chapter VI of its Final Report, of the ISO's and PX's MMIP.¹² Because of the need to move forward promptly on these matters, briefs will be due on or before April 11, 2003;¹³ answers or other responses to the briefs will not be entertained.

¹²We caution that the briefs should not address whether any particular entity, in fact, used the Enron trading strategies or engaged in economic withholding and inflated bidding; that issue is not being set for briefing. Rather, the issue being set for briefing is a more narrow one.

¹³All briefs should be filed in Docket No. PA02-2-005.

Docket No. PA02-2-005

- 7 -

The Commission orders:

Any interested person may submit a brief, double-spaced and no more than 30 pages, on the issue identified in the body of this order, on or before April 11, 2003. All briefs should be filed in Docket No. PA02-2-005.

By the Commission.

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Magalie R. Salas,
Secretary.