

STATE OF NEW YORK DEPARTMENT OF PUBLIC SERVICE

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Acting Secretary

August 18, 2003

Honorable Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Room 1-A209
Washington, D.C. 20426

Re: Docket No. EL01-118-000 - Investigation of Terms and
Conditions of Public Utility Market-Based Rate
Authorizations

Dear Secretary Salas:

For filing, please find the Comments of the New York State Public Service Commission in the above-entitled proceeding. Should you have any questions, please feel free to contact me at (518) 473-8178.

Very truly yours,

David G. Drexler
Assistant Counsel

Attachment

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Investigation of Terms)
and Conditions of Public) Docket No. EL01-118-000
Utility Market-Based Rate)
Authorizations)

COMMENTS OF THE NEW YORK STATE PUBLIC SERVICE COMMISSION

Pursuant to the Order Seeking Comments on Proposed Revisions to Market-Based Rate Tariffs and Authorizations (Order) issued June 26, 2003, and the July 9, 2003 Notice in the Federal Register, the New York State Public Service Commission (NYPSC) hereby submits its comments in the above-captioned proceeding.

INTRODUCTION AND SUMMARY

The Federal Energy Regulatory Commission's (FERC or Commission) Order proposes six specific rules relating to transactions and practices that would be prohibited under sellers' market-based rate tariffs and authorizations. These rules indicate that: (1) unit operation and bidding shall comply with applicable market rules and regulations; (2) market manipulation is prohibited; (3) false or misleading communications are prohibited; (4) sellers shall report accurate information used in electric or natural gas price indices; (5) records for the reconstruction of prices shall be retained for three years; and (6) sellers shall not violate applicable codes

and standards of conduct. Sellers found to have engaged in the transactions or behaviors prohibited under these proposed rules 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.

The NYPSC supports the Commission's initiative to identify and address behavior that yields anticompetitive market conditions.¹ We encourage the Commission to look beyond the proposed remedies it has identified and to include tariff provisions permitting: (1) additional remedies for entities that violate the proposed market rules to deter improper behavior and redress the harm done to innocent market participants; (2) public disclosure of bad actors; and, (3) revocation of market-based authority as a final step.

While disgorging unjust profits should be a first step, it will not provide a sufficient deterrent to anticompetitive behavior. After all, if the maximum monetary remedy is to give back the profits attributable to illegal activity, market participants have little to lose by attempting market manipulation. Thus, the Commission should have discretion to

¹ We note that mitigation by the NYISO generally applies on a going-forward basis, while the proposed rules would enable retroactive remedies.

seek further remedies on a case-by-case basis, including disgorgement of all revenues in excess of variable costs or restoring the market to the status quo in extreme circumstance. The Commission should also require that those who violate the rules be publicly identified as an additional deterrent for companies to avoid the stigma associated with public disclosure of their anticompetitive behavior. Public disclosure would also provide notice for purposes of commencing the Commission's proposed 60-day period within which to file a complaint.

More specifically, with respect to the New York market, the Commission should clarify the application of these proposed rules in light of the existing market monitoring and mitigation measures utilized by the New York Independent System Operator (NYISO). In particular, to the extent that a market participant's behavior is explicitly governed by the thresholds contained in the NYISO's mitigation measures, and there is no legitimate business reason for exceeding those thresholds, only then should that behavior be treated as a violation of the proposed rules.

False or misleading communications addressed in Market Behavior Rule No. 3 should include communications concerning the costs necessary to establish reference levels under the NYISO's procedures. Finally, sellers should be bound by the market

manipulation of their affiliates under Market Behavior Rule No. 2.

DISCUSSION

I. Remedies For Violations Should Not Be Limited To Disgorgement Of Unjust Profits

A. Disgorgement Of Profits Is Not Sufficient To Deter Improper Behavior

We share Commissioner Massey's concerns that disgorgement of unjust profits may not be an adequate remedy in all circumstances.² While disgorging profits to prevent unjust enrichment should be an initial step, it is not a sufficient deterrent. Disgorging unjust profits alone places bad actors in no worse position than before they violated their tariffs. In order to be effective, the deterrent must be designed so that a violator is worse off than if they complied. For example, in the Central Maine case, the Commission required the violator to disgorge all revenues in excess of variable costs.³ Similarly,

² See, Commissioner Massey's Concurring Opinion, issued June 26, 2003, in Docket Nos. EL01-118-000 and EL01-118-001.

³ See Central Maine Power Company, 56 FERC ¶61,200, reh'g denied, 57 FERC ¶61,083 (1991) (requesting refunds of all revenues in excess of variable operating and maintenance expenses). The Commission subsequently modified the Central Maine policy to require refunds of the time value of all revenue recovered during the entire period of the violation. See Prior Notice & Filing Requirements Under Part II of the Federal Power Act (Prior Notice), 64 FERC ¶61,139 at 61,979-80 (1993).

in the case of a failure to timely file a market-based rate, the Commission has required refunds reflecting the time value of all revenues collected during the period of the violation plus "all revenues resulting from the difference, if any, between the market-based rate and a cost-justified rate."⁴ In more onerous situations, where the anticompetitive behavior of a seller raises the market clearing price to excessive levels, it could be appropriate for the Commission to have the discretion to fashion a remedy which could restore the status quo to the market.⁵ In other words, in extreme situations the bad actor could be held responsible for restoring the buyers to where they would have been but for the manipulation. Of course, the Commission would need to consider the long term impacts of such remedy on the entity and on the market.

B. Bad Actors Should Be Publicly Identified

We also encourage the Commission to require public disclosure of the names of the sellers who have engaged in anticompetitive behavior. This remedy should effectively deter

⁴ See Prior Notice.

⁵ Coastal Oil & Gas Corp. v. FERC, 782 F.2d 1249, 1253 (5th Cir. 1986) (indicating that appropriate remedies for a violation could include "restor[ing] the status quo ante and prevent[ing] unjust enrichment of the wrongdoer.").

companies because of the stigma and negative publicity associated with engaging in anticompetitive behavior.

A list of bad actors and dates of violations could easily be maintained on an ISO's Web site. Furthermore, this notification would put market participants on notice that mitigation has occurred and would trigger the Commission's proposed periods within which to submit a complaint to the Commission.

II. The Commission Should Clarify How The Proposed Rules Will Apply In Light Of The NYISO's Existing Mitigation Measures

There are several instances where the proposed rules would overlap with the NYISO's existing market monitoring and mitigation measures. For example, Market Behavior Rule No. 1 states that the seller will "bid supply in a manner that complies with the rules and regulations of the applicable power market."⁶ Moreover, Market Behavior Rule No. 2 states that one of the prohibited actions is "withholding available supply from the market."⁷ Because these two rules would govern behavior that

⁶ Order at ¶ 17.

⁷ Order at ¶ 19.

the NYISO's existing mitigation measures already cover,⁸ it is unclear which provision would apply where such overlap exists.

In particular, we seek clarification regarding the application of the proposed rules in instances where a market participant's behavior is also explicitly governed by the numerical thresholds contained in the NYISO's mitigation measures. Where a seller's behavior is within the NYISO's thresholds, we recommend that such behavior not be treated as a violation of the proposed rules. On the other hand, to the extent a seller's behavior exceeds the NYISO's thresholds,⁹ the Commission should consider that behavior to be a potential violation of the proposed rules. Establishing the thresholds as a bright line would meet the Commission's objective of providing

⁸ The NYISO's existing market mitigation measures already define economic withholding as "submitting bids for an Electric Facility that are unjustifiably high so that (i) the Electric Facility is not or will not be dispatched or scheduled, or (ii) the bids will set a market clearing price." The NYISO's mitigation measures also establish specific thresholds for both conduct (how high a bid is) and specific impact (by how much the behaviors affect prices) in determining whether mitigation is warranted. NYISO's Market Administration and Control Area Services Tariff (Services Tariff), Attachment H, at §2.4(a)(2).

⁹ For bids that violate both the conduct and impact thresholds, the NYISO considers whether or not to mitigate those bids. To the extent that a seller's explanation of the reasons for bidding does not indicate to the satisfaction of the NYISO that the conduct in question is consistent with competitive behavior, the NYISO's rules call for the mitigation of that seller. NYISO Services Tariff, Attachment H, at §3.3.

"reasonable bounds within which conditions on market conduct will be implemented, so as not to create unlimited regulatory uncertainty for individual market participants or harm to the marketplace in general."¹⁰ It would also "not impair the Commission's ability to provide remedies for market abuses whose precise form and nature cannot be envisioned today."¹¹

Where the NYISO has mitigated a seller, the Commission should require the NYISO to announce that it has mitigated; state the starting time and duration time of the mitigation; state the name of the seller that was mitigated; and, identify the market in which the offending bid(s) were made. This notification is necessary, given that it would provide the primary vehicle for market participants to become aware that the NYISO has mitigated a seller and that a violation of the rules may have occurred in the past.

III. Market Behavior Rule No. 2 Should Bind Sellers To The Actions Of Their Affiliates

The Order indicates that:

"any party seeking contract reformation or abrogation based on a violation of one or more of the market behavior rules would be required to demonstrate that such a violation had a direct nexus to contract formation and tainted contract formation itself. If a jurisdictional seller enters into a contract without

¹⁰ Order at ¶ 5.

¹¹ Id.

engaging in behavior that violates its tariff with respect to the formation of such contract, we do not intend to entertain contract abrogation complaints predicated on our market behavior rules.”¹²

We request that the Commission clarify that sellers are bound by the actions of their affiliates. To do otherwise would allow sellers to sidestep this rule through gaming by an affiliate. If a seller’s affiliate violates a rule in a way that improperly raises market prices, and the seller enters into long-term contracts that are impacted by the improper prices, then the seller’s contracts would provide an undue benefit and should be governed by this rule just as if the contracts were signed by the affiliate.

IV. Market Behavior Rule No. 3 Should Apply to Reference Levels

Market Behavior Rule No. 3 provides that “[s]eller will provide complete, accurate, and factual information, and not submit false or misleading information, or omit material information, in any communications with the Commission, market monitors, regional transmission organizations, independent system operators, or similar entities.”¹³

We seek clarification that sellers in the New York market would be bound by this tariff provision as it applies to the

¹² Order at ¶ 24.

¹³ Order at ¶ 25.

setting of reference levels. In areas where sufficient competition does not exist (e.g., New York City), reference levels are used by the NYISO as a surrogate for competitive behavior to determine whether mitigation is warranted. Under the NYISO's procedures, sellers routinely provide generating unit cost information to the NYISO to determine an appropriate reference level for a generating unit. If sellers are able to submit false or misleading cost information in order to overstate their reference levels, then excessive prices may result. As such, communications concerning costs used in setting reference levels should be considered as a type of communication covered under Market Behavior Rule No. 3.

CONCLUSION

The Commission should adopt the proposed tariff provisions consistent with the above discussion.

Respectfully submitted,

Dawn Jablonski Ryman
General Counsel

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Dated: August 18, 2003
Albany, New York

CERTIFICATE OF SERVICE

I, Karen Houle, do hereby certify that I will serve on August 18, 2003 the foregoing Comments of the Public Service Commission of the State of New York by depositing a copy thereof, first class postage prepaid, in the United States mail, properly addressed to each of the parties of record, indicated on the official service list compiled by the Secretary in this proceeding.

Date: August 18, 2003
Albany, New York

Karen Houle