

102 FERC ¶ 61, 041
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Communications with Commission-Approved
Market Monitors

Docket No. RT03-1-000

ORDER MODIFYING THE APPLICATION OF RULE 2201
TO COMMUNICATIONS WITH COMMISSION-APPROVED MARKET
MONITORS

(Issued January 16, 2003)

1. The Commission believes that its surveillance of the operation of the energy markets requires open communications with those individuals and companies who serve as market monitors for, or market monitoring units of, Regional Transmission Organizations (RTOs) or System Operators (ISOs)(collectively, market monitors). For that purpose, in this order, the Commission modifies the application of its regulations on off-the-record communications at 18 C.F.R. § 385.2201 (Rule 2201), to treat communications between the Commission and its staff and Commission-approved market monitors as exempt communications not subject to notice and disclosure.¹

¹To date, the Commission has approved market monitors with respect to five RTO's or ISO's. See New York Independent System Operator, Inc., *et al.*, 89 FERC ¶ 61,196 (1999), *order on reh'g*, 90 FERC ¶ 61,317 (2000); New England Power Pool and ISO New England, Inc., 100 FERC ¶ 61,287 (2002), *order on reh'g*, 101 FERC ¶ 61,344 (2002); Midwest Independent Transmission System Operator, Inc., 97 FERC ¶ 61,326 (2001); PJM Interconnection, L.L.C., 86 FERC ¶ 61,247 (1999), *order on reh'g*, 88 FERC ¶ 61,274 (1999); and Pacific Gas and Electric Company, San Diego Gas & Electric Company and Southern California Edison Company, 81 FERC ¶ 61,122 (1997) (California ISO).

I. BACKGROUND

A. Market Monitors

2. Market monitors for RTOs (and certain ISOs) derive from Order No. 2000, where the Commission provided that RTOs must perform a market monitoring function.² Specifically, RTOs are required to: (1) monitor markets for transmission service and the behavior of transmission owners and propose appropriate action; (2) monitor ancillary services and bulk power markets that the RTO operates; (3) periodically assess how behavior in markets operated by others affects RTO operations and how RTO operations affect those markets; and (4) provide reports on market power abuses and market design flaws to the Commission and affected regulatory authorities, including specific recommendations.³ The Commission explained that because it is engaged in finding ways to understand market operations in real-time, so that it can identify and react to any problems that are preventing the most efficient operations, and to protect against anti-competitive effects in electricity markets, market monitoring is an important tool for ensuring that markets within the region covered by an RTO do not result in wholesale transactions or operations that are unduly discriminatory or preferential or provide opportunity for the exercise of undue market power. In addition, the Commission pointed out, market monitoring provides information regarding opportunities for efficiency improvements.⁴

3. To ensure that these objectives are met, the Commission directed market monitors to design monitoring plans to evaluate the behavior of market participants, including transmission owners, if any, in the region to determine whether their behavior adversely affects the ability of the RTO to provide reliable, efficient and nondiscriminatory

²Regional Transmission Organizations, Order No. 2000, FERC Stats. & Regs., [Regulations Preambles July 1996-December 2000] ¶ 31,089 at p. 30,991 (1999), *order on reh'g*, Order No. 2000-A, FERC Stats. & Regs. [Regulation Preambles July 1996-December 2000] ¶ 31,092 (2000), *petitions for review dismissed sub nom. Public Utility District No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

³Order No. 2000 at p. 31,146.

⁴*Id.* at p. 31,155.

transmission service.⁵ Specifically, the monitoring plan should examine the structure of the market, compliance with market rules, behavior of individual market participants and the market as a whole, and market power and market power abuses. The monitoring plan should also address how information will be used and reported, indicating the types and frequency of reports that will be made and to whom the reports will be sent.⁶ Because the Commission has the primary responsibility to ensure that regional wholesale electricity markets served by RTOs operate without market power under the Federal Power Act, 16 U.S.C. §§ 791a-825r, the Commission further directed that an appropriate market monitoring plan must provide an objective basis to observe markets and, if appropriate, provide reports or market analyses. In particular, the Commission directed the market monitors to file reports with the Commission and affected regulatory authorities on opportunities for efficiency improvements, market design flaws, and market power abuses in the markets the RTO operates and administers.⁷

4. Lastly, the Commission emphasized that performance of market monitoring by RTOs is not intended to supplant Commission authority. Rather, it is to provide the Commission with an additional means of identifying opportunities for improvements in market efficiency detecting market power abuses and market design flaws.⁸

B. The SMD NOPR

5. Since the issuance of Order No. 2000 in 1999, the Commission has approved and otherwise overseen the creation of market monitors in existing and proposed RTOs.⁹ The Commission has also expanded upon the need for market monitors, and in particular the need for independent market monitors, in its Notice of Proposed Rulemaking on Remediating Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design (SMD NOPR).¹⁰ There, the Commission proposed

⁵*Id.* at p. 31,106.

⁶*Id.* at p. 31,156.

⁷*Id.*

⁸*Id.* at p. 31,156.

⁹See *supra* note 1.

¹⁰Remediating Undue Discrimination Through Open Access Transmission Service
(continued...)

that as a condition for participating in the spot markets, and using the transmission grid, market participants must agree to provide market monitors with any information requested, reasoning that the ability of the market monitors to perform their monitoring role is dependent upon their ability to acquire the necessary information.¹¹ Market participant objections to such information requests would be resolved by the Commission on an expedited basis because delays in providing information could result in continuing harm to the market. In any such dispute, the Commission would give substantial deference to the market monitors' stated need for the information.¹²

6. At a minimum, under the SMD NOPR, market monitors would be required to submit annual reports to the Commission and the Independent Transmission Providers' governing boards, and share those reports with the Regional State Committees.¹³ The reports would include a general description of the market operations, supply and demand, and market prices, an analysis of market structure and participant behavior, an evaluation of the effectiveness of mitigation measures taken, an overall assessment of market efficiency, an evaluation of barriers to entry for generating, demand-side, and transmission resources, and any recommended changes to market design or market power mitigation measures to improve market performance.¹⁴ In addition, as set out in the SMD NOPR, market monitors would be required to report to the Commission, through the Office of Market Oversight and Investigations, any instances of conduct by market participants that appear to be inconsistent with the Independent Transmission Providers' tariffs.¹⁵ Early reporting of questionable conduct would permit coordination between

¹⁰(...continued)
and Standard Electricity Market Design, IV FERC Stats. & Regs. ¶ 32,563 (2002).

¹¹*Id.* at p. 34,376.

¹²*Id.* The Commission reinforced the importance of the market monitors' ability to obtain necessary information from market participants by also proposing that the Independent Transmission Providers' tariffs must specify the penalties that would apply to market participants who fail to comply with an information request. *Id.*

¹³*Id.*

¹⁴*Id.*

¹⁵*Id.*

market monitors and the Commission's staff to determine the best methods for developing the facts and addressing conduct that could be harmful to the market.¹⁶

7. Although the SMD NOPR as a proposal does not establish Commission policy on the functions of market monitors and their relationship with Commission market oversight staff, it nevertheless indicates the Commission's current views on those functions and relationships. Accordingly, since the issuance of the SMD NOPR in July 2002, Commission orders on the establishment of RTOs have frequently stated that the applicants' proposals inform the Commission on the policies proposed in the NOPR, and the Commission's actions on the applicants' proposals are in turn informed by the policies proposed in the NOPR.¹⁷

C. Rule 2201

8. In Order No. 607, the Commission promulgated its current regulations governing off-the-record communications, and codified them in Rule 2201, also known as the *ex parte* rule.¹⁸ To protect the due process rights of parties in Commission proceedings, Rule 2201 generally prohibits communications between Commission decisional staff and members of the public on the issues in contested on-the-record proceedings.¹⁹ Rule 2201 provides, however, that the Commission may, by rule or order, modify any provision of the rule, as it applies to all or part of a proceeding, to the extent permitted by

¹⁶*Id.* at pp. 34,376-77.

¹⁷*See, e.g.,* Avista Corp., et al. (RTO West), 100 FERC ¶ 61,274 (2002) at p. 3 ("The Commission looks at the proposal for an RTO as both informing and being informed by the proposed rulemaking on standard electricity market design."). *See also id.* at p. 273.

¹⁸Regulations Governing Off-the-Record Communications', Order No. 607 FERC Stats. & Regs. [Regulations Preambles July 1996-December 2000] ¶ 31,079 (1999), *order on reh'g and clarification*, Order No. 607-A, FERC Stats. & Regs. [Regulations Preambles July 1996-December 2000] ¶ 31,112 (2000).

¹⁹See 18 C.F.R. § 385.2201(b). Contested on-the-record proceedings do not include notice and comment rulemakings under 5 U.S.C. § 553, investigations under 18 C.F.R. Part 1b, proceedings not having a party or parties, or any proceeding in which no party disputes any material issue. See 18 C.F.R. § 385.2201(c)(ii).

law.²⁰ In addition, in Rule 2201, the Commission exempted certain types of communications from the coverage of the rule and required most of these exempt communications to be disclosed to the public through a notice published in the *Federal Register*.²¹ Since the issuance of Order No. 607 in 1999, the Commission has modified the application of Rule 2201 once to permit State-Federal RTO Regional Panels to meet without the general public's participation, with the condition that transcripts of those panel meetings be placed in the relevant RTO dockets.²²

II. DISCUSSION

9. The Commission is committed to ensuring the proper and efficient operation of the wholesale energy markets, and, as its actions to date demonstrate, believes that objective can be met in part by the use of market monitors as contemplated by Order No. 2000 and the SMD NOPR. Market monitors assist the Commission by being in the market and collecting and analyzing relevant data and reporting data analyses, conclusions, and recommendations back to the Commission. Timely receipt of those reports is critical to the Commission's ability to respond and thus avoid unnecessary costs that delay could cause. In these efforts, however, market monitors may encounter situations or matters that are also at issue in ongoing contested on-the-record proceedings at the Commission. While they may rightly need to bring such situations or matters promptly to the Commission's attention, or to discuss them with Commission staff, market monitors are currently prohibited from doing that off-the-record under Rule 2201.

²⁰See 18 C.F.R. § 385.2201(a).

²¹See 18 C.F.R. §§ 385.2201(e)-(h). Where applicable, the disclosure and notice procedure works as follows. Any decisional employee who makes or receives a prohibited or an exempt off-the-record communication is obligated promptly to deliver to the Office of the Secretary (OSEC) a copy of the communication, if written, or a summary of the substance of any oral communication. Next, OSEC places the written communication or summary of an oral communication in the non-decisional file (if a prohibited communication) or in the decisional file (if an exempt communication). Every 14 days, or more frequently, OSEC publishes a notice in the Federal Register identifying exempt and prohibited communications. Parties then have an opportunity to respond to the communications.

²²See 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 nom. Exelon Corp., et al. v. FERC*, No. 02-1154 (D.C. Cir. Sept. 20, 2002).

The reason is, as noted, Rule 2201 prohibits any communication on the merits of any issue in contested proceedings between decisional Commission staff members and any person outside the Commission.²³ The Commission believes that the application of Rule 2201 in these circumstances is counterproductive, and may be impeding its goal to receive as much timely information as possible from market monitors on the operation of the energy markets. Accordingly, as explained below, the Commission is modifying the application of Rule 2201 as that rule applies to certain communications between Commission-approved market monitors and the Commission and its staff, and will treat such communications as exempt communications not subject to disclosure or notice.

10. As an initial matter, the Commission believes that any modification of the application of Rule 2201 to communications with Commission-approved market monitors will not frustrate the purpose behind that rule, *viz.*, that parties in contested on-the-record proceedings receive due process by having access to the information that the Commission's decisional staff and the ultimate decision makers receive in the proceedings from persons outside the agency. To be sure, market monitors are "persons outside the agency"; indeed, they are not employed by the agency but are typically compensated by the operators of the transmission systems. Nevertheless, they serve an important practical and unique function as the Commission's "eyes and ears" in the marketplace, and are 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. Market monitors stand apart from the interests of any market participant and even the RTO or ISO, as the market operator, and must objectively monitor those participants as well as the performance of the RTO or ISO itself and its market rules. In this sense, they are practically an extension of, or a surrogate for, the Commission's own market monitoring and investigative staff. Accordingly, just as those Commission staff members may talk to each another, there should generally be no prohibition on market monitors' talking to the Commission and its staff about the results of their market monitoring.

²³The primary staff with whom market monitors communicate are members of the Office of Market Oversight and Investigations. Commission staff in that office are generally considered to be decisional employees, even though they may not draft orders or opinions, because they participate in the decisional process, and do not fall under the explicit definition of non-decisional employee in Rule 2201. See 18 C.F.R. § 385.2201(b)(3). See also Statement of Administrative Policy on Separation of Functions, 101 FERC ¶ 61,340, mimeo at pp. 27-30 (2002).

11. The Commission recognizes that parties in a contested on-the-record proceeding could be prejudiced by a market monitor's talking freely to the Commission and its staff regarding issues in the proceeding if the market monitor was a party or appeared on behalf of a party. Such communications could undermine the integrity of the decision making process by giving one party an advantage over another party in the proceeding. Therefore, the exemption created here by modifying the application of Rule 2201 to communications with Commission-approved market monitors will not apply to communications between a market monitor and the Commission and its staff regarding issues in a particular contested on-the-record proceeding if the market monitor is a party or appears on behalf of a party in that proceeding.²⁴

12. Furthermore, the Commission believes that the goal of facilitating the timely receipt of important market information by treating communications with Commission-approved market monitors as exempt communications would be frustrated by requiring those communications to be subject to notice and disclosure under 18 C.F.R. § 385.2201(f) and (h). Again, the Commission views market monitors, in practice, as extensions of its own staff who are not required to disclose their findings by placing them in the record of a proceeding. For this reason, the Commission will not require its staff to record exempt communications with market monitors for disclosure and publication in the *Federal Register*.²⁵

13. As a final matter, the Commission emphasizes that the exemption created here may not be used by Commission-approved market monitors as a conduit for prohibited off-the-record communications from others outside the agency. In other words, market monitors may not convey to the Commission's decisional staff comments and arguments of others outside the agency regarding the issues in contested on-the-record proceedings, and likewise may not divulge to others outside the agency the discussions about such issues they have had with Commission staff. In addition, this exemption, like any exemption from the *ex parte* rule, is a permission not a requirement. It allows, but does not require, market monitors and the Commission and its staff to have less fettered communications than otherwise permitted under Rule 2201. Nevertheless, the

²⁴This would not be the case if a market monitor did not seek party status, but rather sought, or was asked by the Commission, to participate as an amicus in a proceeding. Such participation could enhance the decision making process by ensuring that relevant information from the market monitor was part of the decisional record.

²⁵The Commission is, of course, acutely aware of the requirement under Section 706 of the Administrative Procedure Act that it may only rely on evidence in the record in reaching its ultimate decision in a proceeding.

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Commission believes that such communications will enhance its staff's ability to bring important market information to the Commission's attention in a timely way, and thus improve the Commission's ability to ensure a well-functioning energy market.

The Commission orders:

The application of Rule 2201 is hereby modified, as described in this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.