

**UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION
104 FERC ¶ 63,010**

**Enron Power Marketing, Inc.
Enron Capital and Trade Resources Corporation**

Docket No. EL02-113-000

INITIAL DECISION

(Issued July 15, 2003)

APPEARANCES

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Erik Saltmarsh, Esq., on behalf of California Electricity Oversight Board

Amy W. Beizer, Esq., Philip Chabot, Esq., and John S. Jenkins, Jr., Esq., on behalf of the City of Tacoma, Washington

Paul M. Breakman, Esq., Gregg D. Ottinger, Esq., and John Stickman, Esq., on behalf of the City of Burbank, California

Todd O. Edmister, Esq., Arocles Aguilar, Esq., and Sean Gallagher, Esq., on behalf of State of California Public Utilities

Julie M. Moore, Esq., on behalf of California Independent System Operator

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James H. McGrew, Esq., on behalf of California Power Exchange Corporation

Michael J. Wentworth, Esq., and Mark L. Perlis, Esq., on behalf of Duke Energy Trading and Marketing

Stephen Angle, Esq. on behalf of TransAlta Energy Marketing, U.S., Inc., and TransAlta Energy Marketing, California, Inc.

Andrea M. Settanni, Esq. and Paul W. Fox, Esq. on behalf of Powerex Corporation

Lawrence Acker, Esq. on behalf of Idacorp Energy LP

Joel M. Cockrell, Esq. and Daniel R. Simon, Esq. on behalf of Federal Energy Regulatory Commission Staff

Carmen A. Cintron, Presiding Administrative Law Judge

I. INTRODUCTION

1. This proceeding examines the business relationship between El Paso Electric Company (“El Paso”) and two Enron subsidiaries: Enron Capital and Trade Resources (“ECT”) (currently d/b/a Enron North America) and its subsidiary Enron Power Marketing, Inc. (“EPMI”) (sometimes jointly as “Enron”).

II. BACKGROUND

2. On August 13, 2002, under Section 206 of the Federal Power Act (“FPA”), 16 U.S.C. § 824e, the Commission ordered a hearing to investigate whether Enron and El Paso should have made certain filings pursuant to Section 203 and/or 205 of the FPA. This was based on the finding that these entities had entered into a contractual relationship which may have resulted in Enron acquiring control of El Paso’s assets without prior Commission approval.¹

3. The Chief Administrative Law Judge, by order issued August 23, 2002, designated the Presiding Judge.² Several parties sought, and were granted, intervenor status in this

¹ *El Paso Electric Company*, 100 FERC ¶ 61,188 at p. 9-10 (2002).

² “Order of Chief Judge Designating Presiding Administrative Law Judge,” (August 23, 2002).

proceeding.³ The Presiding Judge established a procedural schedule.⁴ By order dated March 27, 2003, issues were established (the parties failed to reach unanimity on the exact language of issues). Testimony was filed by Trial Staff (“Staff”), Enron, El Paso, the California Parties, and Tacoma. The hearing was held on April 1 and 2, 2003.

4. During the hearing, the Presiding Judge requested that Staff witness Barlow present further evidence. Tr. 362-364, 369-370. Additional testimony was submitted by Staff. The California Parties and Enron both responded to the post-hearing exhibit, followed by Staff’s reply.

5. On April 24, 2003, Enron filed a motion seeking additional cross-examination of Staff witness Barlow and California Parties’ witness Merola, offering to provide their witness Kee for cross-examination.⁵ This motion was granted.⁶ Subsequently, the parties waived cross-examination of Merola. On May 5, 2003, Enron filed a motion to substitute a new witness, Beck, for Kee. According to Enron, Kee was unavailable. Enron submitted an exhibit from Beck adopting Kee's post-hearing testimony.

6. At the May 7 hearing, the record was closed without additional cross-examination with the admission of the following exhibits: S-50, 51, CAL-11, and EPMI-8. It was

³ The City of Tacoma, Washington (“Tacoma”) was granted intervention in an Order Granting Motion for Leave to Intervene issued September 30, 2002. In another Order issued on October 10, 2002, the following were allowed to intervene: (1) The California Electricity Oversight Board and (2) the People of the State of California, *Ex. Rel.* Bill Lockyer, Attorney General (collectively “the California Parties”), (3) the California Independent System Operator Corporation (“CAISO”), (4) Pacific Gas and Electric Company, (5) Dynergy Power Marketing, Inc., (6) Californians for Renewable Energy, Inc., and (7) Pioneer America LLC. In an Order Granting Motion to Intervene, issued on October 18, 2002, the City of Burbank, California (“Burbank”) was allowed to intervene. Finally, the Public Utility District No. 1 of Snohomish County, Washington, (“Snohomish”) was allowed to intervene by Order issued December 17, 2002.

⁴ “Order Establishing Procedural Schedule,” (September 7, 2002).

⁵ “Motion to Allow Cross-Examination of Randolph A. Barlow, Edward Kee and Jeffrey D. Merola as to Newly Filed Evidence,” filed on April 24, 2003.

⁶ “Order Scheduling Supplemental Hearing,” (April 30, 2003).

ruled that Enron had waited too late to substitute Beck, and had thereby waived its right to further cross-examination. Initial Briefs were filed on May 14, 2003, by Enron, the California Parties, El Paso, and Staff. Reply Briefs were filed on June 4, 2003, by all the parties previously listed and Tacoma.⁷

III. ISSUES

Issue A. Did Enron violate Sections 205 and 206 of the Federal Power Act by not filing the Power Consulting Services Agreement (PCSA) with the Federal Energy Regulatory Commission? If a violation is found, what is the appropriate remedy?

A. Arguments of the Parties and Staff:

7. Staff asserts that Enron violated FPA Section 205(c) by not filing a Power Consulting Services Agreement (“PCSA”) between Enron and El Paso with the Commission. Staff I.B. at p. 20 and S-2. According to Staff, the FPA requires public utilities to file jurisdictional service contracts. Staff I.B. at p. 20. Under the PCSA, Staff insists, Enron was performing jurisdictional services (operating a power marketing desk and buying and selling wholesale electricity) for El Paso without prior Commission approval. *Id.*

8. Additionally, Staff contends that Enron gained control and operated El Paso’s jurisdictional assets. *Id.* In performing under the PCSA, Staff insists, Enron controlled and operated El Paso’s marketing division, which was a competing public utility, and, by gaining such control, Enron effectively lost its status as a power marketer. *Id.* Consequently, Staff maintains, the FPA required Enron “to file the agreement, explain how it would work, and obtain the Commission’s blessing before performing under it.” *Id.*

9. As Enron provided real-time and prescheduling functions for El Paso, Staff notes, Enron gained the type of control and decisionmaking authority that the Commission has

⁷ On April 4, 2003, El Paso, the California Parties, and Staff filed a “Combined Offer of Settlement in Resolution of Section 206 Proceeding as to El Paso Electric Company.” On May 6, 2003, El Paso filed a Motion to Sever El Paso from this proceeding. This motion was granted by the Chief Administrative Law Judge on May 23, 2003. El Paso’s settlement was docketed as EL02-113-002. The settlement was certified to the Commission on May 28, 2003. “Certification of Uncontested Settlement,” (May 28, 2003).

determined would constitute jurisdictional activity requiring Commission approval. *Id.* at p. 24. Furthermore, Staff asserts, Enron controlled and directed El Paso's generators. *Id.* at p. 26. Staff notes that Enron did not present any factual evidence in its testimony regarding the scope of its responsibilities under the PCSA. *Id.* at p. 28.

10. Despite Enron's contention that the PCSA contract language called for EPMI to perform non-jurisdictional services, Staff insists, Enron actually did provide jurisdictional services. Staff R.B. at p. 6. Also, Staff explains, even contracts providing non-jurisdictional services must be filed if the contract satisfies FPA Section 205(c) requirements. *Id.* Finally, Staff accuses Enron of misrepresenting the PCSA, as it did contemplate providing jurisdictional services. *Id.* at p. 7.

11. Staff argues that Enron's theory that it was not subject to FPA Section 205(c) because it acted as a broker for El Paso is unsound. Staff I.B. at p. 28. Such an argument, Staff insists, is completely unsupported by the record evidence or any testimony. *Id.* at p. 29. Staff points out that El Paso admitted that Enron, by virtue of the PCSA, ordered El Paso to sell energy to Enron, thereby taking title to the energy. *Id.*

12. Additionally, Staff notes that Enron and El Paso shared profits for supplemental market sales and ancillary services made to the CAISO. Staff I.B. at p. 29 and Ex. No. S-9 at 4, ¶ 13(a). Staff asserts that no broker owns a direct financial interest in profits obtained through its transactions. *Id.* at p. 29. Enron, Staff maintains, simply could not and did not act as a broker. *Id.* at p. 30. Finally, Staff explains that a traditional broker role is easy to identify because of the clear-cut nature of the behavior. *Id.* Here, Staff continues, Enron's behavior was extremely convoluted. *Id.* Enron, Staff also notes, does not point to any PCSA language contemplating Enron's activities or behavior as a broker for El Paso. Staff R.B. at p. 8.

13. As for Enron's argument that the PCSA did not need to be filed because it is an umbrella services agreement within the scope of its market based rate tariff, and the Commission had waived the requirement that such contracts be filed, Staff disagrees. *Id.* at p. 10. Staff asserts that the PCSA was an entirely new type of jurisdictional service completely outside the scope of Enron's market based rate tariff, which had to be filed with the Commission. *Id.* According to Staff, the EPMI market based rate tariff only authorized EPMI to sell electricity at wholesale on its own behalf at market rates, not to conduct transactions for other public utilities. *Id.* at p. 11.

14. Staff also argues that, contrary to Enron's assertions, Enron did take title to power it sold on El Paso's behalf. *Id.* at p. 13.

First, the record includes excerpts from the deposition of Pedro Serrano, Jr., who served as head of EPE's marketing division when Enron executed and was performing under the PCSA. Mr. Serrano made it abundantly clear that Enron sometimes took title to the power. He also made clear that it was incredibly difficult, due to the way Enron and EPE established their business relationship, to determine the exact transactions to which Enron took title. Second, Trial Staff sponsored a data response from EPE explaining that Enron sometimes took title to power it purchased from EPE while operating EPE's real-time marketing function. Third, EPE stipulated to this fact. . . . Fourth, Staff witness Segal testified that Enron sometimes engaged in self-dealing, and discussed all of these exhibits in her testimony.

Id. at p. 14 (internal citations omitted). Enron, Staff notes, does not provide evidence disputing these facts. *Id.* at p. 15.

15. Staff asserts that the Commission has determined that the appropriate remedy for failing to file market based rate operation and maintenance types of service agreements is that the party may receive no more than its variable operation and maintenance expenses from the date of commencement of service until the date the Commission accepts such rates for filing. Staff I.B. at p. 31. However, as Staff lacked specific variable operation and maintenance expense information, Staff instead computed Enron's profits. *Id.* Staff recommends that Enron refund the \$45,754,064 earned from EPMI's transactions arising from the PCSA. *Id.* According to Staff, Enron North America and EPMI are jointly and severally liable for the refund as ECT signed the contract and Enron North America is the corporate successor to ECT. *Id.*

16. The California Parties argue, along the lines of Staff, that the PCSA fell within the Section 205(c) filing requirement because the services Enron provided under this agreement, affected or related to jurisdictional sales under this section of the FPA. California I.B. at p. 6. Enron's failure to file, the California Parties contend, violated the FPA. *Id.*

17. In return for fees, the California Parties explain, Enron operated El Paso's real-time marketing desk during off-business hours. *Id.* at p. 7. They point out that El Paso so stipulates and the PCSA itself clearly provides. *Id.* The Section 205(c) filing requirement, the California Parties assert, consistently has been interpreted broadly, assuring that the Commission can effectively regulate jurisdictional activities. *Id.* at p. 8.

According to the California Parties, the case law⁸ interpreting Section 205(c) gives the Commission authority to require the filing of contracts for certain services. *Id.* Furthermore, the California Parties argue, the Commission continues to insist that contracts affecting or relating to jurisdictional services must be filed. *Id.* at p. 9. The California Parties note that a recent Commission decision addressing the brokering exemption completely undercuts Enron's brokering argument.⁹ California R.B. at p. 4.

18. Although Enron had a contract filing requirement waiver because of its status as a power marketer, the California Parties maintain, the waiver did not apply to the PCSA because Enron's services went beyond the arm's-length wholesale power sale transactions' scope envisioned by the Commission in granting the waiver. *Id.* at p. 6. The California Parties accuse Enron of abusing its power marketer status by intentionally depriving the Commission of information regarding its relationship with El Paso. *Id.* at p. 6.

19. At the time the PCSA was executed, the California Parties relate, power marketers were granted waivers of contract filing obligations for short-term power sales transactions (one year or less) and long-term power sales transactions (greater than a year).¹⁰ *Id.* at pp. 10-11. However, the California Parties note, the Commission ordered power marketers to file detailed purchase and sales quarterly transaction reports. *Id.* at p. 11.

20. Upon Enron's waiver request, and envisioning that Enron would purchase power from multiple sources to resell the power in various products, the Commission granted Enron's request.¹¹ *Id.* at pp. 12-13. Nevertheless, the California Parties maintain, the Commission did not waive the FPA Section 205(c) filing requirement for contracts such as the PCSA because "the PCSA gave Enron extensive control over the facilities and

⁸ *Prior Notice and Filing Requirements Under Part II of the Federal Power Act*, 64 FERC ¶ 61,139 (1993) and *Northern Natural Gas Company v. FERC*, 929 F.2d 1261 (8th Cir.), cert. denied, 112 S.Ct. 169 (1991).

⁹ *D.E. Shaw Plasma Power L.L.C.*, 102 FERC ¶61,265 (2003).

¹⁰ The California Parties aver the Commission prospectively rescinded previously-granted waivers of the requirement for power marketers to file long-term service agreements. *Southern Co. Services, Inc., et al.*, 87 FERC ¶ 61,214 at 61,849 (1999).

¹¹ *See Enron Power Marketing, Inc.*, 65 FERC ¶ 61,305 (1993) order on rehearing, 66 FERC ¶ 61,244 (1994).

sales activities of a public utility that had its own franchise territory [and] . . . [t]he PCSA did not relate to particular purchases or sales. Rather, it covered an overall relationship with a single entity.” *Id.* at p. 13. Concluding, the California Parties assert that the PCSA was a completely different creature than that envisioned by the Commission in granting Enron’s waiver request. *Id.*

21. Finally, the California Parties recommend that Enron disgorge all profits made under its market based rate authority from 1997 through 2001 as well as surrender its market based rate authority. California I.B. at pp. 6-14.

22. Enron responds that the PCSA did not need to be filed because the actions arising from it were non-jurisdictional. Enron I.B. at p. 7. The brokering services where Enron did not take title to energy as well as other services not involving the actual sale or transmission of energy in interstate commerce, Enron maintains, are non-jurisdictional. *Id.* at p. 8. Enron contends that it was merely brokering transactions and that brokering is exempt from the FPA Section 205(c) filing requirement. *Id.*

23. The PCSA does not provide that EPMI will take title to the energy, Enron explains, and, therefore, the PCSA does not need to be filed as a power sales contract under FPA Section 205(c). *Id.* at p.10.

24. Also, Enron responds that it was specifically exempted from filing the PCSA. *Id.* at p. 9. Enron argues that the Commission has modified its requirements so that power marketers are exempt from filing power sales contracts or contracts related to them, and this exemption existed at the time the PCSA was signed. Enron R.B. at p. 7. Enron contends that the Commission has exempted power marketers without generation from filing contracts, but, instead, requires the power marketers to file quarterly reports. *Id.* The Commission, Enron insists, granted it such a waiver imposing the same requirements as developed in the *Citizens Power & Light Company* decision. *Id.*

25. Furthermore, Enron argues that the Commission intended to modify this waiver by requiring power marketers to file long-term service agreements, however, Enron continues, the Commission suspended that order.¹² *Id.* at p. 8. Consequently, Enron states, the waiver continues to remain in effect. *Id.* at p. 9.

¹² *Revised Public Utility Filing Requirements*, Order No. 2001, 67 Fed. Reg. 31,043 (May 8, 2002), FERC Stats. & Regs. ¶ 31,127 at P 5, Table 1, n. 1, *reh'g denied*, Order No. 2001-A, 100 FERC ¶ 61,074, *reconsideration and clarification denied*, Order No. 2001-B, 100 FERC ¶ 61,342, Order No. 2001-C, 101 FERC ¶ 61,314 (2002), and Order No. 2001-D, 102 FERC ¶ 61,334 (2003).

26. Even if the PCSA is considered a power sales contract falling within FPA Section 205(c), Enron insists, it is nonetheless an umbrella service agreement contemplating sales. Enron I.B. at p. 9. Consequently, Enron explains, power marketers are not required to file umbrella agreements,¹³ and instead must file only their tariff and quarterly reports. *Id.* Enron states both conditions have been satisfied. *Id.*
27. Enron argues that the Commission ultimately codified the waiver by adding a new section to subpart A of Part 35.

For purposes of paragraph (a) of this section, any agreement that conforms to the form of service agreement that is part of the public utility's approved tariff pursuant to § 35.10(a) of this chapter and any market-based rate agreement pursuant to a tariff shall not be filed with the Commission.

Enron R.B. at p. 10 and 18 C.F.R. § 35.1(g) (2003) and see 67 Fed. Reg. 31,069 (May 8, 2002). Concluding, Enron asserts that if the PCSA was a power sales agreement, then it was specifically exempt from filing the PCSA; however, if the PCSA was not a power sales agreement, then there was no Section 205(c) filing requirement. Enron R.B. at p. 11.

28. The transactions entered into under the PCSA, Enron believes, were fully sanctioned by the Commission,¹⁴ allowing EPMI to “sell power anywhere, at any time, through any arrangement and subject to any rate.” *Id.* at p. 12. Enron insists that nowhere is a power marketer prohibited from selling power on behalf of third parties, which is how Enron characterizes its behavior under the PCSA. *Id.* Finally, Enron argues that even if the PCSA should have been filed, the only available remedy is prospective refunds. Enron I.B. at p. 7.

B. Discussion:

29. Section 205(c) of the FPA provides in pertinent part:

¹³*Power Company of America v. FERC*, 245 F.3d 839, 845 (2001).

¹⁴*Enron Power Marketing, Inc.*, 65 FERC ¶ 61,305 (1993).

(c) every public utility shall file with the Commission, . . . schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classification, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

16 U.S.C. § 824d.

30. The Commission has required the filing of rates, charges, and all contracts and agreements related to jurisdictional service sixty days in advance of the commencement of the jurisdictional service. *Prior Notice and Filing Requirements Under Part II of the Federal Power Act*, 64 FERC ¶ 61,139 (1993). In the cited case, the Commission clarified the filing obligations of public utilities under the FPA “to balance respect for the statutory requirement of prior notice and filing with the market realities of the public utilities.” *Id.* at 61,972. Among other matters, the Commission explained that it has “considerable flexibility in determining what rates and practices are ‘for or in connection with,’ or ‘affecting,’ or ‘pertaining’ or ‘relat[ing] to’ jurisdictional service and, accordingly must be filed for Commission review.” *Id.* at 61,987. The Commission cited *Northern Natural Gas Company v. FERC*, 929 F.2d 1261 (8th Cir.), *cert denied*, 112 S. Ct. 169 (1991), for the proposition that the Commission has authority “to require the filing of rates for certain services, even when the physical act of providing the services is not jurisdictional, when the rates are ‘in connection with’ the provision of jurisdictional service.” *Prior Notice, supra* at 61,987.

31. The evidence in this case demonstrates that ECT and El Paso entered into the PCSA on January 16, 1997. Ex. S-2 at 1. Section 1.1 of the PCSA states that ECT shall be a consultant for El Paso to advise El Paso with respect to certain aspects of its wholesale and retail power supply obligations, as described in Appendix A. *Id.* Appendix A to the PCSA is significant. It establishes, among other things, the type of information El Paso will provide ECT and operating guidelines during normal business hours. *Id.* Significantly, Appendix A establishes that for non-business hours (3:00 pm-7:00 am MST) ECT “may make real time changes to energy schedules.” *Id.* El Paso dispatchers could “deny or alter the real time decision to the extent system reliability or integrity is threatened.” *Id.* Additionally, during non-business hours, El Paso’s power supply group “will forward all relevant phone lines to ECT’s twenty four hour trading operation.” Ex. No. S-2 at 9.

32. In practice, EPMI performed the services under the PCSA. Staff I.B. at p. 7. EPMI and El Paso were competitors during the time frame at issue in this proceeding.

33. The record in this case supports the finding that Enron violated Section 205 of the FPA, since it did not file the PCSA with the Commission.¹⁵ It is clear that the PSCA was a contract which related to or affected the rates, charges, and classifications of jurisdictional services. The PCSA not only impacted the relationship between El Paso and Enron, but also other parties who dealt with these two utilities during the time the contract was in effect. Under the PCSA, during non-business hours, Enron marketed El Paso's power. Enron operated El Paso's power marketing desk, buying and selling wholesale electricity (jurisdictional services), without notifying the Commission or obtaining its approval.¹⁶ Contrary to Enron's claims, this was not just a consulting agreement; consequently, under Section 205 of the FPA, it had to be approved by the Commission. Moreover, contrary to what Enron claims, the PSCA was not an agreement for brokering services.

34. Under the PCSA, Enron received a monthly payment and valuable information in exchange for operating El Paso's real-time marketing function during off-business hours. Ex. S-1 at 21. According to Staff witness Deters, operation of the real-time marketing function during off-business hours, involved the wholesale sale of electricity. *Id.* Since the inception of the PCSA, El Paso and Enron were competitors. Ex. S-9 at 2. Enron, while operating El Paso's real-time desk, would sometimes sell power to itself. The PCSA provided that Enron would be paid a combination of fixed fees and profit sharing based on cost savings to El Paso. Ex. S-2 at 1-3. On July 31, 1997, the parties entered into a First Amendment to the PCSA which provided for \$15,000 per month compensation for Enron.

35. Additionally, from July 1999 until March 2001, Enron was El Paso's scheduling coordinator for selling power into the California Power Exchange ("Cal PX") and the California Independent System Operator ("CAISO"). Exs. S-2 at 12-21; S-9 at 4. El Paso paid Enron 25 cents per MWh for all Cal PX day-ahead sales it made. Ex. S-9 at 4. El Paso also paid Enron 25 cents per MWh for all third-party schedules and a percentage

¹⁵ The findings of fact in this case are applicable solely to Enron since, as discussed above, El Paso entered into a settlement agreement with the California Parties and Staff.

¹⁶ Jurisdictional assets under the FPA include public utilities' corporate organization, contracts, accounts, memoranda, papers and other records, utilized in connection with wholesale sales of electricity. *Citizens Energy Corp.*, 35 FERC ¶ 61,198 (1986); *Hartford Electric Light Company v. FPC*, 131 F.2d 953 (2d Cir.), cert. denied, 319 U.S. 741 (1942).

of margins from supplemental sales and the sale of ancillary services arranged by Enron, from July to December 2001. *Id.*

36. El Paso provided Enron with information about its generation and transmission systems. This included load information (projected and real-time), unit heat rate curves, unit ramp rates and start-up costs, minimum unit operating requirements, Four Corners and Palo Verde operating agreements, unit outage schedules, Four Corners and Palo Verde marginal costs, and El Paso's operating guidelines for complying with Order No. 888. Ex. S-9 at 4. Staff is correct that this information is sensitive, competitive information. Consequently, the PCSA allowed Enron to gain knowledge of El Paso's operations, enabling Enron to gain a competitive advantage over El Paso.

37. Enron operated El Paso's real-time trading desk from 3 p.m. to 7 a.m. (24 hours on weekends and holidays) and entered into day-ahead wholesale electricity contracts on El Paso's behalf. Ex. S-9 at 1, ¶ 3.c. El Paso gave Enron discretion on purchasing matters while Enron was running the El Paso trading desk, thus Enron could decide from whom, how and when Enron could buy or sell power on El Paso's behalf. Ex. S-9 at 3, ¶ 12.b. Additionally, during the time it manned El Paso's trading desk, Enron gave dispatch instructions for El Paso's generation. Ex. S-1 at 22:1-3. Staff correctly points out that the PCSA clearly affected or related to jurisdictional rates or services. Moreover, EPMI was a public utility in accordance with the FPA. Again as Staff correctly points out, EPMI was required to file the PCSA and obtain Commission approval before performing services under the PCSA.

38. In *Illinois Power Co.*, 102 FERC ¶ 61,184, at 61,506, the Commission found that the service provider was required to file a Service Agreement under Section 205 of the FPA. In so holding the Commission re-stated the two part test for determining whether operation and maintenance ("O&M") agreements must be filed with the Commission. Citing *Prior Notice, supra*, (1) the O&M service at issue must be tied to wholesale sales or to transmission in interstate commerce (does the O&M agreement contain rates or charges for or in connection with transmission or sales for resale in interstate commerce, or does it in any manner affect or relate to jurisdictional rates or services); (2) does a public utility provide the O&M service. Under this precedent, the PCSA had to be filed with the Commission and approval for the services needed to be obtained before initiation of the service. The PCSA involved wholesale sales and was being provided by a public utility. As Staff correctly points out, Enron ran El Paso's real-time trading desk during certain hours executing day-ahead wholesale electricity contracts on El Paso's behalf. This affected or related to jurisdictional rates or services.

39. Moreover, Staff is correct that Enron exerted "effective control" over El Paso's facilities. For instance, it was Enron who decided whether to execute a wholesale electric

transaction, with whom, and at what price. Thus, Enron gained control and operated El Paso's assets. In *Prior Notice, supra* at 61, 993, the Commission stated, "[t]he answer to the second question depends on who 'owns' or 'operates' a facility, and requires a specific analysis in each case. 'Ownership' depends on the law. Defining an 'operator' turns on which entity keeps control and decision making authority over major matters. If (i) the entity performing the O&M service under the agreement at issue owns the facility or operates it by virtue of its 'control and decision making authority;' and (ii) the O&M service it performs is related to jurisdictional service, then it must file the O&M agreement for Commission review."

40. In the instant case, Enron provided "power scheduling" services for El Paso under the PCSA. The Commission has rejected a request by a power marketer to receive "scheduling services" from its affiliated public utility which were to be used by the power marketer to deliver power. *UtiliCorp. United Inc.*, 75 FERC ¶ 61,168 at 61,557 (1996). See also, *Automated Power Exchange, Inc.*, 82 FERC ¶ 61,287 at 62,107-08, *reh'g denied*, 84 FERC ¶ 61,020 (1998), *aff'd sub.nom.*, *Automated Power Exchange, Inc. v. FERC*, 204 F.3d 1144 (D.C. Cir. 2000) (Commission asserted jurisdiction over the Automated Power Exchange, since it helps effectuate wholesale sales, and exercises effective control over facilities used for the sale of electric energy for resale in interstate commerce).

41. Analysis of the evidence in this case, in light of Commission precedent, supports Staff's arguments that Enron, in its real-time and prescheduling functions, gained control of decision making authority over sales or transmission of electric energy. Enron, in fact, operated El Paso's jurisdictional facilities (El Paso's power marketing division and its contracts, i.e. purchases and sales of wholesale electricity). Enron conducted power schedules for real-time operations and day-ahead preschedules. Enron manned El Paso's real-time trading desk 76% of the time; 16 hours per day during the work week and 24 hours per day on holidays and weekends. Exs. EPE-1 at p. 19; S-1 at p. 13. Enron was responsible for monitoring and performing real-time marketing on El Paso's behalf 76% of the time. Ex. S-1 at p. 13. Enron set the price and, as long as operational and reliability criteria was met, El Paso could not rescind the transaction. *Id.* The evidence in this case does not establish any instances of any transaction being rescinded. El Paso admitted that it gave Enron discretion on how, when, and to whom it could buy and/or sell power on El Paso's behalf while Enron ran the El Paso trading desk. Ex. S-9 at p. 3 ¶

12(a).¹⁷ Enron's own memorandum supports the fact that it controlled El Paso. Ex. S-34 at p. 3. This relationship lasted for five years. *Id.*

42. In the prescheduled market (day-ahead), the volumes and acceptable prices (minimum, not ceiling) were given to Enron, who purchased/sold the power in the market.¹⁸ Enron had similar authority for El Paso sales to the CAISO's supplemental and ancillary services markets. Exs. S-5 at p. 25; S-9 at p. 3 ¶ 12(a); S-32 at p. 3. The prescheduling function required Enron sometimes to perform "scheduling of the physical power." Ex. S-5 at p. 28. Enron had authority to determine the timing and quantity of bids into the PX and CAISO's, subject to reliability parameters. Ex. S-9 at p. 3 ¶ 12(a). El Paso allowed Enron to dispose of the output of certain generation assets, without prior Commission approval. Ex. S-9 at p. 3 ¶ 11(a).

43. In addition, *D.E. Shaw Plasma Power, L.L.C.*, 102 FERC ¶ 61,265 (2003) provides ample support for the proposition that Enron violated Section 205 of the FPA by not filing the PCSA with the Commission. In *D.E. Shaw*, the Commission asserted jurisdiction over DESCO LP, an investment advisor. The Commission stated that DESCO LP was a public utility due to its potential involvement in wholesale power sales transactions.

The demarcation of functions, responsibilities and decision-making between DESCO LP and Plasma Power (Plasma Trading and Plasma Portfolio) is at best unclear and appears to provide both entities the ability to engage in wholesale power transactions. Plasma Power will enter into wholesale contracts on the recommendation of DESCO LP. . . . More significantly, however, although Plasma Power claims that DESCO LP's activities will be carried out on an agency basis only (on behalf of Plasma Power), the IA Agreement submitted with the Petition authorizes DESCO LP to undertake, as DESCO LP determines in its sole discretion, all investment activities (which include sales of electric products) and to execute contracts.

Id. at 61,825.

¹⁷ This was for real time markets at Palo Verde, Four Corners, and southern New Mexico, subject to operating and reliability parameters provided to Enron on a daily basis. Ex. S-9.

¹⁸ Concerning forward markets, the power amounts and pricing were developed between Enron and El Paso. Ex. S-5 at p. 25.

44. Additionally, in the cited case it was held:

The Commission fails to see how the combination of : (1) the sole discretion to be afforded to DESCO LP to enter into contracts; (2) the exclusive ownership by DESCO LP of the intellectual property on which contracts will be based; and (3) the intention that DESCO LP will recommend the contracts that Plasma Power enters into, does not translate into control by DESCO LP over wholesale contracts to be executed under Plasma Power's market-based rate tariff. Absent a clear demarcation of functions and authorities between DESCO LP and Plasma Power that establish that DESCO LP is acting in a purely agency basis, without control over decisions to enter into a contract and without discretion to independently enter into a contracts, the Commission believes that DESCO LP would be considered a public utility if it participated in wholesale transactions under the conditions described in the Petition.

Id.

45. The Commission further stated that its "fundamental mission is to regulate the transmission and sale of electric energy for resale in interstate commerce. To fully preserve our ability to do so, the Commission considers it vital to be able to encompass within its regulation all of the entities that are actually supplying power to wholesale markets. We regard DESCO LP as one such entity." *Id.* at 61,826.

46. In this case Enron entered into contracts for El Paso based solely on Enron's discretion. Enron was not an agent or a broker for El Paso. As stated above, Enron gained operational control of El Paso's jurisdictional assets with control over decisions involving El Paso's contracts and with discretion to independently enter into such contracts. At times acting on El Paso's behalf, Enron sold power to itself. This belies brokering activities. The Commission has defined a broker as one who takes no title to electricity. *Enron Power Marketing, Inc.*, 65 FERC ¶ 61,305(1993) citing *Citizens Energy Corp.*, 35 FERC ¶ 61,198 (1986) (Citizens providing brokerage type services not involving any purchase or sale of power by Citizens). Unrebutted record evidence demonstrates that in some transactions Enron took title to El Paso's power. Exs. S-40 at p. 44-5; S-39 at p. 3; S-9 at p. 6 ¶ 16; S-10 at p. 9; S-37 at p. 4. Due to the nature of the business relationship between both parties, it is not possible to differentiate in which transactions this did in fact occur. *Id.*

47. The head of El Paso's marketing division testified concerning real time trading sales:

[S]ome were specifically purchased by Enron. Some were purchased by other third parties. However, for billing purposes, to aggregate the billing, and to simplify the billing, it would show up as a sale from Enron to a third party, and as a sale to them. So as a whole, you can say, all the sales were supposedly to Enron and that Enron was the reseller. But not all sales were in fact that. Some were strictly to Enron. Some were not.

Ex. S-40 at pp. 44-45.

48. Furthermore, by Enron's actions (with no input from El Paso) Enron set or affected the price El Paso obtained for its power. Again, this is evidence that Enron was not an agent or broker. Traditionally, an agent or a broker acts on behalf of a client, and the client ultimately decides whether to enter a transaction and the price. Also, traditionally, an agent or broker does not have the capability to act as a counterparty to a transaction. The record evidence demonstrates this was not the situation in this case. Finally, evidence given substantial weight, shows that Enron and El Paso profit-shared supplemental market sales and ancillary services sales to the CAISO. This proves that the relationship was not brokering.

49. In this case, by virtue of Enron's actions, the Commission did not have a clear picture of who was actually supplying power into the wholesale market. Staff is correct that Enron's previously approved tariff¹⁹ did not give it authority to perform the services contemplated in the PCSA, therefore it had to seek prior approval from the Commission before initiating this service. Record evidence supports Staff's argument that Enron, by virtue of the PCSA, gained control of El Paso's generators by controlling the marketing division of El Paso (a utility with a franchised service area).

¹⁹ Enron's market based-rate authority allowed it to sell electricity at wholesale at market based rates. It did not authorize Enron to act as El Paso's marketing division.

50. Enron's posturing is preposterous.²⁰ Case law provides ample support for the findings and conclusions in this case concerning the PCSA. Additionally, Staff correctly points out that the Commission has repeatedly stated that market participants, if uncertain as to filing requirements, should seek a determination from the Commission. *Prior Notice, supra* at 61,977-78. *See also, California Power Exchange Corporation*, 86 FERC ¶ 61,001 at 61,005 (1999); *California Independent System Operator*, 81 FERC ¶ 61,321 at 62,482 (1997). Enron could have sought guidance by using one of the methods enumerated in the cited cases.

51. It is found that Enron operated El Paso's trading desk during non business hours. It is additionally found that during this operation Enron controlled jurisdictional assets and directed sales for El Paso at Enron's sole discretion (subject only to reliability concerns). Enron never filed this contract with the Commission. Consequently, it is concluded that Enron violated Section 205(c) of the FPA.

52. In *Prior Notice, supra* at 61,979-80, the Commission adopted a remedy for failing to comply with prior notice and filing requirement of the FPA. In so doing the Commission stated that it has attempted to convey to the industry the seriousness with which it viewed failures to comply with the prior notice and filing requirements of the FPA, which require rates or charges for jurisdictional service, or contracts affecting or relating to such service to be filed. The Commission held that: "we will require the utility to refund to its customers the time value of the revenues collected, calculated pursuant to section 35.19a of our regulations, for the entire period that the rate was collected without Commission authorization." *Id.* In addition, the Commission stated: "the late filing utility will receive the equivalent of a cost-based rate, less the time value remedy applicable to the unauthorized late filing of cost based rates, until the date of Commission authorization." The time value of the revenues collected is calculated pursuant to section 35.19a of the Rules for the entire period the rate was collected without Commission authorization. *Id.*

²⁰ For instance, Enron argues that the Commission has waived its Section 205(c) requirements for power marketers. This argument defies the realm of reasonableness. *Cf. Ford Motor Company and Rouge Steel Company*, 52 FERC ¶ 61,025 at 61,145 (1990) (Requirement for interlocking directorates comes from the FPA Section 305, 16 U.S.C. § 825d, and the Commission has no authority to waive it). Along the same lines, Enron argued that it was public knowledge that it had entered into a contract with El Paso. This argument is inane.

53. In the instant case, the record is devoid of Enron's costs. Enron asserted a number of reasons for not producing its costs, none of which are persuasive.²¹ Staff witness Barlow calculated an estimated range of profits and recommended a refund amount (this amount is an approximation and it is likely that using variable operation and maintenance expenses plus interest would yield a higher amount). Barlow's uncontradicted testimony is reasonable and entitled to substantial weight.²² Barlow estimates EPMI earned approximately \$19,303,468 using a low profit number and \$45,754,064 using a high profit number, from its transactions as a result of its alliance with El Paso by virtue of the PCSA. Ex. S-50 at pp. 5-6; Attachment A at p. 1. Consistent with Commission policy, as enunciated in *Prior Notice, supra* at 61,980; it is reasonable to average out these two figures to reflect the equivalent of a cost based rate.²³ Accordingly, Enron should disgorge \$32,528,766.

54. The contract was executed by Enron Capital (now d/b/a Enron North America). However, its wholly owned subsidiary EPMI performed the contract. The contract was never amended to substitute EPMI.²⁴ Consequently, as Staff correctly points out, both

²¹ Enron's conduct throughout this hearing was disingenuous. Moreover, it failed to produce relevant data, producing vague and incomplete responses. Exs. S-19 at p. 3; S-20 at p. 1. According to Enron, it could not provide responses, because the "vast majority of Enron's electric traders have left the company." Ex. S-19 at p. 7. As a matter of fact, an adverse inference is appropriate against Enron based on its failure to provide information which is clearly within its control. Thus, the missing information, would most likely raise Enron's profits higher or reduce its costs. *See, Alabama Power v. FERC*, 511 F 2d 383, 391 n. 14 (D.C. Cir 1974). Enron's prior responses in PA02-2 do not cure its lack of candor in this case. Enron's defense was essentially that newspapers articles constituted notice to the Commission and disgorgement is inappropriate since it is in bankruptcy proceedings.

²² Barlow's testimony is more reasonable than California's witness Merola. Accordingly, Barlow's testimony is given substantial weight.

²³ This was done due to the fact that the \$45,754,064 figure does not give Enron the benefit of certain costs such as interest and taxes.

²⁴ The PCSA was effective January 17, 1997, through April 30, 1997, continuing on a month- to- month basis until December 31, 2001. Enron performed services on a week-to-week basis until March, 2002, when UBS Warburg assumed Enron's duties on a week-to-week basis until May 7, 2002 (El Paso instituted its own 24-hour marketing desk). Ex. EPE-1 at p. 19:8-13.

Enron North America and EPMI are jointly and severally liable for the refund amount (contractually and by corporate practice).

55. Enron's arguments concerning the appropriate remedy in this case are meritless. First, the refund effective date of the FPA does not prohibit retroactive refunds in cases such as the case at bar, where the utility did not file a contract pursuant to Section 205(c). As a matter of fact, the case cited above is dispositive of this issue. Additionally, contrary to Enron's arguments, the filed rate doctrine does not bar recovery of the proposed refunds in this case. This is so, since the filed rate doctrine presupposes a filed rate, which is not the situation in the case at bar. The filed rate doctrine generally forbids a regulated utility from charging rates for its services other than those properly filed with the Commission. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 (1981). The doctrine preserves the Commission's jurisdiction over reasonableness of rates and insures that companies charge only those rates "of which the agency has been made cognizant." *Id.* at 577-78. Second, the Commission is authorized to order disgorgement of profits. See *Prior Notice, supra*.²⁵

56. Staff correctly points out, that Enron did not make the Commission cognizant of its rates or the jurisdictional service it was providing El Paso. The filed rate doctrine applies two provisions of the FPA. Sections 205(c) (requires filing of rate schedules) and Section 206(a), 16 U.S.C. § 824e(a), (Commission may fix rates and charges prospectively). Construed together, "these provisions prohibit 'a regulated seller of [power] from collecting a rate other than the one filed with the Commission and prevent the Commission itself from imposing a rate increase for power already sold.'" *Towns of Concord, Norwood, and Wellesley, Massachusetts v. FERC*, 955 F.2d 67, 71-72 (D.C. Cir. 1992).

57. Furthermore, Staff is correct, that, as a matter of policy, refunds are appropriate in this case. As the Commission has previously stated, remedies have been established to convey to the industry the seriousness with which it viewed failures to comply with the prior notice and filing requirements of the Act, which require rates or charges for

²⁵ See also *Enron Power Marketing, Inc.*, 103 FERC ¶ 61,343 at ¶ 72 (2003) (the Commission has discretion to fashion remedies for conduct that has violated its policies or rules). This case cites, *Niagara Mohawk Power Corp. v. FPC*, 379 F.2d 153,159 (D.C. Cir. 1967); *Connecticut Valley Electric Company, Inc. v. FERC*, 208 F.3d 1037, 1044 (D.C. Cir. 2000); *Louisiana Public Service Commission v. FERC*, 174 F. 3d 218, 225 (D.C. Cir. 1999).

jurisdictional service, or contracts affecting or relating to such service to be filed. The disgorgement of this money would place Enron in the same position it would have been in had it sought traditional, cost-based rates.

58. Accordingly, for violation of Section 205(c) of the FPA, Enron is ordered to refund \$32,528,766.²⁶ Staff proposed that the refund amount should go to consumers adversely affected by Enron's actions. The California parties contend that the refunds should go to California because Enron's conduct was targeted at California. This appears to be reasonable and justified by the evidence in this case. See, Exs. CAL-5 at p. 11; S-31 at p. 1; S-30 at p. 12; S-34 at p. 4; TAC-9 at p. 3; EPMI-2 at p. 8; EPMI-2 at p. 7; EPE-18 at pp. 16-17; S-36 at p. 7. Moreover, Tacoma and Snohomish did not claim they made purchases in California and did not submit any evidence of specific monetary claims against Enron. As discussed below, these parties have standing to intervene in new proceedings where disgorgement of profits is being considered.

Issue B. Did Enron Violate the 1993 Order Granting it Market-Based Rate Authority by Not Filing the PCSA or Failing to Notify Material Changes of Circumstances (Including in its Updated Market Power Analysis)? If a Violation is Found, What is the Appropriate Remedy?

²⁶ On April 29, 2003, the California Parties filed a Motion for Institution of Consolidated Proceeding to Address Remedy and Damage Issues and for Common Protective Order (Motion for Consolidation), addressed to this docket and all of the other pending dockets relating to remedies for market manipulation in the California market, including *San Diego Gas & Electric Company, et al.*, Docket Nos. EL00-95, *et al.*, *Fact-Finding Investigation Into Possible Manipulation of Electric and Natural Gas Prices*, Docket No. PA02-2-000, *Reliant Energy Services, Inc.*, Docket No. EL03-59-000, *BP Energy Company*, Docket No. EL03-60-000, *Enron Power Marketing, Inc., et al.*, Docket No. EL03-77-000, *Bridgeline Gas Marketing, LLC, et al.*, Docket No. RP03-311-000, *Portland General Electric Company, et al.*, Docket Nos. EL02-114-000, *et al.*, and *Avista Corporation, et al.*, Docket No. EL02-115-000. This request was denied by the Commission. See *San Diego Gas & Electric Company*, 103 FERC ¶ 61,359 (2003).

A. Arguments of the Parties and Staff:

59. Staff alleges that Enron violated the 1993 Commission order granting Enron market based rate authority. Staff I.B. at p. 32. According to Staff, Enron's market based rate authority was conditioned upon the circumstances existing in 1993. *Id.* Any change in circumstances, Staff maintains, required Enron to inform the Commission of such changes. *Id.* Enron violated the order, Staff asserts, by failing to notify the Commission of material changes in circumstances. *Id.* Specifically, Staff explains, the Enron and El Paso alliance, as well as other alliances entered into between Enron and other participants in the Western power markets, "violated both the spirit and the explicit conditions of that 1993 Order." *Id.*

60. In Staff's view, the Commission described two primary issues in its 1993 Order critical for any public utility in obtaining market based rate authority. Staff I.B. at p. 33. First, Staff states, is the potential for a public utility, either alone or in conjunction with an affiliate, to possess market power, and, second, the potential for a public utility to engage in either self or reciprocal dealing. *Id.*

61. By failing to notify the Commission of its alliance with El Paso, Staff claims, Enron violated the requirement to notify the Commission of any change in circumstances related to Enron's initial market based rate application. *Id.* at p. 34. Staff asserts that the PCSA created changed circumstances in four ways:

(1) by increasing EPMI's market share of generation; (2) by creating an affiliation (or 'effective' affiliation) with EPE; (3) by creating the opportunity for self-dealing; and (4) by providing EPMI with sensitive, competitive market information that gave it a marketplace advantage.

Id. at pp. 34-35.

62. Market share was increased and a change in status created, Staff explains, because the characteristics the Commission had relied upon when approving Enron's market based rate authority was predicated on Enron's control of little or no generation. *Id.* at p. 35. As Enron had the authority to make economic decisions regarding the output of El Paso's Palo Verde nuclear plant in Arizona and the coal-fired Four Corners plant in New Mexico, Staff notes, market share was significantly increased. *Id.*

63. Additionally, Staff states, the PCSA created a changed circumstance requiring Commission notification because the PCSA created an affiliation with El Paso. *Id.* According to Staff, even though there was no common ownership between El Paso and

Enron, the relationship satisfies the Commission's definition for power marketing affiliates. *Id.* The Commission's definition, Staff notes, is whether two entities share a common source of control. *Id.* Enron, Staff asserts, obtained such control by having authority to make decisions over the economics of El Paso's power scheduling activities. *Id.* at p. 36. Furthermore, Staff asserts that the Commission has stated that a consulting agreement such as the PCSA can create an affiliation. *Id.* at p. 39.

64. Alternatively, Staff argues, Enron and El Paso became constructive or effective affiliates and should have followed the same safeguards as affiliates do. *Id.* at p. 40. Staff maintains that the alliance, whether actual or constructive affiliates, raises the same concerns over market power, affiliate abuse or self-dealing, and anti-competitive practices. *Id.* Also, Staff explains, the affiliate relationship is demonstrated by the degree and quantity of confidential and proprietary information transferred as well as the extremely close aligning of business interests beyond normal contractual relationships. *Id.*

65. Staff also believes that the PCSA constituted a changed circumstance because it allowed Enron to engage in self-dealing. *Id.* at p. 42. According to Staff, the PCSA also constituted a changed circumstance because it provided Enron with a constant source of sensitive, competitive, information about the western electricity market. *Id.* at p. 43.

66. Staff claims that the *Morgan Stanley Capital Group, Inc.*, 72 FERC ¶61,082 (1995), decision did not eliminate Enron's duty to disclose the PCSA to the Commission. *Id.* at p. 44. In Staff's view, *Morgan Stanley* did not remove either the notification requirement or the prohibition on affiliate self dealing. *Id.* at pp. 44-45. Instead, Staff insists that *Morgan Stanley* merely provides that power marketers do not need to file all business and financial relationships with those entities in which the power marketers engage in wholesale power transactions. *Id.* at p. 45. However, Staff maintains, power marketers must still notify the Commission if their generation increases, new affiliations are created, or self-dealing opportunities arise. *Id.* at pp. 45-46.

67. Enron's business strategy, Staff asserts, was to secretly dominate the western power markets by actively courting load serving entities and industrial entities in order to control and market their generation. *Id.* at pp. 46-47. Consequently, Staff maintains, "Enron's relationship with [El Paso] was just one piece of the puzzle." *Id.* at p. 48. Enron's failure to notify the Commission, Staff asserts, of these numerous alliances also constitute a violation of Enron's market based rate authority. *Id.*

68. Staff notes that Enron did not present evidence or testimony regarding this issue. *Id.* at p. 49.²⁷ Additionally, Staff argues that Enron's narrow reading of the 1993 Order should be rejected because Enron misinterprets the Order to mean that it must notify the Commission of a change in circumstances only where the changed circumstances involve ownership of transmission or generation. Staff R.B. at p. 21. Staff contends that Enron purposefully distorts the record by claiming that the terms of the PCSA provide that El Paso controls its own generation, and ignores the extent of Enron's control over El Paso's jurisdictional assets. *Id.* at p. 22.

69. Staff dismisses as "utterly absurd" Enron's contention that since the market was aware of its alliance with El Paso and the alliance was reported by the media this was sufficient notice to the Commission. *Id.* at p. 30.

70. As for Enron's argument that the Commission can not order refunds for transactions entered into before the refund date, Staff asserts that this is not so because Enron violated its market based rate tariff when it refused to file the PCSA. *Id.* at p. 21. Retroactive refunds, Staff maintains, may be ordered by the Commission regardless of the refund date for violation of its orders or tariffs. Staff R.B. at p. 34. The prohibition against retroactive ratemaking, Staff explains, merely prevents the Commission from changing a previously filed rate. *Id.* at p. 35.

71. Despite Enron's contention that the Commission can not order disgorgement, Staff notes that the Commission has explicitly stated that it has the authority to order Enron to disgorge profits if the FPA was violated. *Id.* at p. 32. Additionally, Staff asserts that as Enron failed to comply with the 1993 Order, it violated the FPA and could not charge its filed rate. *Id.* at p. 33. At minimum, Staff insists, Enron was selling the wholesale energy on El Paso's behalf without a filed rate. *Id.* at p. 34. Staff states that "[n]o matter which way the Commission ultimately conceptualizes what Enron did, the conclusion is obvious: Enron performed under the PCSA without Commission approval." *Id.*

72. Enron's market based rate authority, Staff recommends, should be revoked and all profits made above cost-based rates after executing the PCSA should be refunded. *Id.* According to Staff, after the PCSA was signed, every Enron transaction was tainted because of the changed circumstances. *Id.* at p. 50. Consequently, Staff insists, the Commission has the authority to order disgorgement for those transactions stemming

²⁷ Staff pointed out Enron's failure to produce relevant data throughout this proceeding. *Id.* at p. 51.

from the Enron and El Paso alliance. *Id.* Witness Barlow estimates this amount to be \$124,727,794 for all Western Systems Power Pool (“WSPP”) transactions entered into by EPMI from 1997 through 2001. *Id.* Staff does not characterize its choice of remedy as a penalty, which Staff concedes would be unlawful. *Id.* at p. 36. Instead, Staff insists that its remedy is permissible because it would place Enron in the same position it would have been under a traditional cost based rate regime. *Id.* According to Staff, its remedy would prohibit Enron from retaining unlawful profits from its contractual rates, while allowing Enron to retain just and reasonable rates. *Id.* at p. 38.

73. As for Enron’s contention that Staff did not properly investigate and analyze Enron’s costs, Staff responds that “this argument is bizarre, for it places upon Trial Staff the duty to present Enron’s own case as to its actual costs.” *Id.* at p. 39. Staff notes that it met its burden of proof by presenting testimony regarding Enron’s profits, and Enron failed to proffer any data challenging Staff’s analysis and conclusions. *Id.* Further, Staff states that the Commission, under the FPA, may make any finding of fact if the finding is based on substantial evidence. *Id.*

74. Furthermore, Staff believes that Enron North America and EPMI should be held jointly and severally liable for the refunds because, even though EPMI performed under the PCSA, ECT executed the contract and was the parent of EPMI. *Id.* ECT, Staff notes, subsequently became Enron North America. *Id.*

75. The California Parties agree with Staff that Enron’s failure to inform the Commission about its relationship with El Paso violated the Commission’s 1993 Order. California I.B. at p. 15. Enron’s alliance with El Paso, the California Parties argue, was a change in status requiring notification. *Id.* According to the California Parties, the Commission’s order granting Enron market based rate authority was predicated on Enron’s lack of generation dominance, and also required Enron to inform the Commission of any change in circumstances. *Id.* The California Parties note that the Commission explained that it granted Enron’s market based rate authority request because generation dominance was not an issue. *Id.* at p. 16. In the California Parties’ view, the Commission was concerned with whether an applicant for market based rate authority actually controlled generation in such a fashion that the applicant could wield market power. *Id.*

76. Enron, the California Parties note, did not own El Paso’s generation facilities and did not have an ownership interest in El Paso. *Id.* at p. 17. Nevertheless, the California Parties explain, Enron exerted sufficient operational control over El Paso’s assets to effectively be in control over El Paso’s generation. *Id.* This operational control, the California Parties insist, qualified sufficiently as change in status so that Enron was obligated to inform the Commission of the PCSA. *Id.* The PCSA granted Enron

significant control, the California parties contend, over the Palo Verde Nuclear Generating Station and the Four Corners Generating Station. *Id.* at p. 18.

77. The *Morgan Stanley* decision, the California Parties claim, did not relieve Enron of its obligation to inform the Commission about the Enron and El Paso alliance. *Id.* at p. 19. They argue that the obligation to report the alliance was independent of the reporting requirement eliminated in the *Morgan Stanley* decision because that decision eliminated only the business and financial arrangements reporting requirement. *Id.* Enron, the California Parties insist, was still obligated to report any changes in generation control. *Id.*

78. The California Parties maintain that the Commission should revoke Enron's market based rate authority and should require Enron to disgorge all profits made under its authority between 1997-2001 because Enron failed to inform the Commission of its change in status. *Id.* at p. 21. However, the California Parties advocate that the best solution is to consider remedies on a market wide basis. *Id.* Accordingly, although the record in this case clearly justifies imposition of both remedies, the California State Parties urge the Commission to defer imposition of any remedy against Enron in this proceeding, consolidate the remedies phase of this proceeding with all other pending proceedings involving remedies for market manipulation in the California markets, and act to grant both retrospective relief (disgorgement of profits) and prospective relief (revocation of market-based rate authority) on a coordinated and market-wide basis. *Id.* at p. 21.

79. According to the California Parties, Enron earned approximately \$2.974 billion from its wholesale power business between 1997 and 2001 and it should be required to disgorge the entire amount. *Id.* Additionally, the California Parties insist that Enron's market based rate authority must be revoked. *Id.* at p. 25. In particularly purple language, they argue that "Enron's cynical and calculated flouting of the Commission's reporting requirements makes it clear that Enron does not deserve and cannot be trusted with the pricing latitude that sellers enjoy under market-based rates." *Id.*

80. Tacoma states that it agrees with Staff's positions and analysis about Enron's behavior. Tacoma R.B. at p. 2. Furthermore, Tacoma argues that Enron's assertion that holding it accountable for failing to file the PCSA would violate the fair notice doctrine is without merit. *Id.* at p. 4. Enron's affiliation with El Paso, Tacoma insists, triggered the 1993 Order's filing requirement. *Id.* at p. 6. Enron's self-dealing behavior, Tacoma alleges, also triggered the filing requirement. *Id.* Despite Enron's arguments, Tacoma maintains, the PCSA should have been filed with the Commission. *Id.* at p. 7.

81. Tacoma recommends that the Commission find a west wide remedy for Enron's actions. Tacoma R.B. at p. 2. It supports Staff's \$125 million disgorgement for all WSPP transactions Enron entered into between 1997 and 2001. *Id.* at p. 3. According to Tacoma, only the all WSPP transactions alternative "fairly acknowledges the nature and extent of Enron's manipulation of the entire Western market." *Id.*

82. Enron asserts that the 1993 Order does not require notification of its relationship with El Paso because that relationship did not change any of the underlying material facts upon which the Commission relied on when issuing its Order. Enron I.B. at p. 11. According to Enron, the material facts were that Enron did not control an undue share of the market, did not control key inputs to the electric generation process, and could not erect barriers to entry. *Id.* at p. 12. Enron insists that the PCSA did not alter any of these material facts. *Id.* at p. 13. As no material facts were changed, Enron states, there was no duty to inform the Commission of the PCSA. *Id.*

83. According to Enron, it did not own El Paso's generation or transmission facilities, asserting that it merely directed El Paso's generation. *Id.* at p. 14. Further, Enron maintains, the PCSA Article 1²⁸ provided that El Paso shall control its generation. *Id.* at p. 15. Enron also contends that Staff agrees that Enron's role was to merely make suggestions to El Paso, which El Paso was then free to reject or accept at its discretion. *Id.* Commission notification, Enron insists, is triggered only where ownership of facilities existed, and, as it never owned any of El Paso's facilities, Enron can not be liable. *Id.* at p. 16.

84. Enron also contends that its relationship with El Paso did not result in an affiliation between the two companies. *Id.* According to Enron, affiliation requires either an ownership interest or control of another firm's management or policies, and it met neither of those conditions. *Id.* at p. 17.

85. Additionally, Enron argues that the *Morgan Stanley* decision eliminated the obligation to report business and financial arrangements in 1995, and, as the PCSA was entered into in 1997, Enron was not required to report that relationship. *Id.* at p. 18. In

²⁸ At all times during the term of this Agreement EPE shall retain ownership and control of, and operational responsibility with respect to, all of its tangible and intangible assets, including generation, transmission, and distribution assets, power purchase and sale contracts, and fuel and transportation agreements. The parties agree that the advice provided by ECT to EPE hereunder will be strictly recommendations and that EPE may, in its sole discretion, reject or accept any such advice. S-2.

any event, Enron asserts, its relationship with El Paso was well reported by the press. *Id.* at p. 19 and Tr. 320:2-3. Consequently, Enron claims, the Commission should have known that Enron was receiving information from El Paso, and it was not willfully evading the Commission's reporting requirement. Enron I.B. at p. 20. Enron also notes that other market participants were aware of the Enron and El Paso arrangement because when those market participants attempted to contact El Paso the phone was answered by Enron personnel. *Id.*

86. The Commission, Enron insists, when listing the triggering issues requiring notification in the 1993 Order meant for the three listed issues to be exhaustive. *Id.* Enron believes that the phrase "include but not limited to" cannot be used to create a separate reporting requirement when the precise reporting requirement involved had already been abolished. *Id.* Enron accuses Staff of attempting to reverse the *Morgan Stanley* decision. *Id.* at p. 21. If the Commission were to accept Staff's position, Enron maintains, "the marketing industry would be in a dither" because the Commission could selectively enforce its reporting requirements. *Id.*

87. Enron further insists that it did not receive a competitive advantage by receiving information from Palo Verde because that information was already available to the seven owners of Palo Verde, those owners had market based rate authority, and were Enron's competitors. *Id.* Consequently, Enron argues that Staff's "insistence that the receipt of information known to others would somehow trigger a reporting requirement is both discriminatory and unduly vague." *Id.* at p. 22. Furthermore, Enron believes that forcing it to disgorge money under such a vague requirement would violate the fair notice provision of the due process clause. *Id.*

88. According to Enron, the fair notice doctrine prevents deference to agency interpretations, thus preventing validation of a regulation in those instances where a regulation fails to give warning of the conduct that is prohibited. *Id.* at p. 23. Enron notes that the test under the fair notice doctrine is whether the provision provides with ascertainable certainty standards with which the agency expects parties to conform. *Id.* at pp. 23-24. As the Commission's reporting requirements have been erratic and shifting over time, Enron contends, it could not have known with ascertainable certainty what the reporting requirements were. *Id.* at pp. 24-26.

89. Enron responds that any remedy forcing retroactive reparations that effectively reduce rates below actual costs is unlawful. Enron I.B. at p. 11. Even if it did violate the Commission's notification requirement, Enron asserts, disgorgement of funds would be an inappropriate and unlawful remedy because disgorgement is an unlawful retroactive refund. *Id.* at p. 27. According to Enron, the Commission is precluded from compelling disgorgement for sales before the refund effective date in this case – October 15, 2002.

Id. In Enron's view, retroactive refunds are forbidden under the FPA. *Id.* FPA Section 206(b), Enron explains, allows the Commission to order refunds 60 days after the Commission or a private party initiates an investigation or files a complaint. *Id.*

90. Enron contends that Staff attempts to contravene the Commission's prohibition against ordering retroactive refunds, by characterizing those refunds as disgorgement, but contends that the Commission is also prohibited from doing something indirectly when it cannot accomplish something directly *Id.* at p. 28. Furthermore, Enron claims that the Courts have forbidden the Commission from ordering disgorgement as a penalty. *Id.* at p. 32.

91. According to Enron, the filed rate doctrine protects its behavior because the doctrine holds that when a rate is on file with the Commission, revenues from sales made pursuant to that rate are protected by the prohibition against retroactive ratemaking. *Id.* at p. 35. As part of the 1993 Order, Enron maintains, the Commission acted on its tariff, which continues to be in effect. *Id.* Consequently, Enron asserts, the rates were charged pursuant to a filed tariff in accordance with Section 205. *Id.* Enron insists that Staff's position that by failing to file the PCSA Enron's sales in the western power markets are unlawful is without basis. *Id.* at p. 36. Additionally, Enron notes that the 1993 Order is silent as to the consequences of failing to notify the Commission about changes in material circumstances, which Enron interprets to mean that the Commission could not have intended to nullify the tariff. *Id.*

92. Enron also argues that before the Commission may reduce rates by any means, it must first declare existing rates to be unjust and unreasonable, must determine the just and reasonable rate, and ensure that the result is not confiscatory. *Id.* at p. 42. No party, Enron explains, provided evidence on these subjects in this proceeding. *Id.* Enron notes that under the FPA Section 205, as long as a power marketer has a tariff on file with the Commission, and files quarterly reports, the rates charged by the power marketer comply with the FPA. *Id.* at p. 38. Enron asserts that it was in full compliance. *Id.*

93. Furthermore, Enron contends that the scope of this case is limited to transactions related to Enron's relationship with El Paso and is not intended as an investigation into Enron's behavior throughout the western power markets. *Id.* at p. 43. Consequently, Enron insists that any remedies must arise only from its relationship with El Paso. *Id.* at pp. 44-45.

94. According to Enron, Staff's methodology fails to consider its actual costs in determining an appropriate refund amount. Moreover, Enron accuses Staff of ignoring data which could have been used to develop a refund amount. *Id.* at p. 46. Finally, Enron

argues that the Commission lacks the authority to issue refunds because the record does not clearly establish who should receive the refunds. *Id.* at pp. 50-52.

B. Discussion:

95. Enron was granted market-based rate authority in 1993. *Enron Power Marketing, Inc.*, 65 FERC ¶ 61,305 (1993). The Commission stated that: Enron did not own generation facilities and was not affiliated with an entity with a franchised service territory; although affiliated with entities which own generating facilities, all but one, are qualifying facilities committed to sell their entire output on a long-term basis and thus cannot sell to others in the market; the one remaining affiliate, Milford Power Limited Partnership (“Milford”), does not have market power in generation; Enron does not own transmission facilities; Milford owns limited transmission facilities but does not have transmission market power; Enron is affiliated with natural gas buyers and sellers and pipelines that are non-discriminatory, open-access carriers; Enron and its affiliates do not own or control any resources which could be used to create barriers to entry to other suppliers; and there is no evidence that Enron will engage in any self dealing or reciprocal dealing. *Id.* at 62,404-05. In this case, the Commission also granted Enron’s request to disclaim jurisdiction over its activities as a broker.²⁹ *Id.*

96. Additionally, the Commission directed Enron

to inform the Commission promptly of any change in status that would reflect a departure from the characteristics the Commission has relied upon in approving market-based pricing. These include but are not limited to: (1) ownership of generation or transmission facilities or inputs to electric power production other than fuel supplies; (2) affiliation with any entity that owns generation or transmission facilities or inputs to electric power production, or affiliation with any entity that has a franchised service area; or (3) business and financial arrangements involving Enron or any entity affiliated with Enron and the entities that buy from or sell power to Enron.

Id.

97. The Commission terminated EPMI’s market-based rate authority and its electric market-based rate tariff. In the same case the Commission also terminated Enron North

²⁹ Citing *Citizens Energy Corporation*, 35 FERC ¶ 61,198 (1986) stating that brokers, take no title to electricity and fall outside FPA jurisdiction.

America Corp.'s authorization under 18 C.F.R. § 284.402 issuing a limited authorization to allow it to conduct certain activities specified in the Order dealing with dissolution of the company. *Enron Power Marketing, Inc.*, 103 FERC ¶ 61,343 (2003) ("Revocation Order"). The Commission looked at the same conduct involved in this proceeding; gaming in the form of inappropriate trading strategies: False Import (i.e. Ricochet or Megawatt Laundering), filing false schedules and the use of partnerships and alliances to gain market share, acquire commercially sensitive data and decision making authority, promote reciprocal dealings, and equity sharing of profits. Moreover, the Commission stated that Enron formed these business alliances or partnerships without notifying the Commission, as required under their market-based rate authorizations. *Id.* at ¶ 53-56. In the case at bar, Enron filed its brief as EPMI and Enron North America Corp., d/b/a Enron Capital and Trade Resources Corporation. The Revocation Order includes Enron North America Corp. There is no evidence in this record that this is a different company. The Commission's Revocation Order is dispositive of this issue. However, for purposes of developing the record and in compliance with the Commission's mandate in this proceeding, the following findings are set forth below.

98. Record evidence demonstrates that Enron's dealings with El Paso violated Enron's market-based rate authority. Enron never informed the Commission of its changed circumstances, the PCSA, or its relationship with El Paso. Staff is correct that the PCSA changed Enron's circumstances in at least four different ways. First, it increased Enron's market share of generation. Second, it created an affiliation with El Paso. Third, it created an opportunity for self-dealing. Fourth, it provided Enron with sensitive, competitive market information which gave it an advantage in the marketplace. Contrary to Enron's contentions, the language in Enron's market-rate based authority did not specifically limit the reporting requirements merely to instances of ownership in generation assets. The order specifically stated the reporting requirements apply to "any change in status" and "include but are not limited to." Record evidence demonstrates there was "a change" in Enron's status and "not limited" includes all the matters discussed in this order.

99. As Staff points out, the PCSA gave Enron control of a portion of the output of two major generators in the Southwest which mainly serve the California market. These are: the Palo Verde nuclear plant in Arizona and the coal-fired Four Corners plant in New Mexico. Enron in fact had authority to make economic decisions regarding the output of these generators to its own advantage.³⁰ As a result, by virtue of the PCSA, Enron's

³⁰ Staff also argues that by virtue of this fact, Enron lost its status as a power marketer since the Commission defines power marketers as non-traditional public utilities, without ownership, operation or control of generation or transmission facilities.

circumstances had changed since this changed the size of its market share. Enron's competitive position in the generation market had changed. Enron should have informed the Commission of this changed circumstance.

100. The PCSA created an affiliation between Enron and El Paso. Enron and El Paso shared a common source of control; Enron exercised decision making authority over the economics of El Paso's power scheduling activities and the related jurisdictional assets. Enron operated the El Paso trading desk and exercised control over the sale of power. Commission decisions support the finding that by virtue of such control, Enron "operated" El Paso's facilities for purposes of the FPA and Commission rules. Thus, Enron and El Paso were affiliates within the purview of the Commission's rules.

101. The Commission has specified that for a determination of affiliation under Part II of the FPA applicable to all public utilities (excluding Exempt Wholesale Generators "EWG" public utilities) it will use the definition of affiliate found in Section 161.2(a) of the Rules. Section 161.2(a) of the Commission Rules, 18 C.F.R. § 161.2(a) defines "affiliate" as "another person which controls, is controlled by, or is under common control with, such person." Subparagraph (b) of this same section states that "control (including the terms 'controlling,' 'controlled by,' and 'under common control with,') includes, but is not limited to, the possession, directly or indirectly and whether acting alone or in conjunction with others, of the authority to direct or cause the direction of the management or policies of a company . . ." *Morgan Stanley Capital Group Inc.*, 72 FERC ¶ 61,082 at 61,436-37 (1995) (all non-EWG public utilities should define affiliate as that term is used in the Commission's regulations regarding Standards of Conduct for Interstate Pipelines with Marketing Affiliates, for matters arising under Part II of the FPA).

102. The Commission has emphasized that it adopted a broad definition of control because "overlapping economic interests create an incentive to grant an affiliate preference." The definition of control "is not limited to the ability to directly control the management of a company but also includes situations in which a pipeline, by itself or in conjunction with others, has an economic incentive to favor an affiliate." In addition, the Commission stated that "any overlapping economic interest gives rise to the possibility that a preference may occur." For shared economic interests, the Commission stated it would examine, on a "case-by-case basis, the particular circumstances involved in the relationship between the pipeline and a natural gas marketer to determine whether a

Citing *Southern Company Services, Inc.*, 87 FERC ¶ 61,847 (1999). Indeed by virtue of its control of generation assets, Enron was not just a "power marketer."

sufficient incentive and opportunity exists to favor the marketer. If the Commission concludes that the incentive and ability to engage in anticompetitive conduct exists, it will require the pipeline to conform to the rule's standards of conduct and reporting requirements." *Inquiry Into Alleged Anticompetitive Practices Related to Marketing Affiliates of Interstate Pipelines, order on reh'g, Order No. 497-A*, 54 Fed. Reg. 52,781 (December 22, 1989), FERC Stats. & Regs. ¶ 30868 at 31,593-94 (1989). Staff correctly analogizes the quoted language to the situation between El Paso (replace the term "pipeline" with El Paso) and Enron (replace that term "natural gas marketer" with "Enron" the entity selling El Paso's power). In the case at bar, the PCSA gave Enron and El Paso overlapping economic interests, and thus they became "affiliates" under the Commission rules.

103. In *New Energy Ventures, Inc.*, 76 FERC ¶ 61,239 at 62,157 (1996), the Commission approved market-based rate authority for New Energy (a power marketer). New Energy had conceded that a Consulting Agreement with Tucson Electric Company ("Tucson") (a transmission-owning utility) created an affiliate relationship with Tucson for purposes of the market-based rate application.³¹ Likewise, in the case at bar, the PCSA (allegedly a consulting agreement also) created an affiliate relationship between the parties.

104. Case law provides examples of the Commission's interpretation of control for purposes of asserting jurisdiction over entities or their agreements. In *Bechtel Power Corporation*, 60 FERC ¶ 61,156 at 61,573 (1992), the Commission interpreted the word 'operates' in Section 201(e) of the FPA as the person who has control and decisionmaking authority concerning the operation of the facility. In the cited case the

³¹ The Commission looks at market power (the utility alone or in conjunction with an affiliate) and the potential for self or reciprocal dealing in determining whether to grant market-based rate authority. *Citizens Power*, 48 FERC ¶ 61,210 at 61,777 (1989). See generally *Entergy Services Inc.*, 74 FERC ¶ 61,137 (1996); *Illinois Power Company*, 73 FERC ¶ 61,371 (1995); *Heartland Energy Services*, 68 FERC ¶ 61,223 (1994). The Commission looks at a number of factors to determine the potential for affiliate abuse: transaction issues (purchases of power by the affiliate power marketer that would otherwise have gone to the public utility's ratepayers; or the public utility fails to compete with the power marketer); services provided on preferential basis (scheduling, accounting, legal or other services); power sales between affiliates not being at arm's-length and information exchange issues. All of these factors were present in the Enron, El Paso relationship in this case. As a result, it can only be concluded, that by virtue of the PCSA, Enron was affiliated with El Paso.

Commission determined that Bechtel had no control or decisionmaking authority concerning “the sale or transmission of electric energy from the facility.” The PSCA granted control or decisionmaking authority to Enron. *See also Idaho Power Company*, 74 FERC ¶ 61,149 at 61,525 (1996) (Commission satisfied Idaho Power had no control or decisionmaking authority over the operations of any jurisdictional facilities, since it will not undertake any power scheduling itself, and any modifications will be pursuant to explicit directions from the owner, and Idaho Power stated it will not be required to make economic decisions regarding such modifications). Staff is correct that these cases stand for the proposition that “control” includes the ability of one public utility to conduct power scheduling, such as determining the sales and purchases, for another public utility. Enron by virtue of the PSCA had decisionmaking authority to sell El Paso power when it was operating El Paso’s trading desk and it scheduled El Paso’s power at its own discretion. Enron could set the prices of wholesale electricity, and used El Paso’s marketing division to execute sales to itself.

105. Enron’s arguments are specious. In this case, Enron had decisionmaking authority over El Paso’s real-time trading desk. Enron decided how, when and to whom it bought and sold El Paso’s power. Additionally, it was Enron who set the price for these transactions. Enron controlled El Paso’s trading desk, 76% of the time, for five years. The evidence in this case also corroborates that Enron was in control during this time. For instance, El Paso employees turned off their computers when Enron was operating the trading desk; El Paso employees forwarded their phones to Enron’s Portland, Oregon office and went home. Ex. S-9 at p. 2 ¶ 3. The only thing El Paso established was the minimum price for power to be sold, and El Paso dispatchers had authority to reject schedules developed and altered by Enron, but only for reliability reasons. Exs. S-1 at p. 13; S-4 at pp. 24-25. Enron decided whether or not to enter into transactions, the counterparties and the price. Ex. S-9 at p. 3, ¶ 12(a). El Paso admitted that it could not reject transactions for economic reasons since the transactions occurred in real time. Exs. S-1 at p. 13. El Paso relinquished control or management of its trading desk (marketing division) by switching the phones to Enron.

106. Documentary evidence shows that Enron admitted it gained control of El Paso and this was part of a larger strategy to gain control of many resources in the West. Exs. S-27 at p. 40; S-34 at pp. 2-3. El Paso also admitted in documents that Enron benefits from the relationship by virtue of the information available to it regarding generation resources, specifically at Palo Verde and Four Corners. Ex. S-5 at p. 26.³² Enron changed its

³² Staff argues alternatively that Enron effectively acted as an EPE affiliate which created a changed circumstance warranting Commission notification. Staff avers the “effective affiliation” is supported by the degree and quantity of confidential and

competitive position in the generation market, and should have disclosed this fact to the Commission. Staff is correct that the profit-sharing arrangement for certain transactions can be analogized to limited ownership interests. Moreover, since the transactions took place in real-time, El Paso had no control over them, and could not undo a transaction for economic reasons.

107. Staff is also correct that the PCSA resulted in Enron engaging in self-dealing, and this warranted Commission notification due to a change in Enron's status reflecting a departure from the characteristics the Commission relied upon in approving its market-based rate authority. El Paso admitted that "circumstances existed during which Enron, acting on behalf of El Paso made sales to itself." Exs. S-37 at pp. 3-6; S-9 at p. 6; S-39 at p. 3 and S-40. The PCSA itself stated that transactions with third parties for the purchase of wholesale capacity and/or energy "may include EPMI, a wholly owned subsidiary of ECT." Ex. S-2 at p. 4. The facts developed in this case show that EPMI actually executed wholesale electricity transactions (both buying and selling) with itself on El Paso's behalf. Staff correctly points out that the type of self-dealing in this case is more blatant than affiliate abuse between two subsidiaries sharing the same parent. In this case the transactions between El Paso and Enron were not made at arms-length. Enron profit-shared in certain transactions. Thus, Enron had an economic incentive in the sale price it charged for El Paso's power.³³ The DC courts have stated that it is appropriate to inquire

proprietary information transferred and the aligning of business interests beyond that normally found in simple contractual relationships. First, Enron was privy to El Paso's thoughts and policies on establishing minimum wholesale power sale prices. Exs. S-2; S-9 at p. 1. Second, the business relationship had aligned financial interests. Originally there was a profit sharing program which was replaced, but Enron maintained a financial stake in El Paso's performance through the financial arrangements created for Enron as El Paso's scheduling coordinator into the Cal PX and CAISO. In the supplemental and ancillary services sales into the CAISO, Enron shared revenues directly with El Paso. Thus, Staff argues that due to the financial arrangements, Enron shared a commonality of business interests (common profit motive on specific transactions and in their dealings in the California market) and was a *de facto* affiliate. As a result, Enron effectively acted as if it were affiliated with El Paso. Due to the ruling above it is unnecessary to consider this very persuasive argument.

³³ As a result of Enron's lack of candor with the Commission, there were no measures in place to mitigate any adverse effects from these transactions. *Compare Heartland supra*, at 62,063 (Commission prohibits self-dealing between affiliates absent approval of measures to mitigate adverse effects).

into the motivations of, and alliances between, the sellers and the buyers to determine whether arms-length transactions have taken place.³⁴ The economic interests of Enron coincided with El Paso's.

108. Additionally the PCSA provided Enron with access to sensitive, competitive information which under normal circumstances El Paso would not have wanted its competitors to have. Ex. S-9 at p. 5 ¶ 14(b). This changed circumstance warranted Commission notification. Documentary evidence indicates that Enron admitted the information advantages generated by the PCSA. For instance, the PCSA "provides for constant monitoring of major generating assets in the SW, including Palo Verde nuclear plant." Ex S-5 at p. 17.³⁵ In a briefing paper dated August 1998, El Paso stated that "Enron benefits in that it has established an affiliation with a utility and the information it is privy to regarding the status of generating resources especially Palo Verde and Four Corners." Ex. S-5 at p. 26. El Paso stipulated that in 1999, Enron and El Paso "acknowledged that the primary benefit Enron obtained from their relationship was the information it received." Ex. S-9 at p. 5 ¶ 14(c).

109. Due to the arguments presented by Enron, the Morgan Stanley precedents have been analyzed. In *Morgan Stanley*, 69 FERC ¶61,175 at 61,694 (1994), the Commission required Morgan Stanley Capital to report business and financial arrangements between its affiliates and its customers and suppliers.³⁶ This was due to the Commission's concerns for reciprocal dealing. On rehearing, the Commission eliminated this requirement and provided guidance for determining "affiliation" under Part II of the FPA. The Commission stated in pertinent part: "[A]s the Commission explained in the November 8 Order, the Commission has required power marketers, as a condition of market approval, to report business and financial arrangements involving the marketer (or

³⁴ *Midwest Gas Users v. FERC*, 833 F.2d 341 (1987) (technically nonaffiliated parties may nonetheless have the potential to distort market forces).

³⁵ In order to guarantee a level playing field the Commission places information-sharing restrictions on affiliates. *Compare Duke Power, a Division of Duke Energy Corp.*, 84 FERC ¶ 61,235 at 62,200 (1998) (code of conduct limitations on disclosure of market information between affiliates).

³⁶ The Commission stated that in prior cases, it had required as a "condition of market rate approval, the reporting of business and financial arrangements involving the marketer or any entity affiliated with the marketer and the entities that buy from or sell power to the marketer." *Morgan Stanley*, 69 FERC at 61,694.

an affiliate of the marketer) and the entities that buy power from, sell power to, or transmit power on behalf, of the marketer.³⁷ “We have given careful consideration to the concerns voiced by MS Capital (and other power marketers) that the costs and burdens of the business and financial arrangements reporting requirements far outweigh any possible benefits of such reporting. We find that MS Capital has raised valid concerns as to, among other things, the breadth of such reporting requirement, the potentially impossible compliance burden” that the requirement imposes on marketers such as MS Capital that are ‘involved in numerous, disparate investments and business arrangements pertaining to thousands of different business matters,’ and the adequacy of the resulting data in detecting reciprocal dealing. On this basis, we conclude that the business and financial arrangements reporting requirement imposes costs and burdens on power marketers (in terms of compiling and filing the data) as well as on the Commission (in terms of reviewing the data for the purpose of detecting reciprocal dealing) that are not justified by the potential benefits of such reporting. As a result, although the possibility of reciprocal dealing remains a valid concern, we do not believe that the business and financial arrangements reporting requirement is an effective means of detecting such behavior by power marketers. Rather, we believe that this matter can be appropriately addressed through a complaint mechanism.”³⁸

110. In the Morgan Stanley rehearing order the Commission also provided guidance on the determination of affiliation (this was discussed above). In so doing the Commission stated that in the November 8 Order it had “directed MS Capital, as a condition to authorization to transact at market-based rates, to report, among other things, affiliation with any entity that owns generation or transmission facilities or inputs to electric power production, or affiliation with any entity that has a franchised service area.”³⁹ Language in this order is salient for purposes of this case. To wit, the Commission stated: “[w]e reiterate here our holding in the November 8, 2003 Order that, for purposes of complying with the requirement to report affiliation with any entity that owns generation or transmission facilities or inputs to electric power production, MS Capital ‘need not report the mere transitory holdings of its affiliates in electric facilities and inputs.’ 69 FERC at p. 61,695. However, MS Capital must ‘report all of its own investments in electric facilities and inputs.’ *Id.* As we stated in the November 8 Order, ‘there is no reason to ascribe generation ownership or control to MS Capital because of transitory holdings of

³⁷ 72 FERC at 61,435.

³⁸ 72 FERC at 61,436.

³⁹ *Id.*

electric utility stocks by Morgan Stanley in connection with investment or merchant banking, market-making, or asset management activities.’ *Id.* at p. 61,693.”⁴⁰ This language is significant for various reasons. First, it shows that Enron’s arguments concerning the Morgan Stanley case are erroneous. In that same case the Commission discussed the reporting requirements for affiliates based on market-based rate authority. Second, it supports the proposition that Enron had to report its affiliation with El Paso (an entity that owns generation). Enron’s involvement with El Paso was not transitory holdings of electric utility stocks by its affiliates in connection with investment or merchant banking, market-making, or asset management activities.

111. Staff correctly points out that *Morgan Stanley*⁴¹ did not eliminate the requirement that the PCSA be filed with the Commission. The *Morgan Stanley* decision did not remove the requirement that a power marketer inform the Commission of any change in status that would reflect a departure from the characteristics the Commission has relied upon in approving market-based pricing. In addition, *Morgan Stanley* did not change the substantive requirements that a power marketer disclose relationships with the potential for affiliate abuse, or take the necessary steps to prevent affiliate abuse. The only requirement eliminated by *Morgan Stanley* was the requirement to file all business and financial relationships with those entities in which they engage in wholesale power transactions. As Staff points out, under *Morgan Stanley*, a power marketer still had to notify the Commission of business arrangements that increase the amount of generation under its control, create new affiliations (actual or effective), create opportunities for self-dealing, and provides a constant stream of highly sensitive, competitive market information.

112. The record in this case supports the finding that Enron developed a business strategy to control and market power generated by numerous public utilities and qualifying facilities throughout the Western power grid. Exs. S-27 at pp. 39-43; S-34; S-35. As a result of these relationships Enron increased its presence in the market or its market share. As Enron documents demonstrate:

Gaining Control of Assets

Currently pursuing two strategies. The first is gaining control of a variety of small resources or capabilities around the west. For example, the combination of

⁴⁰ Morgan Stanley refers to any and all Morgan Stanley Group Inc. affiliates other than MS Capital. 72 FERC at 61,437 n. 13.

⁴¹ *Morgan Stanley Capital Group, Inc.*, 72 FERC ¶ 61,082 (1995).

El Paso Electric, Las Vegas cogen, Valley Electric, and Glendale joint venture provide us with a useful mix of loads and resources in the southwest. These transactions require relatively little capital, but will require automated IT links to customers and more people in the logistics group.”

Ex. S-34 at p. 3. The record evidence shows that many of these relationships involved service agreements with a number of entities. Ex. S-34 at pp. 5-6. Enron documents show that these were service deals including: Scheduling, Ancillary Services, General Management and Load/Resource Balance. Ex. S-34 at p. 18. The same records show Enron admitted it “touched/managed 3500 MW a day with no risk.” Ex. S-34 at p. 10.

113. Staff recommended that EPMI be ordered to disgorge all the profits it made above cost-based rates after executing the PCSA. According to Staff, Enron’s violation of its market-based rate authority is relevant to its total position in the western markets.⁴² Witness Barlow estimated that the profits Enron made for all WSPP transactions entered into by EPMI from 1997 through 2001 was \$124,727,794. Ex. S-50 at p. 5-6. The monies according to Staff should be paid to consumers adversely affected by the high energy prices that resulted from Enron’s misconduct. Tacoma supported Staff’s recommendation for West-wide disgorgement.

114. The California Parties argued that Enron should be ordered to disgorge all profits it earned under its market-based rate authorization or \$2.974 billion (from 1997 to 2001). Exs. CAL-11 at p. 6:8-7; CAL-12. In addition, they claim that the money should go to California, since California was the primary target of Enron’s conduct.

115. The conduct the Commission looked at in the designation order in this proceeding was the relationship between Enron and El Paso. As a result, the disgorgement of \$32,528,766 for transactions identified to have involved El Paso and Enron seems an appropriate remedy. Although Staff is correct that violation of market-based rate authority is a continuing violation which would permeate all transactions in the WSPP, the imposition of such a remedy seems outside of the jurisdictional parameters of this proceeding. Especially, in light of the fact that the Commission has ordered Enron to show cause why it should not be ordered to disgorge all profits it made involving a number of transactions which violated the CAISO and PX tariffs. The transactions involved in the Order to Show Cause proceeding include transactions at issue in this

⁴² Staff analogizes this situation to formula rate violations where the Commission has ordered refunds because the company failed to update its costs pursuant to a fuel clause in its tariff citing *Electric Cooperatives of Kansas*, 14 FERC ¶ 61,176 (1981).

proceeding. To wit, Ricochet. This proceeding thus, overlaps with the ongoing Order to Show Cause proceeding and the Commission will establish additional remedies for the same conduct in the Order to Show Cause proceeding. The remedy recommended here is in addition to the license revocation which has already been ordered by the Commission. *See Enron, supra*. Based on the evidence in this proceeding it is found that license revocation would have been an appropriate remedy for violation of market-based rate authority. Moreover, the Commission in a separate proceeding is looking into whether Enron's alliances/partnerships gamed the market in violation of the Cal PX, CAISO tariffs. This includes Enron's relationship with El Paso. *Enron Power Marketing, Inc.*, 103 FERC ¶ 61,346 at ¶ 39.⁴³

Issue C: Did Enron engage in unlawful actions (including but not limited to, unlawful practices or actions flowing from or enabled by its relationship with El Paso Electric Company "El Paso") to adversely affect prices and markets in the Western United States? What is the appropriate remedy if Enron engaged in unlawful actions?

A. Arguments of the Parties and Staff:

116. This issue was stipulated to before the Commission issued its most recent order to Show Cause. *American Electric Power Service Corp.*, 103 FERC ¶ 61,345 ("OSC"). The OSC proceeding includes conduct encompassed in Issue C in the current proceeding. Consequently, Enron's trading practices are being considered by the Commission in a separate proceeding. However, the parties' contentions in this proceeding are set forth below, in order to complete the record in this case.

117. Staff contends that Enron's traders engaged in marketing strategies which adversely affected California energy markets. Staff I.B. at p. 53. The two strategies at issue in this proceeding – "Ricochet" and "Fat Boy" or "Inc-ing" of load strategies – were facilitated, Staff asserts, by Enron's alliance with El Paso. This was possible, Staff argues, through Enron's control over El Paso's generation as well as Enron's use of El Paso's system to "park" energy. *Id.* According to Staff, El Paso admits that Enron used El Paso's power in transactions such as "Ricochet" and "Fat Boy." *Id.* Staff accuses

⁴³ "Enron and the other entities with whom it had partnership, alliance or other arrangements . . . appear to have jointly engaged in market manipulation schemes that had profound adverse impacts on market outcomes, and that violated the ISO and PX tariffs for which the monetary remedy of disgorgement of unjust profits and other appropriate, additional non-monetary remedies may be appropriate." *Id.* at ¶ 42.

Enron of using El Paso's system to park power in such a way as to violate transmission open access requirements, as well as using the "Ricochet" and "Fat Boy" strategies to violate the CAISO tariff. *Id.*

118. Staff asserts that Enron engaged in parking and lending not authorized under El Paso's Open Access Transmission Tariff ("OATT"), which facilitated other unlawful trading practices. Staff I.B. at p. 53. Enron convinced El Paso, Staff believes, to provide parking and lending service,⁴⁴ and subsequently used the service to engage in unlawful

⁴⁴ Staff explains parking and lending. Staff I.B. at pp. 54-55.

[P]arking and lending constitute transmission services, and involve more than the mere purchase or sale of electricity. Typically, a point-to-point customer is required to reserve transmission for a complete transaction, from an actual generator (the "source") to an actual power-consuming load (the "sink"). This rule can complicate the process for a power marketer wanting to engage in 'inter-temporal arbitrage, where the power marketer buys energy in the forward market, hoping to later resell that energy at a higher price.' A point-to-point customer – such as a power marketer – may be able to buy power but is unable to reserve the transmission if it has not yet identified a buyer and named its location on the grid. Also, the transmission customer may be able to sell power but has yet to identify from whom it will purchase the power to fill the contract. Under either scenario, because the point-to-point transmission customer would not know the sink or the source for the generation until sold or purchased in the real-time, it could be denied a reservation for firm transmission service.

As a control area/transmission owner, EPE solved this problem for Enron. When Enron bought power in the day-ahead market, EPE allowed Enron to 'park' the power on its system (call EPE the sink) for a negotiated fee until Enron sold the power in real-time. 'Lending' was the reverse of parking. When Enron sold power in the day-ahead market it hoped to fill with power it would buy in real-time, EPE allowed Enron to list EPE's system as the source of the power until Enron obtained the real source in real time the lending provider as the sources of the power. In real time, the lending customer goes out and purchases the actual power used to fill its initial sell obligation arranged in the forward market.

Id. (internal citations omitted).

and/or highly manipulative trading practices. *Id.* at pp. 53-54. Furthermore, Staff contends, Enron parked at a generator in a fashion prohibited by the Commission because the Commission had forbidden Enron from receiving transmission service not provided through the pro forma tariff without first petitioning the Commission. *Id.* at p. 54.

119. According to Staff, parking and lending are transmission services that could potentially hinder transmission reliability. Staff notes that Enron's witness Kee concedes this point. *Id.* at pp. 55-56. Staff insists that Enron could have obtained parking and lending services legitimately, but, instead, through the alliance, obtained an unduly preferential service not available to other parties in violation of the Commission's open access policies. *Id.* at p. 56.

120. Staff also accuses Enron of violating the marketing monitoring and information protocol contained in the CAISO and CAL PX tariffs by engaging in "Ricochet" and "Fat Boy" transactions. *Id.* at pp. 61-72. Enron's trading strategies, Staff insists, constitute both gaming and anomalous behavior under the marketing monitoring and information protocol, and, consequently, the Commission should demand a full accounting from Enron for all profits made from these trading strategies. *Id.* at p. 72.

121. Despite Enron's contention that Staff did not meet its evidentiary burden, Staff insists that it presented substantial evidence showing that Enron engaged in unlawful practices adversely affecting western power prices. Staff R.B. at p. 42.

122. The California parties agree with Staff's accusations against Enron. California I.B. at p. 26. Enron, the California parties insist, used its El Paso alliance to engage in "Ricochet" and "Fat Boy" transactions in the California markets. *Id.* Consequently, the California parties contend, prices were higher than they should have been. *Id.* Additionally, the California parties assert, Enron engaged in similar transactions with other parties resulting in a similar effect. *Id.* As "Ricochet" and "Fat Boy" transactions are violations of the CAISO tariff, the California parties maintain, Enron should disgorge all profits earned under its market based rate authority. *Id.* Furthermore, the California parties urge that a proper remedy for Enron's behavior must include a market wide remedy. *Id.* The California parties recommend that the market clearing prices between May 1, 2000, through October 1, 2000, must be reset to the level they would have been without market manipulation. *Id.*

123. Enron responds that there is no evidence demonstrating that any specific EPMI power sales or transmission transaction was unlawful or that any transaction had an adverse effect upon rates. Enron I.B. at p. 52. Also, Enron contends that without identification of specific transactions or harm to specific customers, it is impossible to determine that refunds to specific customers would be an appropriate remedy. *Id.* Staff,

Enron asserts, has not met its burden of demonstrating that the market was damaged by Enron's transactions. *Id.* Additionally, Enron claims evidence has not been produced which would allow quantification of a remedy for specific transactions. *Id.* at p. 55.

124. Parking, lending, and hubbing, Enron asserts, were services provided by El Paso and there is no evidence that Enron's purchase of these services was unlawful. Enron R.B. at p. 34. As for Staff's contention that certain CAISO tariff provisions were violated, Enron insists, this claim was made after the record was closed and is unsupported by any evidence. *Id.* at p. 36

B. Discussion:

125. This issue was stipulated before the Commission issued its most recent order to Show Cause. *American Electric Power Service Corp.*, 103 FERC ¶ 61,345 ("OSC"). The OSC proceeding includes conduct encompassed in Issue C in the current proceeding. As a result, it is not necessary to decide Issue C, since Enron's trading practices are being considered by the Commission in a separate proceeding.

126. However, it bears noting that this record supports the finding that Enron engaged in "Ricochet" activities. Ex. S-8. *See American Electric Power Service Corporation*, 103 FERC ¶ 61,345 at ¶ 39 (2003) ("Ricochet" or "Megawatt Laundering" is a gaming practice which violated the California ISO and California PX tariffs and warrants disgorgement of unjust profits).⁴⁵ The other conduct involved in this case "Inc-ing" or "Fat Boy" was determined by the Commission to violate the MMIP, but the Commission is not going to seek disgorgement of unjust profits for this practice. *AEP supra*, at 103 at ¶ 60.

127. Ricochet and Fat Boy were facilitated by Enron's alliance with El Paso, through the control of generation and the use of its system to "park" energy. Ex. S-9 at p. 6 ¶ 17(a); S-30 at p. 2; S-31. Enron used El Paso to park and lend generation without a Commission tariff. Witness Ballard provided evidence that parking and lending are "transmission services provided by control area operators through scheduling and operation of generation. Tr. at 381. Additionally, this witness testified that default can create problems for transmission reliability. Ex. S-45 at pp. 14-5. Finally, as Staff correctly argued, Enron obtained an unduly preferential service not made available to

⁴⁵ At least 36 transactions involving El Paso and Enron were likely Ricochet transactions. Exs. S-22 at 7:13-11:14; S-23; S-41 at 4:16-8:4; S-22 at 9:12-11:2.

others, contrary to the Commission's open access policies and Section 205 (b) of the FPA.⁴⁶

IV. CONCLUSIONS

128. Enron violated Section 205 (c) of the FPA. Enron should disgorge \$32,528,766 for this violation. Additionally, Enron violated its market based rate authority. Accordingly, for this violation, Enron's market-based rate authority should be revoked (which the Commission has already done in a separate proceeding).

Carmen A. Cintron
Administrative Law Judge

⁴⁶ Enron could have obtained the provision of this service through legitimate means by filing a section 206 petition to amend El Paso's OATT (or any other transmission providers' OATT) or El Paso could have filed a section 205 rate schedule to amend its OATT. See *Entergy Services, Inc.*, 92 FERC ¶ 61,108 at 61,398 (2000). Despite having been prohibited from designating a generation unit as a point of delivery, Enron engaged in this practice until 2001(a fictitious sink for generation). Exs. EPE-16 at 26-7; S-45 at 7; S-47; S-46 at 1. See *Wisconsin Power and Light*, 84 FERC ¶ 61,300 at 62,385 (1998); *Entergy Services, Inc.*, 91 FERC ¶ 61,151 at 61,565-66 (2000), affirmed *Enron Power Marketing Inc. v. FERC*, 296 F.3d 1148 (D.C. 2002).