

Background

2. Spot market sales in the CAISO and WECC markets outside of the CAISO are subject to a “soft” \$400/MWh bid and price cap, respectively.³ Sellers that exceed the \$400 bid or price cap must file cost justification within seven days after the end of the month in which the sale occurred.⁴

3. During 2006, as part of its on-going oversight responsibilities, the Office of Enforcement (OE) conducted a review of third quarter Electric Quarterly Reports (EQRs) to determine, among other things, whether the soft \$400/MWh bid/price cap had been exceeded by any EQR filers.⁵ This review revealed that several EQR filers had entered into transactions where the price at which they sold energy was in excess of the cap. In particular, Avista Energy, Inc. (Avista), Morgan Stanley Capital Group, Inc. (Morgan Stanley), and ConocoPhillips Company (ConocoPhillips) reported transactions that exceeded the soft bid/price cap at different times during the month of July 2006. This order addresses the filings that these three companies made in response to OE’s inquiries to provide justifications for exceeding the cap.

Avista Energy, Inc. (EL06-44-005)

4. OE’s review of Avista’s third quarter EQR filings indicated that Avista had reported a transaction that took place in July 2006 that was in excess of the \$400 price cap. OE staff contacted Avista to verify the accuracy of the filing. When Avista confirmed that the transaction had, in fact, taken place at a price above the cap, OE staff explained to Avista that it was required by the prior Commission orders to make a filing to cost justify any transaction that exceeded the cap within seven days of the end of the

³ 114 FERC at P 1.

⁴ 101 FERC at P 17, n.7.

⁵ The EQR is filed by public utilities and summarizes pertinent data about their currently effective contracts as well as data detailing power sales made during the reporting period. It is an important tool facilitating the Commission’s ability to monitor the market. *See Revised Public Utility Filing Requirements*, Order No. 2001, FERC Stats. & Regs. ¶ 31,127, *reh’g denied*, Order No. 2001-A, 100 FERC ¶ 61,074, *reh’g denied*, Order No. 2001-B, 100 ¶ 61,342, *order directing filing*, Order No. 2001-C, 101 FERC ¶ 61,314 (2002), *order directing filing*, Order No. 2001-D, 102 FERC ¶ 61,334 (2003).

month in which the transaction took place. On March 30, 2007, Avista submitted a letter describing the transaction in question, stating that it believed the price was cost justified.⁶

5. Avista states that the contract governing this particular transaction obligates Avista to provide hourly balancing energy to its customer. The transaction identified by OE staff took place on July 24, 2006, and, according to Avista's account, constituted a single transaction spanning a four-hour time period.⁷ Avista asserts that the energy commodity sold to its customer did not exceed the \$400 cap because the transaction included charges for losses, transmission and ancillary services. In other words, Avista claims that the energy price it charged was below \$400 and the cap was exceeded only when additional charges for delivering the commodity were added. Avista asserts the appropriate price to which the \$400 cap should apply in this type of transaction is the commodity price before the addition of transmission and related charges.

6. Avista's filing was published in the *Federal Register*, 72 Fed. Reg. 19,914 with motions to intervene or protest due on or before April 30, 2007. None was received.

Morgan Stanley Capital Group (ER07-516-000)

7. OE's review of Morgan Stanley's third quarter EQR filing indicated that it had reported two transactions that took place in July 2006 that were in excess of the \$400 price cap. OE staff contacted Morgan Stanley to verify the accuracy of the filing. When Morgan Stanley confirmed that the transactions had, in fact, taken place at a price above the cap, OE staff explained to Morgan Stanley that it was required by the prior Commission orders to make a filing to cost justify any transaction that exceeded the cap within seven days of the end of the month in which the transaction took place. On January 26, 2007, Morgan Stanley filed a response. Morgan Stanley requested confidential treatment of certain information provided because, according to Morgan Stanley, it is sensitive commercial and financial information that is privileged under 5 U.S.C. § 552(b) (4) and sections 1b.9 and 388.112 of the Commission's regulations.⁸

8. Morgan Stanley states that one of the two transactions at issue was a sleeve transaction, in which it served as a creditworthy intermediary between a power marketer and a seller. Morgan Stanley asserts that it sold the power for \$401/MWh, which

⁶ See Letter submitted by Avista Energy, Inc. on March 30, 2007, in Docket No. EL06-44-005.

⁷ *Id.*

⁸ We can address the issues here without disclosing the information. Thus, we need not decide the merits of the claim of confidentiality.

included a \$1/MWh assessment for the credit risk and administrative costs it accepted as part of the transaction.⁹ Morgan Stanley asserts that the \$1/MWh surcharge is just and reasonable because it is a reasonable approximation of the credit risk and administrative cost Morgan Stanley incurred for providing the sleeving service.

9. According to Morgan Stanley, the second transaction in question was entered into on the InterContinental Exchange (ICE), an electronic exchange that allows parties to enter into bilateral energy transactions, including spot power transactions. Morgan Stanley states further that it entered into the transaction in response to a blind bid on ICE seeking 200 MWs of super-peak power for delivery at Palo Verde at a price of \$475/MWh.¹⁰

10. Morgan Stanley claims that the sales price is just and reasonable because it agreed to the transaction at a price established by the buyer, which reflected the buyer's assessment of the current market price for power at that specific delivery point. Morgan Stanley asserts that because of the fact that the ICE trading process is conducted blindly, Morgan Stanley could not know the identity of the purchaser and had to choose to sell power to an anonymous buyer at the buyer's price or not meet the buyer's bid. Without conceding that the original sale price is not just and reasonable, and without prejudice to its right in the future to sell power at a price above the WECC soft cap, Morgan Stanley states that it will revise the price of the transaction to \$400, refile its EQR to reflect the revised price, and credit the difference to the buyer.

11. Morgan Stanley's filing was published in the *Federal Register*, 72 Fed. Reg. 8,722 with motions to intervene or protest due on or before March 2, 2007. None was filed.

12. OE staff's review of ICE data indicated that, contrary to Morgan Stanley's assertions in its January 26, 2007 filing that it responded to a bid, Morgan Stanley had, in fact, posted an offer on ICE to sell power at above the \$400 cap. Upon discovering this apparent discrepancy, OE staff contacted Morgan Stanley to share its findings.

13. After considering OE's information regarding the offer on ICE, on March 29, 2007, Morgan Stanley filed an amendment to its January 26, 2007 filing.¹¹ Morgan

⁹ See *Report of Morgan Stanley Capital Group Inc. Regarding Certain WECC Spot Transactions* at 3.

¹⁰ *Id.* at 5.

¹¹ Morgan Stanley requested confidential treatment of its entire March 29, 2007 submittal with the exception of the transmittal letter. Because the Commission needed to use information from that submittal to address the issue here, on May 15, 2007, pursuant to 18 C.F.R. § 388.112 (e), the Director of the Office of Enforcement sent Morgan

Stanley stated that a further review of its records revealed that certain statements in the January 2007 report were incorrect. Regarding the second transaction, conducted on ICE, Morgan Stanley stated that contrary to the explanation provided in its earlier filing, the transaction had in fact resulted from the buyer accepting an offer that Morgan Stanley had posted on ICE to sell 200 MW of super-peak power at \$475/MWh.

14. Notice of Morgan Stanley's March 29, 2007 filing was published in the *Federal Register*, 72 Fed. Reg. 17,150 (2007) with motions to intervene and protests due on or before April 19, 2007. None was filed.

15. As Morgan Stanley states that it has adjusted the transaction price to \$400 and credited the difference, this transaction is no longer an issue in this proceeding.

ConocoPhillips Company (EL06-44-004)

16. OE's review of ConocoPhillips' third quarter EQR filing indicated that it had reported four transactions that took place in July 2006 that were in excess of the \$400 price cap. OE staff contacted ConocoPhillips, a wholesale power marketer, to verify the accuracy of the filing. When ConocoPhillips confirmed that the transactions had, in fact, taken place at a price above the cap, OE staff explained to ConocoPhillips that it was required by the prior Commission orders to make a filing to cost justify any transaction that exceeded the cap within seven days of the end of the month in which the transaction took place. On February 15, 2007, ConocoPhillips filed a Request for Clarification or, in the alternative, Request for Waiver and Cost Justification. ConocoPhillips requested privileged treatment with respect to certain sensitive commercial, financial and transaction information, pursuant to section 388.112 of the Commission's regulations. ConocoPhillips filed a public version with the privileged information redacted and a non-public version.¹²

17. ConocoPhillips seeks clarification that the \$400/MWh soft price cap in California and in WECC does not apply to sales that result from the trading of basis differentials or

Stanley a letter notifying the company that it may be necessary to release the information so that the Commission can address Morgan Stanley's filing. The letter informed Morgan Stanley that the information might be made publicly available within five (5) calendar days from the date of the letter. On May 16, 2007, Morgan Stanley's counsel advised OE staff that Morgan Stanley did not oppose the release of the information and would not appeal the Commission's decision to do so. Accordingly, Morgan Stanley's request for privileged treatment of the March 29, 2007 submittal is rendered moot.

¹² We can address the issues here without disclosing this information. Thus, we need not decide the merits of the claim of confidentiality.

spreads on the ICE. In addition, ConocoPhillips requests waiver of the reporting requirement and cost justification requirements for the four transactions that occurred in July 2006 above the \$400/MWh cap.

18. ConocoPhillips argues that the four transactions it entered into should not be treated as wholesale sales subject to the \$400/MWh soft cap, and attempts to distinguish price differential trades made on ICE from traditional seller/buyer wholesale sales. ConocoPhillips states that traders do not submit bids to purchase or sell electricity at specific prices for wholesale sales. Rather, those sales occur on the basis of differentials or spreads on ICE. ConocoPhillips states that traders submit bids on price differentials or spreads at two different locations, explaining that if the differential occurs in the market, it triggers a purchase at the lower-priced location and a corresponding sale at the higher-priced location. ConocoPhillips concedes that sales above the soft cap may result depending on the underlying spot market prices at the higher priced location. ConocoPhillips argues that the price cap established by the Commission applies only to the submission of bids by generators to sell electricity at prices that exceed the applicable cap, and that this type of bid submission does not occur when a trader bids a basis differential on ICE. Thus, ConocoPhillips asserts that traders that enter into sales based on price differentials do not have the ability to manipulate or otherwise influence market prices.

19. Alternatively, ConocoPhillips requests that if the soft cap does apply to sales resulting from bidding price differentials on ICE, the Commission determine that the four sales made by ConocoPhillips are cost justified and requests waiver of the seven-day deadline to file the cost justification because it claims that it did not become aware that trading price differentials on ICE may implicate the soft price cap until it was contacted by OE staff.

20. Notice of ConocoPhillips' filing was published in the *Federal Register*, 72 Fed. Reg. 10,194 (2007), with motions to intervene and protests due on or before March 1, 2007. CAISO filed a late answer to the filing on March 12, 2007.

21. CAISO asserts that there is an inadequate record and insufficient notice to potentially interested parties for the Commission to find that the transactions are, or should be, exempt from the soft cap requirement. CAISO further recommends that the Commission undertake a thorough review of all transactions reported on ICE that exceeded the \$400 soft cap before making any determination regarding ConocoPhillips' request for clarification.

Commission Determination

22. The transactions in excess of the \$400/MWh soft cap, discovered by OE staff's EQR review, all took place in July 2006. The justifications filed by Avista, Morgan

Stanley, and ConocoPhillips, on March 30, 2007, January 26, 2007, and February 15, 2007, respectively, are months beyond the grace period extended by the Commission, *viz.*, that sales in excess of the bid/price cap are subject to justification and must be filed within seven days after the end of the month in which the excess sale occurred.¹³ In addition, none of the three companies made any effort to seek clarification until contacted by OE staff in late 2006.

23. The bid/price cap is an important tool in helping the Commission to ensure just and reasonable rates. It is important that all transactions exceeding the cap be justified in a timely manner. Accordingly, we find that Avista, Morgan Stanley and ConocoPhillips each failed to comply with our directive to make a filing to justify prices exceeding the \$400/MWh soft cap within seven days of the end of the month in which the transactions occurred. For these reasons, we will not address the merits of the companies' proposed justifications for the transactions in excess of the soft cap but, rather, reject the late filed compliance filings.

24. The inaccurate filing of information by Morgan Stanley is a matter we do not take lightly. We expect every filing, including every pleading, filed with us to be complete, accurate and truthful. In this regard, Rule 2005 of our Rules of Practice and Procedure expressly provides that every filing must be signed and that such signature constitutes certification that the signer has read the filing and knows the contents and that the contents are true as stated to the signer's best knowledge and belief. See 18 C.F.R. § 385.2005(a) (2003). We will not sanction Morgan Stanley for its inaccurate filing in this instance but caution against any such future carelessness.

25. We also reject the request for clarification or, in the alternative, waiver filed by ConocoPhillips. We recognize that ConocoPhillips believes that the transactions at issue were not subject to the soft cap and that, therefore, it was not required to file to justify exceeding the cap. We agree with CAISO, however, that this issue of interpretation would be better addressed in a proceeding in which all affected participants in the CAISO and WECC markets could participate. Therefore, if ConocoPhillips continues to believe that basis differential bids should not be subject to the \$400 soft cap, it should file a petition for declaratory order requesting such a finding.

26. This brings us to the matter of what, if any, sanction the Commission should impose on the companies for failing to comply with the requirement to file justification for exceeding the \$400 soft cap within seven days after the end of the months in which the relevant sales occurred. We have the authority to penalize companies failing to comply with our orders issued under part II of the Federal Power Act.¹⁴ We exercise our

¹³ 101 FERC ¶ 61,061 at P 17, n.7.

¹⁴ Under section 316A of the Federal Power Act, as amended by the Energy Policy

discretion, however, not to penalize or sanction the companies here for their failure to comply with the seven-day requirement. As an initial matter, we recognize that the seven-day requirement is not stated anywhere in the 2006 orders raising the original \$250 cap to \$400. Rather, it is found in a footnote in the 2002 order that established the \$250 cap, a footnote which in turn only referenced an earlier 2001 order.¹⁵ Imposition of a penalty under these circumstances seems disproportionate to the violation. Furthermore, no market participant appears to have been harmed by the actions of the companies; indeed, the CAISO was the only intervenor and it only addressed ConocoPhillips' request for clarification, not the underlying transactions. Nevertheless, the Commission will take this opportunity to reiterate that it holds sellers accountable for their adherence to the \$400 soft cap and the seven-day filing requirement to justify exceeding that cap as both are critical to ensuring that the sales rates continue to be just and reasonable. Accordingly, the Commission will consider penalizing or imposing some other appropriate monetary or other remedy on companies that fail to comply with these requirements in the future.

The Commission orders:

- (A) The filings made by Avista, Morgan Stanley, and ConocoPhillips, are hereby rejected, as discussed in the body of this order.
- (B) ConocoPhillips' request for clarification is denied.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

Act of 2005, failure to abide by Commission's directives could lead to the imposition of civil penalties up to \$1,000,000. *See* 16 U.S.C. § 825o-1 (b) (2004), as amended by Pub. L. No. 109-58, 119 Stat. 594, § 1284(e) (2005).

¹⁵ *See supra* note 4.