

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeen G. Kelly.

Investigation of Terms and Conditions of Public
Utility Market-Based Rate Authorizations

Docket No. EL06-16-001

ORDER DENYING REHEARING

(Issued April 17, 2006)

1. In this order, the Commission addresses the requests of parties seeking clarification or rehearing of the Commission's February 16, 2006 "Order Revising Market-Based Rate Tariffs and Authorizations" (February 16 Order).¹ The February 16 Order rescinded Market Behavior Rules 2 and 6 following the promulgation of new regulations prohibiting the employment of manipulative or deceptive devices or contrivances in wholesale electricity and natural gas transactions.² For the reasons discussed herein, we deny the requests for rehearing.

¹ *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 114 FERC ¶ 61,165 (2006).

² *Prohibition of Energy Market Manipulation*, Order No. 670, 71 Fed. Reg. 4244 (Jan. 26, 2006), FERC Stats. & Regs. ¶ 31,202, 114 FERC ¶ 61,047 (2006) (Order No. 670). Order No. 670 implemented new section 4A of the Natural Gas Act and new section 222 of the Federal Power Act, as added to the statutes by the Energy Policy Act of 2005 (EPAct 2005). See Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594 (2005), sections 315 and 1283, respectively. The Commission's new anti-manipulation rules are located in part 1c of the Commission's general regulations.

I. Background

2. On November 17, 2003, acting pursuant to section 206 of the Federal Power Act (FPA),³ the Commission amended all market-based rate sellers' tariffs and authorizations to include the Market Behavior Rules.⁴ One of the Market Behavior Rules, Rule 2, prohibited "actions or transactions that are without a legitimate business purpose and that are intended to or foreseeably could manipulate market prices, market conditions, or market rules for electric energy or electricity products." Actions or transactions explicitly contemplated in Commission-approved rules and regulations of an organized market, or undertaken by a market-based rate seller at the direction of a regional transmission organization (RTO) or independent system operator (ISO), however, were not violations of Rule 2. In addition, Rule 2 prohibited certain specific behavior: Rule 2(a) prohibited wash trades, Rule 2(b) prohibited transactions predicated on submitting false information, Rule 2(c) prohibited the creation and relief of artificial congestion, and Rule 2(d) prohibited collusion for the purpose of market manipulation.

3. On August 8, 2005, EPAAct 2005 became law. Section 1283 of EPAAct 2005 amended the FPA by adding section 222, which prohibits the use or employment of manipulative or deceptive devices or contrivances in connection with the purchase or sale of electric energy or transmission services subject to the jurisdiction of the Commission. FPA section 222 closely tracks the language in section 10(b) of the Securities Exchange Act of 1934 (Exchange Act),⁵ and specifically requires that the terms "manipulative or deceptive device or contrivance" are to be used "as those terms are used in section 10(b) of the Securities Exchange Act of 1934." On October 20, 2005, we issued a notice of proposed rulemaking to adopt new rules to implement the new statutory anti-manipulation authority.⁶

³ 16 U.S.C. § 791a *et seq.* (2000).

⁴ *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, "Order Amending Market-Based Rate Tariffs and Authorizations," 105 FERC ¶ 61,218 (2003), *reh'g denied*, 107 FERC ¶ 61,175 (2004), at Appendix A (Market Behavior Rules Order). The Market Behavior Rules Order was limited to conditioning existing and future grants of market-based rate authority, and did not deal with the merits of granting such authority in the first instance.

⁵ Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (2000).

⁶ *Prohibition of Energy Market Manipulation*, 113 FERC ¶ 61,067 (2005).

4. In an order dated November 21, 2005,⁷ the Commission proposed to rescind the Market Behavior Rules once we issued a final rule implementing FPA section 222 and had the opportunity to incorporate certain other aspects of the Market Behavior Rules in appropriate Commission orders, rules, and regulations. The Commission also requested comment on whether the Market Behavior Rules should be revised or rescinded. We noted that rescission of Rule 2 would be consistent with Congressional intent in EPAct 2005, and would simplify the Commission's rules and regulations, avoid confusion, and provide greater clarity and regulatory certainty to the industry, yet not eliminate beneficial rules governing market behavior.⁸

5. On January 19, 2006, the Commission issued Order No. 670 adopting a final rule modeled on Securities and Exchange Commission (SEC) Rule 10b-5.⁹ The new rule, along with an analogous rule applicable to natural gas, codified in new part 1c of the Commission's regulations, broadly prohibits fraud in connection with the purchase or sale of electric energy or transmission services, or natural gas or transportation services, subject to the jurisdiction of the Commission.¹⁰

6. The Commission then rescinded Market Behavior Rules 2 and 6 in the February 16 Order. We explained that rescission of Rule 2 was appropriate to avoid regulatory uncertainty and confusion, to assure that all market participants are held to the same anti-manipulation standard, and to provide clarity to entities subject to our rules and regulations. The Commission also found that rescission of Rule 2 will not dilute customer protection and is consistent with Congressional direction in EPAct 2005.¹¹

⁷ *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 113 FERC ¶ 61,190 (2005) (November 21 Order).

⁸ November 21 Order at PP 13-18. The Commission received 21 comments and four reply comments in response to the November 21 Order.

⁹ 17 C.F.R. § 240.10b-5 (2005).

¹⁰ 18 C.F.R. part 1c (effective January 26, 2006).

¹¹ February 16 Order at PP 25, 50, 54. Rule 6 was rescinded as no longer necessary. No party challenges the rescission of Rule 6.

II. Requests for Rehearing and Clarification

7. The Public Utilities Commission of the State of California (CPUC) and the California Electricity Oversight Board (CEOB) argue that the Commission committed legal error by rescinding Rule 2 because nothing in EAct 2005 mandated such a rescission. CPUC argues that rescission cannot be reconciled with the Commission's obligation to ensure that rates are just and reasonable, and that the Commission committed legal error by not first finding that former Rule 2 was unjust and unreasonable before rescission. CPUC also argues that the Commission lacks jurisdiction to rescind Rule 2, when orders relating to the promulgation of Rule 2 are currently under judicial review.

8. The New England Conference of Public Utility Commissioners, the Vermont Department of Public Service, and the Vermont Public Service Board (collectively, NECPUC), Transmission Dependent Utility Systems (TDUS), and the American Public Power Association, Transmission Access Policy Study Group, and the Sacramento Public Utility District (collectively, APPA) contend that a public utility with a market-based rate tariff may not use its market-based rate authority to intentionally or knowingly exercise market power. In addition, NECPUC, TDUS, and APPA seek clarification or rehearing that, if a public utility under its market-based rate intentionally or knowingly exercises market power, it will be subject to the full range of remedies (including disgorgement of profits) for charging rates that violate Commission statutes, rules, order, regulations, or tariffs on file.

9. CPUC and CEOB further express concern that the new anti-manipulation rule will not reach all of the conduct that had been prohibited under Rule 2. Like NECPUC, TDUS, and APPA, CPUC and CEOB also seek clarification or rehearing on the scope of remedies available for violations of the rules and regulations administered by the Commission. Finally, CEOB argues that rescission of Rule 2 is inconsistent with the retention and codification of other Market Behavior Rules.¹²

¹² Another party, Edison Mission Energy, Edison Mission Market and Trading, Inc., and Midwest Generation EME, LLC (Edison Mission), filed a request for rehearing but thereafter filed a notice of withdrawal of its request for rehearing. No party has opposed Edison Mission's notice of withdrawal. Accordingly, the withdrawal is effective pursuant to Rule 216 of the Commission's Rules of Practice and Procedure. 18 C.F.R. § 385.216 (2005).

III. Discussion

A. The Commission appropriately rescinded Rule 2 following the implementation of the Commission's new anti-manipulation authority

1. Requests for Rehearing

10. CPUC and CEOB argue that there is no evidence of Congressional intent in EAct 2005 to repeal Rule 2, stating that there is no reference anywhere in EAct 2005 to the Market Behavior Rules, and no reference in the legislative history of EAct 2005 evidencing any intent to repeal Rule 2.¹³ CPUC argues that nothing in EAct 2005 mandates that any and every Commission tariff, rule, or regulation addressing market manipulation in the energy markets must include the element of scienter that is required for a violation of section 10(b) of the Exchange Act.¹⁴ CEOB contends that Congress could have said the only type of illegal market manipulation is conduct that is intentional, *i.e.*, manipulative behavior with scienter, but did not impose that limitation on the definition of market manipulation.¹⁵

2. Commission Decision

11. At the outset it is important to recognize that Rule 2 and the Commission's new anti-manipulation rule have the same purpose—to prohibit manipulation of energy markets subject to the jurisdiction of the Commission. Before Congress enacted EAct 2005, we fashioned a market manipulation rule specific to certain jurisdictional entities, relying on our ability to place conditions on market-based rate authorizations. Passage of EAct 2005, however, brought about a fundamental change in circumstances because Congress specifically prohibited market manipulation by any entity in connection with a jurisdictional transaction, not just those entities over whom the Commission has rate jurisdiction. While the terminology differs between Rule 2 and our new anti-manipulation rule, both rules are aimed at market manipulation. Replacing the Commission's tariff-based prohibition of market manipulation appropriately implements Congressional intent.

¹³ CPUC at 4; CEOB at 4-5.

¹⁴ CPUC at 4.

¹⁵ CEOB at 5.

12. Congress directed that market manipulation includes the requirement of scienter, that is, intentional or reckless conduct.¹⁶ Therefore, CEOB's argument that Congress did not impose the requirement of scienter is without merit. The question is whether the Commission should retain two rules prohibiting manipulation, using two different standards of proof. In recognizing and adapting to the changed circumstances presented by EAct 2005, the Commission decided that it would promote regulatory certainty yet still assure customer protection to rely on the language of FPA section 222, which directs that the terms manipulative or deceptive device or contrivance be used as they are in section 10(b) of the Exchange Act. This approach applies a consistent standard of proof for market manipulation to all entities. Nevertheless, as we said in the February 16 Order, the Commission will continue to monitor wholesale markets as they evolve and will consider changes in our regulations as may be necessary to assure that wholesale markets are well-functioning and result in just and reasonable energy prices.¹⁷

13. CPUC's and CEOB's approach would subject market-based rate sellers to a different set of rules than other market participants. The Commission reiterates its concern about the potential for uneven application of anti-manipulation provisions based on whether an entity is a public utility engaged in jurisdictional transactions under the FPA or a "non-jurisdictional" entity, or whether an entity is a public utility selling under market-based rate authority or selling at cost-based rates.¹⁸ Congress barred

¹⁶ In new section 222 of the FPA, Congress used the terms "manipulative or deceptive device or contrivance" and directed that they be given the same meaning as used in section 10b of the Exchange Act. It is well settled that those terms require a showing of scienter, that is, an intent to deceive, manipulate or defraud. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 201 (1976); Order No. 670 at PP 52-53. Reckless conduct also satisfies the scienter requirement. *Id.* at P 53. Proof of scienter can be inferred from circumstantial evidence. *See Herman & Maclean v. Huddleston*, 459 U.S. 375, 390-91 n.30 (1983) ("proof of scienter required in [securities] fraud cases is often a matter of inference from circumstantial evidence"); *see also United States v. Flynn*, 196 F.3d 927, 929 (8th Cir. 1999) (upholding conviction in a SEC Rule 10b-5 securities fraud case, the court noted "[f]raudulent intent need not be proved directly and can be inferred from the facts and circumstances surrounding a defendant's actions"); *Wechsler v. Steinberg*, 733 F.2d 1054, 1058 (2d Cir. 1984) ("Proof of scienter need not be direct, but may be a matter of inference from circumstantial evidence").

¹⁷ February 16 Order at P 54.

¹⁸ *Id.* at P 21.

manipulation by “any entity” in connection with a jurisdictional transaction. Applying the same rule to all entities to determine whether market manipulation occurred is sound practice and is consistent with Congressional intent. This is not a situation in which different rules should apply depending on the regulatory status of a market participant.

14. In arguing that the Commission can retain the foreseeability standard of former Rule 2 despite Congress’ requirement of scienter in rules promulgated under FPA section 222, CPUC concedes that there is no authority on point showing that the analysis in the February 16 Order is flawed.¹⁹ CPUC nonetheless claims that “there is no reason why the Commission’s contention [that the foreseeability standard of former Rule 2 is inconsistent with Congressional direction in EAct 2005] should not be analyzed under the same standards that are used to analyze claims that Congress repealed a statute.” CPUC’s approach does not withstand scrutiny.

15. Congress required the terms “manipulative or deceptive device or contrivance” be used “as those terms are used in section 10(b) of the Securities Exchange Act of 1934.” The Supreme Court noted that “[t]he words ‘manipulative or deceptive’ used in conjunction with ‘device or contrivance’ strongly suggest that § 10(b) was intended to proscribe knowing or intentional misconduct . . . conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.”²⁰ The Commission has carefully considered the arguments raised by CPUC and CEOB but, in light of Congressional direction to follow precedent establishing that market manipulation under the Exchange Act requires scienter,²¹ and our desire to apply the new anti-manipulation rule uniformly to all entities, the Commission declines to retain former Rule 2’s foreseeability standard for determining whether conduct is manipulative under

¹⁹ CPUC at 4.

²⁰ *Hochfelder, supra*, 425 U.S. at 197. Further, Congress directed the Commission to use FPA section 222 as the basis of “such rules and regulations as the Commission may prescribe as necessary or appropriate” to protect electric ratepayers from market manipulation. FPA section 222(a).

²¹ *Hochfelder*, 425 U.S. at 214 (“[w]hen a statute speaks so specifically in terms of manipulation and deception, and of implementing devices and contrivances—the commonly understood terminology of intentional wrongdoing—and when its history reflects no more expansive intent, we are quite unwilling to extend the scope of the statute to negligent conduct”).

the FPA.²² The Commission's new anti-manipulation rule implements clear statutory authority prohibiting market manipulation, and while the new anti-manipulation rule, unlike Rule 2, requires a showing of scienter, it is a "catch-all" provision reaching all manner of fraud perpetrated by any entity in connection with a transaction subject to the jurisdiction of the Commission.

16. CPUC argues, as does CEOB, that Congress did not direct the rescission of former Rule 2 and, therefore, the Commission should not have rescinded Rule 2.²³ We disagree. We have acted consistently with Congress' direction by adopting a single prohibition of market manipulation based on the statutory authority in FPA section 222. We believe such uniformity will promote regulatory certainty while assuring customer protection. Furthermore, Congress knows how to ratify agency regulation, but elected not to ratify former Rule 2 or even use it as a model for its EAct 2005 legislation.²⁴ Instead, Congress gave the Commission new statutory authority to prohibit market manipulation pointedly modeled on section 10(b) of the Exchange Act.

B. Rule 2 was not a market power rule

1. Request for Rehearing

17. NECPUC, TDUS, and APPA request the Commission to clarify that the knowing exercise of market power by public utilities or their affiliates that hold market-based rate

²² CPUC further argues that the Commission can justify rescission of Rule 2 only if there is an irreconcilable conflict with the new anti-manipulation rule. CPUC at 6. This is not the case. The Commission is free to adopt such rules and regulations as will best implement our statutory authority. In this instance, we have determined that retaining Rule 2's foreseeability standard would be both inconsistent with and inappropriate in light of Congressional direction as expressed in FPA section 222.

²³ CPUC at 3-6; CEOB at 4-5.

²⁴ See, e.g., An Act to Ratify the Authority of the Federal Trade Commission to Establish a Do-Not-Call Registry, Pub. L. 108-82, 117 Stat 1006 (2003); *Mainstream Mktg. Servs. v. FTC*, 358 F.3d 1228, 1250 (10th Cir. 2004) (following Congressional ratification, "the FTC's statutory authority is now unmistakably clear"), *cert. denied*, 543 U.S. 812 (2004). We presume, of course, that Congress was aware of Rule 2 when it enacted FPA section 222 which, like Rule 2, is titled "Market Manipulation." *Goodyear Atomic Corp. v. Miller*, 486 U.S. 174, 184 (1988) ("We generally presume that Congress is knowledgeable about existing law pertinent to the legislation it enacts").

authority violates their market-based rate tariffs.²⁵ TDUS argues that former Rule 2 was a prohibition against the knowing exercise of market power.²⁶ NECPUC, TDUS, and APPA also request the Commission to direct public utilities and their affiliates to incorporate into their market-based rate tariffs a provision prohibiting the intentional or knowing exercise of market power.²⁷

2. Commission Decision

18. Former Rule 2 prohibited market manipulation. It did not prohibit market power. Rather, it focused on actions or transactions intended to manipulate market prices, conditions, or rules, not the existence or use of market power absent some manipulation.²⁸ If market power was used by a seller in connection with some scheme of manipulation, it was the act of manipulation that was the violation of former Rule 2, not the existence of market power. The same is true under the new part 1c anti-manipulation rule.²⁹

19. In the February 16 Order we said market power is a structural issue to be remedied, not by behavioral prohibitions, but by processes to identify and, where necessary, mitigate market power that a tariff applicant may possess or acquire.³⁰ This occurs in the screening process before the Commission grants an application for market-based rate authority, on consideration of changes in the seller's status or operations, and in the triennial review of market-based rate authorization, all of which are designed to assure just and reasonable rates. The Commission ensures that market rules governing

²⁵ NECPUC at 2; TDUS at 5, 7-10; APPA at 5.

²⁶ TDUS at 4.

²⁷ NECPUC at 3-4; TDUS at 5, 7, 10-16; APPA at 5.

²⁸ Apart from the express statement that Rule 2 prohibited manipulation, the specifically prohibited behaviors of Rule 2(a)-(d) all clearly involve fraud or deceit—wash trading, submission of false statements, creating artificial congestion, or colluding to manipulate.

²⁹ February 16 Order at PP 22-23.

³⁰ *Id.* at P 23. Similarly, adoption of Rule 2 was limited to placing an anti-manipulation condition on all new and existing market-based rate tariffs, and was not a review or reconsideration of the Commission's previous approval of market-based rate tariffs for qualifying sellers.

RTO/ISO-operated markets are designed to prevent the exercise of market power. In addition, the Commission requires RTOs and ISOs to have independent market monitors³¹ and Commission staff members observe and review energy market operations. It is our expectation that any market participant who becomes aware of market power abuse will bring such information to our attention. When market abuse or structural problems are detected, they can be addressed under FPA sections 205 or 206 to assure that reliance on market mechanisms produces just and reasonable rates.

C. Rescission of Rule 2 does not legitimize market manipulation or lessen the remedies at the Commission's disposal

1. Request for Rehearing

20. CEOB contends that limiting the Commission's ability to remedy market manipulation to those instances which involve scienter will operate to legitimize conduct which formerly was prohibited under Rule 2.³² CEOB further argues that non-intentional behavior which has a foreseeable manipulative impact on the market will no longer be remedied unless a market participant or ratepayer initiates a Section 206 proceeding, and contends this is an abdication of the Commission's duty under the FPA.³³

21. NECPUC, TDUS, and APPA argue that the rescission of Rule 2 could be interpreted to diminish the remedies available to the Commission.³⁴ They express concern that certain statements of the Commission in Order No. 670 could be construed to leave the exercise of market power as a problem to be remedied only prospectively by the filing of a complaint. Accordingly, NECPUC, TDUS, and APPA request the

³¹ In May 2005 the Commission issued a policy statement on market monitors which discussed, among other things, the important role organized market monitors perform in enhancing competitive markets. We noted that the market monitors' tasks include identifying ineffective market rules and tariff provisions and recommending changes to the RTO or ISO that will better promote competition and efficient market behavior. *Market Monitoring Units in Regional Transmission Organizations and Independent System Operators*, "Policy Statement on Market Monitoring Units," 111 FERC ¶ 61,267 at PP 2-4 (2005).

³² CEOB at 5.

³³ *Id.* at 5-6.

³⁴ NECPUC at 2-6; TDUS at 5-7, 16-18; APPA at 8-9.

Commission clarify that public utilities and their affiliates that violate their market-based rate tariffs and/or the FPA are subject to the Commission's remedial authority, such as disgorgement of profits, an obligation to provide refunds, and potential revocation or modification of their market-based rate authority.³⁵

22. CPUC seeks clarification on whether remedies, including retroactive refunds, are available for unjust and unreasonable rates that are not the result of fraud or deceit.³⁶ CPUC argues that the Commission may not arbitrarily restrict monetary remedies for violations of Commission rules and regulations.³⁷

2. Commission Decision

23. The Commission rejects CEOB's argument that the rescission of Rule 2 legitimizes certain manipulative market behavior. By modeling part 1c on SEC Rule 10b-5, we adopted a broad, "catch-all" anti-fraud provision. As we said in Order No. 670, if any entity engages in manipulation and the conduct is found to be "in connection with" a jurisdictional transaction, the entity is subject to the Commission's anti-manipulation authority.³⁸

24. In Order No. 670, the Commission also was careful to note that the specifically prohibited actions in Rule 2 (*i.e.*, wash trades, transactions predicated on submitting false information, transactions creating and relieving artificial congestion, and collusion for the purpose of market manipulation) all are prohibited activities under our part 1c regulations and are subject to sanctions and remedial action.³⁹ Furthermore, we have recognized that

³⁵ NECPUC at 3; TDUS at 7, 16-18; APPA at 3-9.

³⁶ CPUC at 11-12.

³⁷ *Id.* at 19-20.

³⁸ Order No. 670 at PP 21-23. CEOB's argument ignores Congress' definition of market manipulation. The terms "manipulative or deceptive device or contrivance" are "terms that make unmistakable a congressional intent to proscribe a type of conduct quite different from negligence." *Hochfelder*, 425 U.S. at 199. While our new anti-manipulation rule is a "catch-all" provision, "what it catches must be fraud." *Aaron*, *supra*, 446 U.S. at 705.

³⁹ Order No. 670 at P 59.

fraud is a very fact-specific violation, the permutations of which are limited only by the imagination of the perpetrator.⁴⁰ Therefore, we declined to adopt a list of prohibited activities because no such list could be all-inclusive.⁴¹ However, we noted that the absence of a list of specific prohibited activities does not lessen the reach of the new anti-manipulation rule, nor did we foreclose the possibility that we may need to amplify part 1c as we gain experience with the new regulations.⁴²

25. As to whether conduct not meeting the elements of market manipulation set forth in Order No. 670⁴³ will go unpunished, we note that we have many tools to deal with situations as they arise. Conduct that is not fraud or deceit, or otherwise does not meet the elements of the new anti-manipulation rule or other Commission rule, regulation, order, or tariff on file, but that nonetheless results in unjust and unreasonable rates can be addressed prospectively under FPA section 206 to modify rates that have become unjust and unreasonable. Accordingly, the rescission of Rule 2 does not lessen customer protection.

26. We disagree with NECPUC, TDUS, and APPA, all of whom contend that rescission of Rule 2 could be interpreted as diminishing remedies. All of our remedial powers remain intact. For instance, the Commission can order disgorgement of profits or restitution, and has the option of conditioning, suspending, or revoking market-based rate authority, certificate authority, or blanket certificate authority. The Commission retains full authority to order disgorgement of profits and other remedies, as appropriate, for the violation of any tariff, rule, regulation, or order. Accordingly, the Commission has the authority to order disgorgement of profits and other remedies, as appropriate, resulting

⁴⁰ February 16 Order at P 24.

⁴¹ *Id.*

⁴² After considerable experience with SEC Rule 10b-5, upon which our new anti-manipulation rule is modeled, the SEC expanded the original Rule 10b-5 to add a number of specific provisions describing prohibited conduct. *See* 17 C.F.R. §§ 240.10b-5-1 through 240.10b-5-14.

⁴³ Order No. 670 at P 49.

from violations of the new anti-manipulation regulations.⁴⁴ In addition, we now have significant civil penalty authority for FPA violations.

D. The Commission properly rescinded Rule 2

1. Request for Rehearing

27. CPUC argues that, in order to rescind Rule 2, the Commission must first establish that Rule 2 was unjust, unreasonable, unduly discriminatory, or preferential, citing *Atlantic City Elec. Co. v. FERC*, 295 F.3d 1 (D.C. Cir. 2002). This is required, CPUC argues, because the Commission made a determination in 2003 that the Market Behavior Rules were necessary to ensure that market-based rates are just and reasonable, that is, the product of competitive forces and thus in a zone of reasonableness.⁴⁵ To make a change now, CPUC claims, the Commission first must provide a rational basis that markets will produce just and reasonable rates without Rule 2.⁴⁶

28. CPUC further argues that rescission of Rule 2 is unlawful because the Commission lacks jurisdiction to rescind Rule 2 when orders relating to the promulgation of Rule 2 are currently under review in the United States Court of Appeal.⁴⁷

2. Commission Decision

29. The *Atlantic City* case relied on by CPUC is one of a series of cases that discuss the rights of public utilities and natural gas companies to file rate changes, and the procedures by which the Commission can require changes in rates not sought in the first instance by the filing company. In short, these cases stand for the proposition that when the Commission seeks to change an existing approved rate, or an unchanged part of an

⁴⁴ The Commission's discretion is at its zenith when determining the appropriate remedy for a violation of a tariff, Commission rule, regulation or order. *See Niagara Mohawk Power Corp. v. FERC*, 379 F.2d 153, 159 (D.C. Cir. 1967); *accord* 16 U.S.C. § 825h (2000); *Consolidated Gas Transmission Corp. v. FERC*, 771 F.2d 1536, 1549 (D.C. Cir. 1985); *Gulf Oil Corporation v. FPC*, 563 F.2d 588, 608 (3rd Cir. 1977), *cert. denied* 434 U.S. 1062, *reh'g denied*, 435 U.S. 981 (1978); *Mesa Petroleum Co. v. FERC*, 441 F.2d 182, 187-88 (D.C. Cir. 1971).

⁴⁵ CPUC at 8-9.

⁴⁶ *Id.* at 10-11.

⁴⁷ *Id.* at 3, 21.

otherwise changed rate, we must first show the existing rate or practice to be unjust, unreasonable, unduly discriminatory, or preferential before ordering the change.⁴⁸ The circumstances presented here, however, are substantially different.

30. In adopting the Market Behavior Rules in 2003, the Commission modified all electric sellers' tariffs and market-based rate authorizations on a prospective, blanket basis to incorporate basic "rules of the road" guiding sellers' conduct in competitive markets.⁴⁹ Similarly, the Commission here acted under FPA section 206 once again to modify sellers' tariffs prospectively. We placed all market-based rate sellers on notice in the November 21 Order that their tariff provisions may be changed prospectively in light of the new anti-manipulation rules implementing FPA section 222.⁵⁰ Then, in the February 16 Order, we determined that adoption of the new anti-manipulation rule meant that it was no longer necessary or advisable to maintain Rule 2 in sellers' market-based rate tariffs.⁵¹ In this case, we find Rule 2 to be unjust, unreasonable and unduly discriminatory because of the regulatory uncertainty and inconsistency that would result from having two anti-manipulation rules, applying to different universes of sellers and with two different standards of proof. The Commission's goal is to promote regulatory certainty and protect customers by applying a uniform prohibition of market manipulation to all entities. Therefore, the Commission finds the new anti-manipulation rule to be the just and reasonable replacement for Rule 2.

31. Unlike the situation in *Atlantic City* and its predecessors, the 2003 Market Behavior Rules Order did not "deny a utility the right to file changes" or "force public utilities to file particular rates."⁵² Rather, we set out a framework of appropriate behavior

⁴⁸ See, e.g., *Western Resources, Inc. v. FERC*, 9 F.3d 1568, 1578 (D.C. Cir. 1993); *Public Service Commission of New York v. FERC*, 866 F.2d 487, 488-89 (D.C. Cir. 1989); *Northern Natural Gas Co. v. FERC*, 827 F.2d 779 (D.C. Cir. 1987) (en banc); *Sea Robin Pipeline Co. v. FERC*, 795 F.2d 182, 183 (D.C. Cir. 1986); *ANR Pipeline Co. v. FERC*, 771 F.2d 507, 513-14 (D.C. Cir. 1985).

⁴⁹ Market Behavior Rules Order at P 2; February 16 Order at P 3.

⁵⁰ November 21 Order at PP 1, 12-18.

⁵¹ February 16 Order at P 21.

⁵² *Atlantic City*, 295 F.3d at 10. See also *Sea Robin*, 795 F.2d at 187; *ANR Pipeline*, 771 F.2d at 513-14.

in energy markets, including a prohibition of market manipulation, in which sellers were authorized to sell at market-based rates based on findings that the sellers did not have, or had adequately mitigated, market power. The case relied on by CPUC, on the other hand, dealt with the issue of whether the Commission could require a public utility to give up its FPA section 205 filing rights. The *Atlantic City* line of cases is simply inapposite to the circumstances under which we adopted the Market Behavior Rules in 2003.

32. Nor has the Commission rescinded Rule 2 without justification, as CPUC claims.⁵³ To the contrary, and as discussed earlier, the Commission responded to significant changed circumstances by adopting a new anti-manipulation rule following the direction of Congress. Rescission of Rule 2 does not leave a regulatory gap. To the contrary, the new anti-manipulation rule applies to the conduct of all entities, not just market-based rate sellers, and catches all manner of fraud in connection with transactions subject to the jurisdiction of the Commission. The changed circumstances and reasons for shifting to the new, statute-based rule were discussed both in the November 21 Order and the February 16 Order.⁵⁴ Moreover, concurrent with the February 16 Order, we codified Market Behavior Rules 1, 3, 4, and 5 in part 35 of our regulations, without substantive change. These rules, in combination with the new anti-manipulation rule in part 1c of our regulations, provide the same basic framework for sellers' conduct in competitive markets as was provided by the Market Behavior Rules.

33. We also reject CPUC's argument that the Commission lacked jurisdiction to rescind Rule 2.⁵⁵ The petitions for review before the United States Court of Appeals for the District of Columbia Circuit in *Cinergy Marketing & Trading, L.P. v. FERC, et al.*, Nos. 04-1168, *et al.*, give the Court "exclusive" jurisdiction "to affirm, modify, or set aside" the orders adopting the Commission's Market Behavior Rules.⁵⁶ The pending appeal does not, however, prevent the Commission from deciding, as we did in the February 16 Order, to rescind rules prospectively based on a new record in a newly

⁵³ CPUC at 10-11.

⁵⁴ November 21 Order at PP 10-18; February 16 Order at PP 21-25.

⁵⁵ CPUC at 21.

⁵⁶ 16 U.S.C. § 8251(b) (2000).

instituted proceeding.⁵⁷ Moreover, this proceeding is at its core a rulemaking for electric market-based rate sellers, not an adjudication in which parties have specific rights and as to which the decision on the underlying record, once filed with the court, cannot be changed by the agency.⁵⁸

E. Rescission of Rule 2 is consistent with the codification of Market Behavior Rules 1, 3, 4, and 5

1. Request for Rehearing

34. CEOB contends that the Commission's rationale for codifying former Market Behavior Rules 1, 3, and 4 applies equally to the retention and codification of Rule 2. CEOB argues that, like Market Behavior Rule 1, codifying Rule 2's prohibition of manipulative conduct would reinforce the ethical and legal obligations of each market participant.⁵⁹ Similarly, CEOB notes that we concluded Market Behavior Rule 3 applies to all communications and not just those that are material in the furtherance of a fraudulent or deceptive scheme. CEOB argues that, like Rule 3, Rule 2 is broader than the new anti-manipulation rule because it also covers a second type of conduct: market manipulation which is foreseeable but not an intentional deception or manipulation.⁶⁰

⁵⁷ See *Alabama Power Co. v. FPC*, 511 F.2d 383, 388 (D.C. Cir. 1974) (distinguishing a case where the Commission seeks to alter its findings on a prior record, which it cannot do pending appeal without permission from the court, from one in which, as here, "what is sought is a change of policy, to be effected by promulgation of a new general regulation"); see also *Chamber of Commerce v. SEC*, No. 05-1240 (D.C. Circuit April 7, 2006) (following *Alabama Power* and noting that an agency has the authority to consider whether to modify a rule on appeal, thus "allowing an agency broad scope to carry out its mission").

⁵⁸ In the February 16 Order we specifically recognized that this proceeding is a "rulemaking seeking comment from all interested entities." February 16 Order at P 12, n.14, citing *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, "Order Addressing Application of *Ex Parte* Rule and Requests for Extension of Time," 104 FERC ¶ 61,132 at P 5 (2003).

⁵⁹ CEOB at 7.

⁶⁰ *Id.*

And CEOB argues that Market Behavior Rule 4 was intended to reinforce the importance of existing Commission policy on price reporting and duplicates strictures in FPA Section 221.⁶¹

2. Commission Decision

35. As discussed earlier, there has been a fundamental change in circumstances with regard to the prohibition of market manipulation. FPA section 222 directs that market manipulation requires a showing of scienter and, based on that direction, CEOB's argument that we can prohibit market manipulation which is foreseeable, but not an intentional or reckless deception or manipulation, is inconsistent with FPA section 222. Without the requisite intent or recklessness, conduct cannot be manipulative under FPA section 222.

36. The non-manipulation provisions of the Market Behavior Rules, specifically Market Behavior Rules 1, 3, 4, and 5, were not affected by EAct 2005, and therefore, codification of those rules is appropriate.

IV. Conclusion

37. The Commission acted promptly to implement the FPA section 222 anti-manipulation authority and then to conform its rules and regulations to the new anti-manipulation rule. The rescission of Rule 2 is consistent with the new statutory scheme, avoids the confusion of duplicative rules governing the same conduct, and provides greater clarity and certainty to energy markets. At the same time, the Commission's powers, including the new civil penalty authority, give the Commission a wide range of options to address market participants' behavior as energy markets evolve and to ensure open and competitive markets.

⁶¹ *Id.* at 8. FPA section 221 prohibits filing false information on electricity prices to Federal agencies. EAct 2005, section 1282. Rule 4, now codified in 18 C.F.R. § 35.37(c), requires accurate reporting of price information to price index publishers. There is no duplication of FPA section 221 in now-codified Rule 4.

The Commission orders:

The requests for rehearing of the February 16 Order are denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.