PROJECT NO. 40073

RULEMAKING TO IMPLEMENT HB 2133 BY AMENDING PUC SUBST. R. §25.503 AND PUC PROC. R. §22.246	**§ § §**	**PUBLIC UTILITY COMMISSION OF TEXAS**

ORDER ADOPTING AMENDMENTS TO §22.246
AS APPROVED AT THE OCTOBER 12, 2012 OPEN MEETING

The Public Utility Commission of Texas (commission) adopts amendments to §22.246, relating to Administrative Penalties, with changes to the proposed text as published in the May 11, 2012 issue of the *Texas Register* (37 TexReg 3483). The purpose of these amendments, coupled with substantive amendments proposed to §25.503, is to establish procedures to return excess revenues to affected wholesale electricity market participants when the commission has ordered disgorgement of those excess revenues in an enforcement proceeding. The passage of HB 2133 in the 82nd legislative session required the commission to adopt rules to establish such a procedure. The amendments constitute a competition rule subject to judicial review as specified in PURA §39.001(e). Project Number 40073 is assigned to this proceeding.

The commission received comments on the proposed amendments from the Alliance for Retail Markets (ARM); City of Austin d/b/a Austin Energy (Austin Energy); Luminant Energy Company LLC and Luminant Generation Company LLC (Luminant); NRG Energy, Inc. (NRG); Steering Committee of Cities Served by Oncor (Cities); Texas Competitive Power Advocates (TCPA); Texas Electric Cooperatives, Inc. (TEC); Texas Industrial Energy Consumers (TIEC); and TXU Energy Retail Company LLC (TXU Energy).

ARM was composed of Constellation NewEnergy, Inc./StarTex Power; Direct Energy, LP; and Gexa Energy, LP.

Proposed Subsection (b)

TEC requested that the commission consider whether the definition of affected wholesale electric market participants in proposed subsection (b)(1) would enable the return of disgorged excess revenues to other wholesale market participants on a case by case basis as contemplated by proposed subsection (j). TEC noted that the restrictive definition proposed refers only to entities that sell energy to retail customers; such entities are referred to as load serving entities (LSE) in the ERCOT Protocols. TEC stated that there may be wholesale market participants other than LSEs who are adversely affected by wholesale market violations and thus, it may be appropriate in certain circumstances for the commission to recognize non-LSE wholesale market participants when returning disgorged revenues to the market. TEC believed that recognizing such non-LSE wholesale market participants would be possible under the case by case approach, but the definition proposed in subsection (b)(1) may constrain the commission's ability when refunding disgorged revenues as PURA §15.025 only allows refunds to affected wholesale electric market participants and the commission has defined such as LSEs. TEC recommended that the commission clarify how other wholesale market participants that are properly entitled to receive disgorged revenues will be determined and defined.

Commission Response

The commission understands that market participants beyond the scope of the proposed definition in subsection (b)(1) may be affected by wholesale electric market violations.

Therefore, the commission clarifies, as requested by TEC, that the rule allows the commission to recognize wholesale electric market participants that do not serve retail load when allocating disgorged excess revenues in a subsequent proceeding. HB 2133 requires excess revenues ordered disgorged to be returned to affected wholesale market participants to be used to reduce costs or fees incurred by retail electric customers. The commission believes that proposed subsection (j) grants the commission broad flexibility to open a subsequent proceeding when it determines other wholesale electric market participants are affected or a non-standard distribution method is appropriate. Other wholesale market participants that are properly entitled to receive disgorged revenues will be determined in the subsequent proceeding. However, market participants who do not serve load at retail are not eligible to receive disgorged funds if they are unable to use such funds to reduce costs or fees incurred by retail electric customers. Parties in the subsequent proceeding would not be limited to the parties in the penalty or disgorgement proceeding. The commission believes the definition of affected wholesale electric market participants is appropriate as proposed and declines to adopt amendments to the definition based on the comments of TEC.

Luminant requested that the commission revise the definition of affected wholesale electric market participant in proposed subsection (b)(1) to remove the affiliate exclusion. Luminant stated that HB 2133 is clear in that any excess revenue ordered disgorged shall be returned to the affected wholesale electric market participants to be used to reduce costs or fees incurred by retail electric customers. Excluding affiliates would unreasonably discriminate against certain retail electric customers merely because they choose a REP affiliate of a company ordered to

disgorge excess revenue. Luminant stated that so long as affiliated companies are able to demonstrate that the refunded monies have been used to reduce costs or fees incurred by retail electric customers, the statutory mandate is achieved. Luminant noted that implementation and monitoring of such a commitment could be overseen by the independent organization charged with distributing the disgorged excess revenues. Luminant recommended striking the affiliate exclusion from proposed subsection (b)(1).

Cities commented that Luminant's request to remove the affiliate restriction from the definition of affected wholesale market participant underscores the importance of its recommendation that the rule expressly require disgorged funds to be used to reduce the fees and charges paid by retail electric customers. Cities stated that otherwise, disgorged funds may stay within the corporate family of the entity from which funds are disgorged, making a disgorgement penalty completely ineffectual. Cities commented that it did not object to Luminant's proposed language, provided that its own language regarding the use of the disgorged funds as provided in comment regarding substantive amendments to §25.503 are also adopted.

Commission Response

The commission agrees with Luminant that the definition of affected wholesale electric market participants should include affiliates of the person found in violation and that HB 2133 is clear that any excess revenue ordered disgorged shall be used to reduce customer costs and fees. HB 2133 requires the commission to adopt rules prescribing how disgorged excess revenues should be returned to affected wholesale electric market participants. The commission agrees with Cities that disgorged funds should not stay within the corporate

family of the person from which excess revenue is disgorged, as such would render a disgorgement order partially ineffectual. However, the commission believes that the requirement in HB 2133, that any excess revenue ordered disgorged shall be used to reduce customer costs and fees, prevents the excess revenues given to affiliate from remaining within the corporate structure. Therefore, the commission believes the exclusion of affiliates from the definition of affected wholesale electric market participants is unnecessary and amends the proposed definition of "affected wholesale electric market participant."

Proposed Subsection (e)

NRG noted that under the proposed rule, the report regarding a violation or continuing violation can be issued at any time after the action or decision precipitating the investigation has occurred. NRG stated that the competitive market is harmed by the regulatory uncertainty surrounding a pending investigation as market participants do not know whether certain actions would be considered abuse of market power. NRG stated that regulatory certainty is critical to the success of the competitive market and allows for more reasonable ERCOT fees and market participant costs, as well as encourages capital market investment. NRG noted that regulatory certainty also serves to inform market participants of the rules under which they may operate and allows them to conduct business with as few qualifications as possible. An investigation into market power abuse by definition disrupts market certainty. NRG feared that years after an action or decision by a market participant, the commission could commence an investigation which would potentially lead to disgorgement of revenues. As proposed, once an investigation begins there is no timetable to notice the market participant of when the investigation may have concluded or

what would lead to further action. NRG commented that open ended timelines would require market participants to keep their books and records open, which could impact the ability and cost of participants to transact business.

NRG recommended a sufficient but finite timeframe within which the Executive Director Report must be issued and proposed that the report be issued within two years of the decision or action that lead to the investigation. NRG commented that two years is sufficient time to conduct an in-depth analysis for the purpose of deciding whether penalties will be proposed and it is only fair to affected parties to know within some finite point in time that actions taken and decisions made are no longer actionable. NRG stated that should the report of violation recommend formal proceedings and an administrative penalty or disgorgement of excess revenue, the ensuing investigation and hearing process would not be subject to time constraints. NRG provided language amending subsection (e) with its proposed time constraints.

In the reply period, Luminant supported NRG's proposal to limit the issuance of a report of violation to within two years of the date of the alleged violation or start of the continuing violation. Luminant agreed with NRG that a two-year limitation is reasonable.

Cities disagreed with Luminant and NRG. Cities noted that HB 2133 did not contain language imposing a time limit on the executive director in which it must be reported that a violation has occurred and such a time limit could present implementation problems. Cities commented that it is unclear exactly when the two years would apply if the violation at issue is a continuing violation or was difficult to identify. Further, Cities noted that there is no showing that the

proceedings anticipated in HB 2133 will drag on inexorably and, if extensive proceedings become a problem in the future, the commission may address the issue at that time. Cities stated that NRG's proposal should be rejected but, if the commission determines that such a limitation is appropriate, recommended that the two year window start at the time the executive director is made or becomes aware of a violation taking place. Cities proposed alternative language that would clarify this intent, but reiterated that such a time limit is unnecessary and not supported by statute.

Commission Response

The commission disagrees with Luminant and NRG that the executive director should face time limitations when issuing a report of violation or continuing violation. The commission agrees with Cities that HB 2133 did not impose a time limit on reporting that a violation has occurred and such a time limit could present implementation problems. Regulatory certainty for the market as a whole should not be challenged by a pending investigation into either market power abuse, or wholesale electric market violations of other PURA sections, commission rules, or wholesale electric market protocols. Market participants are responsible for understanding the rules under which they may operate and conduct business. HB 2133 granted the commission authority and discretion to pursue disgorgement without limiting such authority based on a presupposed timeframe. The commission will use discretion to determine, on a case-by-case basis, whether disgorgement is an appropriate remedy for any applicable wholesale electric market violation. The commission declines to adopt the amendments proposed by NRG.

TEC recommended that changes be made throughout proposed subsection (e) to maintain consistent terminology throughout the section. TEC specifically identified several necessary changes that would conform the reference to a penalty in the report of violation to an administrative penalty separate from a recommendation that excess revenue be disgorged.

Commission Response

The commission agrees with TEC and adopts the clarifying amendments to subsection (e) as proposed.

Proposed Subsection (f)

Luminant recommended clarifying proposed subsection (f)(3) so that a person may submit a written request for hearing on any or all of the following, including the occurrence of the violation or continuing violation, the amount of the administrative penalty, and the amount of disgorged revenue, if applicable.

Commission Response

The commission agrees with Luminant and adopts the recommended clarifications to subsection (f)(3) as proposed.

Proposed Subsection (h)

Luminant recommended that proposed subsection (h) be revised to require that the SOAH administrative law judge, in issuing a proposal for decision, make specific fact findings establishing whether the market entity acted with the requisite intent and thus whether

disgorgement is appropriate. Luminant's proposed language was consistent with conforming recommendations made under proposed subsections (b), (i) and (j), along with similar comments made in regards to proposed amendments to §25.503.

Commission Response

The commission disagrees with Luminant that a wholesale electric market violation of PURA sections other than as mandated by statute for PURA §39.157, commission rules, or wholesale electric maker protocols should require a specific fact finding establishing affirmative intent or reckless disregard prior to establishing whether disgorgement is appropriate. The commission maintains that HB 2133 granted the commission the discretion to determine, on a case-by-case basis, whether disgorgement is an appropriate remedy for any applicable wholesale electric market violation. The commission therefore declines to adopt the amendments proposed by Luminant.

Proposed Subsection (i)

Luminant recommended language that would amend proposed subsection (i) so that parties to a proceeding are limited to the person who is alleged to have committed the violation or continuing violation and the commission, including the independent market monitor.

Commission Response

The commission agrees with Luminant. A market participant is alleged to have committed a violation or continuing violation pending the approval of settlement documents or a decision following an administrative hearing. The recommendation also conforms

proposed subsection (i) to similar language previously adopted by the commission under §22.246(e)(2). The commission adopts the amendments proposed by Luminant in subsection (i).

Austin Energy and TIEC requested clarifications regarding the limitations of parties to participate in a subsequent proceeding to determine an alternative allocation under proposed subsection (j) should the commission determine such a proceeding is appropriate. Austin Energy stated that intervention in a subsequent proceeding should not be restricted in the same manner as the original administrative proceeding. Austin Energy proposed language under a new subsection (k) that would explicitly allow any affected market participant to intervene to protect its interest in a proceeding relating to the distribution of disgorged excess revenues.

Though it opposed permitting the commission the ability to open a subsequent proceeding to determine a method of returning disgorged revenues, TIEC stated that clarifications to proposed subsection (i) are needed if the provision is retained. TIEC commented that all affected wholesale market participants should be able to intervene in the subsequent proceeding to determine the distribution methodology under proposed subsection (j) and recommended language to make the clarification.

Commission Response

The commission agrees with Austin Energy and TIEC that clarifications are needed regarding participation in a possible subsequent allocation proceeding as contemplated by proposed subsection (j). HB 2133 amended PURA §15.024(f) to limit the parties to a

proceeding under that subchapter to the alleged violator and the commission, including the independent market monitor. HB 2133 also required the commission to adopt rules describing how any disgorged excess revenues shall be returned to affected wholesale electric market participants. The commission believes that the limitation on participation in the administrative proceeding in which disgorgement may be ordered is separate from any separate proceeding the commission could open to decide on the allocation of such funds to the wholesale electric market. The commission appreciates the clarifying amendments proposed by both Austin Energy and TIEC. The commission believes that clarifications recommended by TIEC best reflect the intent of subsection (i) and therefore adopts its amendments in subsection (i) as proposed.

Proposed Subsection (j)

NRG, TCPA, and TIEC requested that the provision allowing a subsequent proceeding to determine if other wholesale electric market participants are affected or a non-standard distribution method is appropriate be struck.

TCPA stated that, as proposed, subsection (j) adds a layer of unnecessary complexity and delay to the disgorgement process. TCPA commented that the proposed rule does not comport with the intent of HB 2133 as the independent system operator is only required to distribute disgorged revenues to LSEs. TCPA believed that revenues returned to LSEs are unlikely, or at the very least, highly uncertain to reduce costs or fees to retail customers as the LSE is under no obligation to credit such customers any of the returned funds. Further, TCPA noted that LSEs do not constitute all affected wholesale electric market participants. In a situation where

generator purchased replacement power during an interval in which a violation occurred, the generator would not be eligible to receive any of disgorged funds. TCPA stated that allowing the commission to open a subsequent proceeding should it determine other wholesale electric market participants are affected, or a different distribution method is appropriate, is an inadequate and unworkable remedy. Specifically, TCPA commented that because PURA explicitly excludes affected parties other than the accused from participating in an administrative penalty proceeding, other market participants who may have been affected by the violation would have no opportunity to assert or demonstrate that they have been affected. The commission would have to come to the conclusion such parties were affected without any direct input from the parties, and the subsequent proceeding would likely be long, drawn out, and expensive. TCPA stated that a subsequent proceeding would discourage participation by some affected wholesale market participants, delay the return of the disgorged revenues to affected parties, and delay relief to retail customers.

Cities commented that TCPA's suggestion that an affected generator buying replacement power from ERCOT qualifies to receive disgorged funds should not be taken into consideration as it is unclear how disgorgement of funds to generators could ensure that retail electric customers receive a reduction in the costs or fees they pay for electric service.

NRG stated that the load ratio share allocation is a fair and expedient method of distributing disgorged revenues. NRG commented that the possibility of straying from this allocation in order to track specific market participants to the time the violation occurred would be administratively cumbersome, expensive and would not necessarily accomplish a more exact

allocation. NRG stated that with a subsequent proceeding, the independent system operator would have to research and reconfigure its allocation based on whatever method was ultimately selected by the commission, increasing administrative costs. Further, NRG commented that the subsequent proceeding and hearing would likely be a waste of resources with little or no benefit to the market and would delay conclusion of the matter. Since hearings would be limited to the alleged violator and the commission, wholesale market participants that could have been affected by the violation may not be able to participate in any proceeding initiated under the pertinent subchapter. NRG questioned how a subsequent proceeding could be accomplished under HB 2133 and recommended the use of load ratio share allocation in all circumstances. NRG provided language amending subsection (j) to remove the option for a subsequent proceeding.

Similarly, TIEC stated that the load ratio share allocation in proposed subsection (j) is both appropriate and consistent with requirements adopted under HB 2133. TIEC commented that this allocation would properly remit disgorged revenues to LSEs in proportion to the harm each sustained as a result of the violation, consistent with the requirement that disgorged revenues flow back to retail customers (through their LSEs). TIEC stated that a subsequent proceeding would be a contentious, cumbersome, and complex administrative process and result in an unnecessary expenditure of time and resources. TIEC noted that statute requires that disgorged revenues flow back to retail customers and therefore no other wholesale market participants should be entitled to the disgorged revenues except for those entities in the market during the violation. TIEC recommended that the proposed rule remove any reference to a subsequent proceeding.

Commission Response

The commission clarifies that the provision in subsection (j) concerning a subsequent proceeding grants the commission broad flexibility to open a separate proceeding to address the situation in which it determines other wholesale electric market participants are affected or a non-standard distribution method is appropriate. As discussed above regarding proposed subsection (i), parties in a subsequent proceeding would not be limited to the parties in the administrative penalty and disgorgement proceedings. Other wholesale market participants that are properly entitled to receive disgorged revenues could be determined and all affected parties would have the ability to participate in the subsequent proceeding.

The commission disagrees with NRG, TCPA, and TIEC that the commission should be denied by rule the flexibility to consider the issues concerning the distribution of disgorged excess revenues in a separate proceeding. The commission appreciates the concerns raised by parties regarding the expense and administrative burden a subsequent proceeding could incur. The commission will consider such factors when determining if a subsequent proceeding is appropriate. The commission therefore declines to adopt the amendments proposed by NRG, TCPA, and TIEC.

ARM and TCPA stated that a more efficient and effective means of distributing disgorged revenues would be to simply direct the independent organization to apply the disgorged funds as an offset to the System Administration Fee. TCPA commented that this would be a more rational, equitable and expeditious way to meet the statute's intent and would completely

eliminate any need for multiple hearings. Further, TCPA noted that an offset to the System Administration Fee would also solve the inherent competitive inequities created by distributing disgorged funds only to LSEs without a requirement to reduce fees or costs incurred by their retail customers. ARM stated that while proposed subsection (j) is an appropriate mechanism for implementing HB 2133, using the disgorged excess revenues to reduce the System Administrative Fee would also appropriately implement the statutory requirements.

In the reply period, ARM, NRG, and TXU agreed with TCPA and requested the commission consider the System Administrative Fee offset as an alternative to the methodology originally proposed in §22.246. ARM stated that it would support the System Administrative Fee offset as an alternative to its own initial recommendations regarding proposed subsection (j). ARM commented that either option would provide a relatively simple and straightforward approach to executing the directive of HB 2133 relating to the return of disgorged excess revenue to affected wholesale electric market participants without imposing unnecessary burdens on affected market participants, the commission, or the independent system operator. ARM stated that it interprets the TCPA System Administrative Fee offset to include use of those monies to offset the costs recovered through the fee if the disgorged excess revenues are not sufficient to reduce the fee by at least one cent. ARM provided alternative language should the commission move to adopt the System Administrative Fee offset allocation methodology clarifying that the independent organization shall use the excess revenue to reduce the costs recovered through its fee authorized and approved by the commission pursuant to PURA §39.151 or to reduce the fee.

NRG commented that while it agrees with the load ratio share allocation, the possibility of a subsequent proceeding initiated by the commission at its discretion creates a number of concerns that would be avoided if TCPA's recommendation were adopted. NRG stated that it was unclear whether parties other than those defined under proposed subsection (i) could participate in a subsequent proceeding. NRG also questioned if wholesale market participants did have standing to appear in the subsequent proceeding, that hearing would cause market participants to incur additional regulatory expenses to litigate an alternative allocation methodology. NRG stated that TCPA's recommendation would eliminate the debate on whether a subsequent proceeding is necessary and would instead establish a process of billing QSEs, who in turn would reduce the charges to LSEs. NRG noted that this would support the intent of HB 2133 to reduce fees incurred by retail electric customers.

TXU supported the System Administrative Fee offset in lieu of any alternative allocation methodology. TXU believed that the System Administrative Fee offset would effectuate the intent of HB 2133 to ensure that retail customers realize the benefits of disgorgement. As stated above in comments regarding proposed subsection (b), TXU provided an alternative proposal should the commission choose not to adopt TCPA's proposal.

Luminant did not oppose TCPA's suggestion to apply disgorged funds as an offset to the System Administrative Fee as the means for using disgorged revenues to reduce the costs and fees incurred by retail electric customers.

Cities and TIEC disagreed and asked the commission to reject the System Administrative Fee offset proposal. Cities believed that TCPA's suggestion would not ensure that disgorged funds reach retail electric customers because the System Administrative Fee is charged to QSEs rather than retail electric customers. Disbarment of the disgorged funds through the reduction of such fee is not a certain way to ensure the statutory mandate that disgorged funds reduce fees and costs for retail customers.

TIEC noted that no other commentators opposed the methodology in the proposed rule or supported the approach recommended by TCPA, including the consumers who would ultimately be entitled to the disgorged revenues. TIEC commented that there is no guarantee if and how the fee would be passed through to a given retail customer as retail contracts treat the System Administration Fee in various ways. Specifically, TIEC commented that the TCPA proposal failed to allocate disgorged revenues to LSEs in proportion to the harm suffered as a result of the violation and instead distributed the funds to all market participants regardless of whether or not they were affected. The System Administrative Fee offset allocation would be based on load ratio share at the time of distribution rather than the actual violation. TIEC maintained that the offset does not follow cost-causation principles and bears no relationship to the level of additional costs incurred by a given LSE as a result of the violation.

Commission Response

The commission disagrees with ARM, NRG, TCPA, and TXU that applying disgorged excess revenues as an offset to the independent system operator's System Administrative Fee is an appropriate means of allocating disgorged funds. While a System Administrative

Fee offset might be simple and straightforward, the commission agrees with Cities and TIEC that an offset does not best reflect the statutory intent of HB 2133. Specifically, the System Administrative Fee allocation would not necessarily allocate the disgorged funds only to affected wholesale electric market participants. The System Administrative Fee offset would be applied across the board to all wholesale market participants active at the time the disgorged revenues are distributed in proportion to current load ratio share. This does not reflect the harm caused to affected parties at the time of the violation. Additionally, the commission agrees that the System Administrative Fee offset would not ensure compliance with the requirement in PURA §15.025(e) that any disgorged revenues be returned only to the affected wholesale electric market participants to be used to reduce costs or fees incurred by retail electric customers.

The commission believes that disgorged excess revenues should be allocated to affected wholesale electric market participants based on the load ratio share of affected parties at the time of the violation or during the affected intervals of a continuing violation. The proposed load ratio share allocation methodology best reflects the intent of HB 2133 that disgorged excess revenues be returned to affected wholesale electric market participants. The commission therefore declines to adopt the amendments proposed by ARM and TCPA.

ARM requested clarification on any ambiguity regarding the manner in which an independent organization fulfills the requirement to distribute disgorged excess revenues. ARM stated that a literal reading of proposed subsection (j) may suggest that the independent organization is

required to directly distribute excess revenues to affected wholesale electric market participants as defined in proposed subsection (b)(1). ARM noted that in the ERCOT region, qualified scheduling entities (QSE) represent LSEs in all communications and other interactions involved with the independent organization, including settlement invoicing and remittance of payments. LSEs, including REPs, MOUs, and electric cooperatives, are not directly or actively participate in ERCOT administrative functions. ARM specifically noted that the ERCOT System Administrative Fee is assessed to QSEs based on the load it represents, rather than directly assed to each LSE. ARM stated that ERCOT lacks ready access to load information specific to LSEs, which would hinder its ability to allocate excess revenues based on an LSE's load ratio share for each relevant interval. ARM commented that proposed subsection (j) should be read to allow the independent organization to allocate and distribute disgorged excess revenues at the QSE level and proposed language clarifying this intent. ARM stated that this would allow ERCOT to calculate the allocation of funds for a QSE representing one or more REPs based on the total load served by those REPs during the relevant intervals and would leave any further allocation of such funds to the contractual arrangements between the QSE and REPs. This would be consistent with the current market operations of QSEs serving multiple REPs, but would occur through the separate process contemplated by proposed subsection (j). If the commission does not adopt the language proposed by ARM, it requested that the intent of subsection (j) be fully explained in the preamble of the adopted rule.

TEC agreed that the proposed method of returning disgorged revenues to LSEs is not entirely clear. Specifically, TEC noted that ERCOT, as the current independent organization, has no protocols for returning disgorged revenues and it is not certain whether ERCOT would choose to

pay disgorged revenues to QSEs or would make payment directly to LSEs. TEC commented that if disgorged revenues are returned to QSEs, it questioned how the commission could assure that the monies are ultimately returned to LSEs and how entities that buy or sell in the wholesale market but do not serve retail load would be affected. TEC commented that it may not be appropriate to allocated funds to QSEs as they do not serve load. Further, QSEs might have contractual relationships allowing them to retain disgorged revenues that would otherwise go to affected wholesale market participants. TEC stated that these questions could be avoided if the independent organization was required to pay disgorged revenues directly to LSEs.

Commission Response

The commission disagrees with ARM's statement that an independent organization will lack ready access to load information specific to LSEs. ERCOT, the current independent organization, has the ability to determine the load ratio share of individual loads and to specify the appropriate allocation of funds to the affected wholesale market participants. Although the commission declines to adopt the language proposed by ARM, the commission clarifies that disgorged funds should be distributed to the QSEs by ERCOT with an instruction detailing the amounts owed to each LSE within the QSE's portfolio.

While the commission appreciates TEC's concern that disgorged revenues may not end up with the LSEs, the commission notes that any failure to comply with the obligations of the statute and rule to reduce fees and costs to customers would be a violation of PURA and commission rules.

TIEC stated that the proposed rule should clarify how the independent organization will treat disgorged revenues allocated to a market participant that is no longer active. As proposed, a disparity between the total amount of revenues to be disgorged and the total amount owed to active market participants would exist if an affected market participant is no longer active at the time disgorged funds are allocated to the market. TIEC recommended removing the load of market participants that are no longer active at the time of distribution from the total load prior to the independent system operator calculating the load ratio share allocation of the active affected market participants. TIEC provided language amending subsection (j) to express that intent.

In the reply period, Cities supported TIEC's recommendation and urged the commission to adopt TIEC's proposed language.

Commission Response

The commission agrees with TIEC that inactive market participants should not be allocated disgorged excess revenues. The intent of HB 2133 was for affected wholesale electric market participants to use the funds to reduce costs or fees incurred by retail electric customers. Inactive market participants do not serve load and therefore may not be able to utilize the funds to the benefit of retail customers. The commission believes that the language proposed by TIEC clarifies the intent of proposed subsection (j) that the independent organization shall distribute the monies to affected wholesale electric market participants active at the time of distribution. The commission adopts TIEC's relevant amendments to subsection (j) as proposed.

Cities recommended that proposed subsection (j) expressly state that the independent organization shall distribute the excess revenue to affected wholesale electric market participants to be used to reduce costs or fees incurred by retail electric customers. Cities also proposed requiring the independent organization to include with the distributed monies a communication that explains instructions that the disgorged monies must be used to reduce costs or fees incurred by retail electric customers. Cities provided more extensive comments regarding the legislative intent of the disgorged excess revenues in comment to the proposed substantive amendments under §25.503.

Commission Response

The commission agrees with Cities. HB 2133 expressed the clear intent that affected wholesale electric market participants who receive an allocation of disgorged funds should use such funds to reduce costs or fees incurred by retail electric customers. The commission adopts Cities' recommendation by amending subsection (j) to mirror the intent of the statue that the independent organization shall distribute the excess revenue to affected wholesale electric market participants in proportion to their load during the intervals when the violation occurred to be used to reduce costs or fees incurred by retail electric customers and include such instruction in a communication with distributed monies.

Luminant recommended that a REP of an affiliated generation company be required, at the commission's discretion, to demonstrate to the commission that any disgorged excess revenues it received were applied to reduce the costs and fees incurred by its retail electric customers.

Luminant clarified that its proposal was meant to apply only to REPs affiliated with the entity subject to the disgorgement order.

TXU agreed and stated that if the commission does not adopt the distribution methodology recommended by TCPA under proposed subsection (j), it would be reasonable to require an affiliate REP in receipt of disgorged revenues, on request, to demonstrate that the funds were actually applied to reduce the costs and fees of its retail customers. TXU agreed with Luminant that such a demonstration would ensure that the affiliated REP's affected retail customers receive benefits to which they are entitled under the statute. TXU also agreed that this requirement should not be imposed on unaffiliated REPs, as imposing any additional administrative requirements would be both unnecessary and unjustifiably burdensome.

ARM stated that while the limited impact of Luminant's proposal is markedly different from the harm Cities' reporting proposal would inflict, it also opposes Luminant's recommendations. Specifically, ARM commented that it opposed Luminant based on its reading of PURA §15.025(e) and its arguments filed in response to proposed substantive amendments to §25.503 regarding a REP's ability to recover the increased wholesale costs from customers prior to its receipt of disgorged excess revenues.

Commission Response

The commission recognizes Cities' point that it may be beneficial to require all entities receiving disgorged funds to demonstrate to the commission that the funds were actually used to reduce customers' costs and fees. However, the commission recognizes in some

cases non-affiliates receiving disgorged excess revenues may find reporting overly burdensome and costly. Therefore, the commission adopts Luminant's language under subsection (j) as originally suggested, which allows the commission the discretion to require a demonstration of how funds were used, but does not require it.

The commission agrees with TXU and Luminant that it is reasonable to require an affiliate REP in receipt of disgorged revenues to demonstrate that the funds were actually applied to reduce the costs and fees of its retail customers. This would ensure that the affiliate's corporate family would not retain the disgorged revenue. Thus, the commission amends subsection (j) to include a requirement that affiliates in receipt of disgorged excess revenues shall distribute all of the disgorged excess revenues directly to its retail customers and shall provide certification under oath to the commission that the entirety of the revenues were distributed to its retail electric customers.

All comments, including any not specifically referenced herein, were fully considered by the commission. In adopting this section, the commission makes changes for the purpose of clarifying its intent.

The amendments are adopted under the Public Utility Regulatory Act, Texas Utilities Code Annotated §14.002 and §14.052 (West 2007 and Supp. 2012) (PURA), which provide the commission with the authority to make and enforce rules reasonably required in the exercise of its powers and jurisdiction, including rules of practice and procedure. Specifically, PURA §15.023 requires the commission to order disgorgement of excess revenues acquired by a market

participant by violation of PURA §39.157 and grants the commission discretion to order disgorgement of excess revenues for wholesale electricity market violations of other PURA sections, commission rules, or wholesale electricity market protocols. Also, PURA §15.024 limits the parties to an administrative penalty proceeding to the person alleged to have committed the violation and the commission. PURA §15.025 requires the commission to adopt rules to return excess revenues ordered disgorged to affected wholesale electric market participants to be used to reduce costs or fees incurred by retail electric customers. PURA §35.004 requires that the commission ensure that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, predatory, or anticompetitive. PURA §39.001 establishes the Legislative policy to protect the public interest during the transition to and in the establishment of a fully competitive electric power industry. PURA §39.101 establishes that customers are entitled to protection from unfair, misleading, or deceptive practices and directs the commission to adopt and enforce rules to carry out this provision and to ensure that retail customer protections are established that afford customers safe, reliable, and reasonably priced electricity. PURA §39.151 requires the commission to oversee and review the procedures established by an independent organization, directs market participants to comply with such procedures, and authorizes the commission to enforce such procedures. PURA §39.157 directs the commission to monitor market power associated with the generation, transmission, distribution, and sale of electricity and provides enforcement power to the commission to address any market power abuses. PURA §39.356 allows the commission to revoke certain certifications and registrations for violation of an independent organization's procedures, statutory provisions, or the

commission's rules. Finally, PURA §39.357 authorizes the commission to impose administrative penalties in addition to revocation, suspension, or amendment of certificates and registrations.

Cross Reference to Statutes: Public Utility Regulatory Act §§14.002, 15.023, 15.024, 15.025, 35.004, 39.001, 39.101, 39.151, 39.157, 39.356, and 39.357.

§22.246. Administrative Penalties.

(a) **Scope.** This section is intended to address enforcement actions related to administrative penalties or disgorgement of excess revenues only and does not apply to any other enforcement actions that may be undertaken by the commission or the commission staff.

(b) **Definitions.** The following words and terms, when used in this section, shall have the following meanings unless the context clearly indicates otherwise:

(1) **Affected Wholesale Electric Market Participant --** An entity, including a retail electric provider (REP), municipally owned utility (MOU), or electric cooperative, that sells energy to retail customers and served load during the period of the violation.

(2) **Excess Revenue** -- As defined in §25.503 of this title (relating to Oversight of Wholesale Market Participants).

(3) **Executive director** -- The executive director of the commission or the executive director's designee.

(4) **Person** -- Includes a natural person, partnership of two or more persons having a joint or common interest, mutual or cooperative association, and corporation.

(5) **Violation** -- Any activity or conduct prohibited by the Public Utility Regulatory Act (PURA), commission rule or commission order.

(6) **Continuing violation** -- Except for a violation of PURA Chapter 17, 55, or 64, and commission rules or commission orders pursuant to those chapters, any instance in which the person alleged to have committed a violation attests that a

violation has been remedied and was accidental or inadvertent and subsequent investigation reveals that the violation has not been remedied or was not accidental or inadvertent.

(c) **Amount of administrative penalty.**

(1) Each day a violation continues or occurs is a separate violation for which an administrative penalty can be levied, regardless of the status of any administrative procedures that are initiated under this subsection.

(2) The administrative penalty for each separate violation may be in an amount not to exceed $25,000 per day, provided that an administrative penalty in an amount that exceeds $5,000 may be assessed only if the violation is included in the highest class of violations in the classification system.

(3) The amount of the administrative penalty shall be based on:

(A) the seriousness of the violation, including the nature, circumstances, extent, and gravity of any prohibited acts, and the hazard or potential hazard created to the health, safety, or economic welfare of the public;

(B) the economic harm to property or the environment caused by the violation;

(C) the history of previous violations;

(D) the amount necessary to deter future violations;

(E) efforts to correct the violation; and

(F) any other matter that justice may require, including, but not limited to, the respondent's timely compliance with requests for information, completeness of responses, and the manner in which the respondent has

cooperated with the commission during the investigation of the alleged violation.

(d) **Initiation of investigation.** Upon receiving an allegation of a violation or of a continuing violation, the executive director shall determine whether an investigation should be initiated.

(e) **Report of violation or continuing violation.** If, based on the investigation undertaken pursuant to subsection (d) of this section, the executive director determines that a violation or a continuing violation has occurred, the executive director may issue a report to the commission.

(1) **Contents of the report.** The report shall state the facts on which the determination is based and a recommendation on the imposition of an administrative penalty, including a recommendation on the amount of the administrative penalty and, if applicable pursuant to §25.503 of this title, a recommendation that excess revenue be disgorged.

(2) **Notice of report.** Within 14 days after the report is issued, the executive director shall, by certified mail, return receipt requested, give written notice of the report to the person who is alleged to have committed the violation or continuing violation which is the subject of the report. The notice must include:

(A) a brief summary of the alleged violation or continuing violation;

(B) a statement of the amount of the recommended administrative penalty;

(C) a statement recommending disgorgement of excess revenue, if applicable, pursuant to §25.503 of this title;

(D) a statement that the person who is alleged to have committed the violation or continuing violation has a right to a hearing on the occurrence of the violation or continuing violation, the amount of the administrative penalty, or both the occurrence of the violation or continuing violation and the amount of the administrative penalty;

(E) a copy of the report issued to the commission pursuant to this subsection; and

(F) a copy of this section, §22.246 of this title (relating to Administrative Penalties).

(f) **Options for response to notice of violation or continuing violation.**

(1) **Opportunity to remedy.**

(A) This paragraph does not apply to a violation of PURA Chapters 17, 55, or 64, or of a commission rule or commission order pursuant to those chapters.

(B) Within 40 days of the date of receipt of a notice of violation set out in subsection (e)(2) of this section, the person against whom the administrative penalty or disgorgement may be assessed may file with the commission proof that the alleged violation has been remedied and that the alleged violation was accidental or inadvertent. A person who claims to have remedied an alleged violation has the burden of proving to the

commission both that an alleged violation was remedied before the 31st day after the date the person received the report of violation and that the alleged violation was accidental or inadvertent. Proof that an alleged violation has been remedied and that the alleged violation was accidental or inadvertent shall be evidenced in writing, under oath, and supported by necessary documentation.

(C) If the executive director determines that the alleged violation has been remedied, was remedied within 30 days, and that the alleged violation was accidental or inadvertent, no administrative penalty will be assessed against the person who is alleged to have committed the violation.

(D) If the executive director determines that the alleged violation was not remedied or was not accidental or inadvertent, the executive director shall make a determination as to what further proceedings are necessary.

(E) If the executive director determines that the alleged violation is a continuing violation, the executive director shall institute further proceedings, including referral of the matter for hearing pursuant to subsection (h) of this section.

(2) **Payment of administrative penalty and/or disgorged excess revenue.** Within 30 days after the date the person receives the notice set out in subsection (e)(2) of this section, the person may accept the determination and recommended administrative penalty and, if applicable, the recommended excess revenue to be disgorged through a written statement sent to the executive director. If this option is selected, the person shall take all corrective action required by the commission.

The commission by written order shall approve the determination and impose the recommended administrative penalty and, if applicable, recommended disgorged excess revenue.

(3) **Request for hearing.** Not later than the 20th day after the date the person receives the notice set out in subsection (e)(2) of this section, the person may submit to the executive director a written request for a hearing on any or all of the following:

(A) the occurrence of the violation or continuing violation;

(B) the amount of the administrative penalty; and

(C) the amount of disgorged excess revenue, if applicable.

(g) **Settlement conference.** A settlement conference may be requested by any party to discuss the occurrence of the violation or continuing violation, the amount of the administrative penalty, disgorged excess revenue~~,~~ if applicable, and the possibility of reaching a settlement prior to hearing. A settlement conference is not subject to the Texas Rules of Evidence or the Texas Rules of Civil Procedure; however, the discussions are subject to Texas Rules of Civil Evidence 408, concerning compromise and offers to compromise.

(1) If a settlement is reached:

(A) the parties shall file a report with the executive director setting forth the factual basis for the settlement;

(B) the executive director shall issue the report of settlement to the commission; and

(C) the commission by written order will approve the settlement.

(2) If a settlement is reached after the matter has been referred to SOAH, the matter shall be returned to the commission. If the settlement is approved, the commission shall issue an order memorializing commission approval and setting forth commission orders associated with the settlement agreement.

(h) **Hearing.** If a person requests a hearing under subsection (f)(3) of this section, or fails to respond timely to the notice of the report of violation or continuing violation provided pursuant to subsection (e)(2) of this section, or if the executive director determines that further proceedings are necessary, the executive director shall set a hearing, provide notice of the hearing to the person, and refer the case to SOAH pursuant to §22.207 of this title (relating to Referral to State Office of Administrative Hearings). The case shall then proceed as set forth in paragraphs (1)-(5) of this subsection.

(1) The commission shall provide the SOAH administrative law judge a list of issues or areas that must be addressed.

(2) The hearing shall be conducted in accordance with the provisions of this chapter.

(3) The SOAH administrative law judge shall promptly issue to the commission a proposal for decision, including findings of fact and conclusions of law, about:

(A) the occurrence of the alleged violation or continuing violation;

(B) whether the alleged violation was cured and was accidental or inadvertent for a violation of any chapter other than PURA Chapters 17, 55, or 64, or of a commission rule or commission order pursuant to those chapters; and

(C) the amount of the proposed administrative penalty and, if applicable, disgorged excess revenue.

(4) Based on the SOAH administrative law judge's proposal for decision, the commission may:

(A) determine that a violation or continuing violation has occurred and impose an administrative penalty and, if applicable, disgorged excess revenue;

(B) determine that a violation occurred but that, pursuant to subsection (f)(1) of this section, the person remedied the violation within 30 days and proved that the violation was accidental or inadvertent, and that no administrative penalty will be imposed; or

(C) determine that no violation or continuing violation has occurred.

(5) Notice of the commission's order issued pursuant to paragraph (4) of this subsection shall be provided under the Government Code, Chapter 2001 and §22.263 of this title (relating to Final Orders) and shall include a statement that the person has a right to judicial review of the order.

(i) **Parties to a proceeding.** The parties to a proceeding relating to administrative penalties or disgorgement of excess revenue shall be limited to the person who is alleged to have committed the violation or continuing violation and the commission, including the independent market monitor. This does not apply to a subsequent proceeding under subsection (j) of this section.

(j) **Distribution of Disgorged Excess Revenues.** Disgorged excess revenues shall be remitted to an independent organization, as defined in PURA §39.151. The independent organization shall distribute the excess revenue to affected wholesale electric market participants in proportion to their load during the intervals when the violation occurred to be used to reduce costs or fees incurred by retail electric customers. The load of any market participants that are no longer active at the time of the distribution shall be removed prior to calculating the load proportions of the affected wholesale electric market participants that are still active. However, if the commission determines other wholesale electric market participants are affected or a different distribution method is appropriate, the commission may direct commission staff to open a subsequent proceeding to address those issues.

(1) No later than 90 days after the disgorged excess revenues are remitted to the independent organization, the monies shall be distributed to affected wholesale electric market participants active at the time of distribution, or the independent organization shall, by that date, notify the commission of the date by which the funds will be distributed. The independent organization shall include with the distributed monies a communication that explains the docket number in which the commission ordered the disgorged excess revenues, an instruction that the monies shall be used to reduce costs or fees incurred by retail electric customers, and any other information the commission orders.

(2) The commission may require any affected wholesale electric market participants receiving disgorged funds to demonstrate how the funds were used to reduce the costs or fees incurred by retail electric customers.

(3) Any affected wholesale electric market participant receiving disgorged funds that is affiliated with the person from whom the excess revenue is disgorged shall distribute all of the disgorged excess revenues directly to its retail customers and shall provide certification under oath to the commission that the entirety of the revenues were distributed to its retail electric customers.

This agency hereby certifies that the adoption has been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority. It is therefore ordered by the Public Utility Commission of Texas that §22.246, relating to Administrative Penalties is hereby adopted with changes to the text as proposed.

SIGNED AT AUSTIN, TEXAS on the _____ day of _____ 2012.

PUBLIC UTILITY COMMISSION OF TEXAS

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DONNA L. NELSON, CHAIRMAN

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KENNETH W. ANDERSON, JR., COMMISSIONER

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ROLANDO PABLOS, COMMISSIONER