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 §25.503
AS APPROVED AT THE OCTOBER 12, 2012 OPEN MEETING

The Public Utility Commission of Texas (commission) adopts amendments to §25.503, relating to Oversight of Wholesale Market Participants, 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 procedural amendments proposed to §22.246, 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.

General Comments

Cities stated that while it generally supports the proposed rule as published, it believes that the proposed amendments to §25.503 and §22.246 could more accurately track the language and intent of HB 2133, which it supported during the 2011 Legislative Session. Specifically, Cities commented that the essence of HB 2133 is the provision that disgorged excess profits must be used to reduce fees and charges for the ultimate retail customer. Cities noted that prior to the legislation, any administrative penalties collected by the commission were sent to the state's General Revenue Fund and HB 2133 provided that any excess revenues ordered disgorged would instead be returned to affected wholesale market participants to be used to reduce costs or fees incurred by retail electric customers. The proposed rule omits that disgorged funds are to be used in such a manner.

Cities stated that it recognizes that distribution of disgorged funds to customers may require different approaches based on the particular wholesale market participant and the amount of funds disgorged. Cities commented that it intends its proposed amendments to give market participants the discretion to lower bill charges and fees for electric customers in a manner tailored to the individual circumstance of the wholesale market participant and recommended a reporting requirement to ensure that the funds are actually used for this purpose. Cities proposed a new subsection (n) and provided language to require market participants to file a report at the commission within 60 days of disbursement of disgorged funds to detail how the affected party

intends to distribute the funds to retail customers. These amendments included a requirement that the wholesale market participant apportion disgorged funds in a reasonable manner across all customer classes and clearly label the funds on customers' bills. Cities proposed holding any party who fails to comply with the recommended new provisions subject to enforcement proceedings. Cities also provided amendments in comments under §22.246 that would conform the procedural rule to this intent.

ARM disagreed with Cities' recommendation and stated that Cities' proposed billing and reporting requirements would subvert the disgorgement process, contrary to the interests of the affected market participants that the legislation intended to serve. ARM commented that such requirements would be onerous and unjustified. ARM requested that the commission reject Cities' proposed revisions to both §22.246 and §25.503 on three principal grounds.

First, ARM noted that PURA §15.025(e) directs the commission to adopt rules prescribing the process for returning excess revenue to affected market participants, but does not include a directive requiring the commission to prescribe affected market participants' use of the excess revenue in those rules. If the legislature had intended REPs to simply act as a vessel to pass through disgorged excess revenue to retail customers, it would have directed the commission to adopt rules prescribing how revenue should be returned to affected retail customers rather than affected wholesale electric market participants. ARM stated that the narrow interpretation of §15.025(e) used by Cities ignores the statute's emphasis on this distinction, and fails to reference that the term "costs" generally refers to the capital and other expenses underlying the provision of retail service. PURA uses the term "credit" to describe an offset to a bill or price similar to

the mechanism contemplated by Cities. ARM stated that the statute is reasonably interpreted to reflect a legislative presumption regarding the use of the disgorged amount to directly or indirectly reduce the costs borne by retail customers, rather than an enforceable obligation as proposed by Cities.

Second, ARM commented that the billing and reporting requirements proposed by Cities are based on a flawed assumption that presupposes that a REP has recovered an amount equal to or greater than its allocated share of excess revenue from its retail customers. ARM stated that REPs have limited ability to recover increased wholesale costs attributable to the unlawful action upon which disgorgement is based. ARM noted that a REP's ability to change retail prices is limited by contract terms and parameters establishing the degree to which a REP can or may recover an increase in wholesale costs attributable to the unlawful exercise of market power upon which a disgorgement order is based. Specifically, a REP cannot adjust the price of a fixed price product to recover such incremental amounts as a matter of law; indexed products may not to be tied to information that will fully capture the increase in wholesale costs attributable to unlawful conduct. Variable price products may give REPs greater latitude to recover increased wholesale costs, but competitive market risks limit the ability to recover such increases due to customer churn following a price increase. ARM noted that similar restrictions regarding price adjustments could limit the ability of REPs to recover incrementally higher wholesale costs from commercial or industrial customers; if the terms of service on a particular product allow the recovery of such increases, it may also require the REP to pass through a portion of any excess revenues to the customer. ARM stated that Cities' proposed billing and reporting requirements

could actually worsen the financial harm experienced as a result of the market power violation by requiring a REP to liquidate any restitution provided.

Finally, ARM stated that compliance costs associated with the billing and reporting requirements proposed by Cities would further exacerbate the financial harm experienced by REPs as a result of a disgorgement allocation. ARM commented that the reports proposed would require a detailed compliance plan and statement of compliance. Given the possibility of a violation leading to disgorgement affecting a large number of usage intervals and a REP offering numerous different retail products, such reports would require REPs to spend an extensive amount of time and resources to formulate the reports. ARM stated that Cities' proposal frames the allocation of excess revenues in traditional ratemaking terms, treating the affected market participant like a regulated utility rather than acknowledging the fluid nature of energy costs in the competitive wholesale market. ARM noted that these requirements could compel REPs to incur costs when modifying their billing systems in order to pass through excess revenues in a clearly labeled manner; these costs may not differ greatly from the amount passed through to the customers in the case of small or moderate disgorgements. ARM commented that it was also unclear if anyone would in turn review the reports in a commensurate manner, or at all.

Commission Response

The commission agrees with Cities in part. HB 2133 intended 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 market entities allocated disgorged excess revenues shall utilize such funds to reduce costs or fees incurred

by retail electric customers as was the express intent of the Legislature when amending PURA §15.025(e). The commission considered the relationship between wholesale market participants and retail customers when proposing the amendments to both §25.503 and §22.246. Therefore, the definition of affected wholesale electric market participants proposed under §22.246(b)(1) reflects the intent that retail entities that served load during the period of the violation would be eligible to receive funds.

The commission disagrees with Cities that a mandatory reporting requirement is necessary to ensure that disbursed excess revenues are actually used to reduce costs or fees. The commission agrees with ARM that the statute does not include a directive requiring the commission to specifically prescribe affected market participants' use of the excess revenue by rule. The commission also agrees that the restrictive reporting and billing requirements proposed by Cities could be burdensome and costly for affected parties' allocated funds. The commission appreciates the intention of Cities in its comments to give market participants the discretion to lower bill charges and fees for electric customers in a manner tailored to the individual circumstance of the wholesale market participant.

For the above mentioned reasons, the commission declines to adopt new subsection (n) as proposed. However, the commission does believe that it should have the flexibility to require affected wholesale electric market participants to report on how any disgorged excess funds received were used to benefit retail electric customers on a case-by-case basis. In certain cases, the commission may conclude reporting is warranted and order such upon the conclusion of the proceedings. The commission believes that reporting standards are

better suited in the procedural amendments proposed under §22.246. The commission further discusses discretionary reporting and Cities' proposed amendments in response to comments filed regarding §22.246(j).

Proposed subsection (m)

Luminant stated that the commission's new disgorgement authority should invest a reasonable degree of regulatory discretion with the agency, but it believed some guidelines or standards of application to be appropriate and beneficial. Luminant noted that standards are especially appropriate as applied to wholesale market violations outside of PURA §39.157 when the commission is given to discretion of when to use the drastic and extraordinary remedy. Luminant specifically recommended that the rule include a requirement that the violation giving rise to disgorgement was intentional or reckless, and establish a dollar threshold of excess revenue that must be met in order for disgorgement to become available in an enforcement action. Luminant stated that disgorgement functions as a means of achieving specific restitution, restoring misappropriated property to the rightful owner and depriving the misappropriator of his unjust gain; disgorgement is a concept of restitution built to fill the gap of the rest of the law. Luminant noted that even when courts possess the authority to exercise their inherent equitable powers, they commonly recognize that disgorgement is not appropriate or necessary if the conduct was not intentional, knowing, or in bad faith, if disgorgement will only serve a punitive purpose, or if other remedies are sufficient to compensate the wrong. Agencies, unlike courts, do not have broad remedial powers or inherent equitable jurisdiction.

Luminant cited similar administrative authority possessed by the Federal Energy Regulation Commission (FERC) and the relationship between §25.503 and FERC's corresponding rule, which is derived from section 222 of the Federal Power Act. The FERC anti-manipulation rule has been interpreted to proscribe knowing or intentional misconduct, based on the understanding that such conduct inherently requires a culpable mental state. Luminant noted that FERC has determined disgorgement to be appropriate only when entities intentionally engaged in gaming practices or offered energy into the market although it knew units could not provide energy if dispatched. Luminant commented that HB 2133 requires disgorgement for similar market abuse violations of the same intentional or knowing character as those recognized by FERC, but that other wholesale electric market violations do not necessarily merit the same remedy. FERC directs its enforcement resources at only flagrant misconduct and Luminant requested similar prosecutorial discretion from the commission when directing enforcement resources to pursue disgorgement. Luminant stated that incorporating standards into the commission's rules would ensure that disgorgement is sought in appropriate cases, and would provide predictability to market participants, ensuring that disgorgement remains an extraordinary remedy to be used only in the rare cases when it is necessary to achieve a just result. Luminant provided language under proposed subsection (m) that would amend the rule to include a requirement that the violator acted with the necessary culpable mental state, either affirmative intent or reckless disregard.

Further, Luminant proposed establishing a monetary threshold for market impact before a disgorgement action could be triggered. Luminant noted that a disgorgement ruling would impose a considerable administrative burden and incorporating a monetary threshold into the rule would narrow the number of cases eligible for disgorgement to only those where the costs

associated with returning money to the affected market participants could be justified. Luminant recommended a threshold of $1,000,000.00 as a sensible amount in view of prior enforcement actions at the commission. Luminant stated that in otherwise small penalty cases, benefits realized after a complex disgorgement proceeding would outweigh the costs of retuning the money to customers.

Cities and TIEC disagreed with Luminant and requested that the commission reject suggestions to revise the proposed rule in a manner that is inconsistent with the Legislature's directive. Cities stated that such restriction on the imposition of disgorgement and threshold of violation are not contained in HB 2133, nor do they give effect to the language of HB 2133. Cities stated that Luminant's suggested language would frustrate the intent of the legislation to ensure that retail customers are made whole after a commission finding that market power abuse has occurred. Cities further questioned how the commission could ever prove that the entity accused of market power abuse acted with the requisite subjective intent.

TIEC similarly stated that Luminant's request to limit the commission's ability to order disgorgement for non-PURA §39.157 violations has no statutory basis or other support. HB 2133 provided the commission with discretion to determine, on a case-by-case basis, whether disgorgement is an appropriate remedy for any violation of the statute, commission rules, or protocols relating to wholesale markets beyond PURA §39.157 for which disgorgement is mandatory. TIEC commented that the proposed subsection (m) tracks this language by generally providing that disgorgement may be ordered for violations of wholesale market requirements without restriction and allows the commission to determine whether disgorgement is appropriate

based on the particular circumstances of a violation. TIEC noted that as proposed, the commission would be able to take into consideration factors raised by Luminant along with other fact-specific circumstances to determine whether disgorgement should be ordered.

Commission Response

The commission disagrees with Luminant that a culpable mental state, either affirmative intent or reckless disregard, should be a necessary qualification for disgorgement and also disagrees that a specific monetary threshold should be reached as a result of a violation prior to disgorgement becoming an available tool to the commission in an enforcement action. Such restrictions are not required by HB 2133. HB 2133 granted the commission both authority and discretion to pursue disgorgement for wholesale electric market violations of PURA sections other than PURA §39.157 or commission rules, or wholesale electric market protocols. The legislature did not limit the authority of the commission to pursue disgorgement based on the monetary size of a violation or require that the market entity act intentionally or recklessly. 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 therefore declines to adopt the amendments proposed by Luminant.

All comments, including any not specifically referenced herein, were fully considered by the commission.

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.

§25.503. Oversight of Wholesale Market Participants.

(a) **Purpose.** The purpose of this section is to establish the standards that the commission will apply in monitoring the activities of entities participating in the wholesale electricity markets, including markets administered by the Electric Reliability Council of Texas (ERCOT), and enforcing the Public Utility Regulatory Act (PURA) and ERCOT procedures relating to wholesale markets. The standards contained in this rule are necessary to:

(1) protect customers from unfair, misleading, and deceptive practices in the wholesale markets, including ERCOT-administered markets;

(2) ensure that ancillary services necessary to facilitate the reliable transmission of electric energy are available at reasonable prices;

(3) afford customers safe, reliable, and reasonably priced electricity;

(4) ensure that all wholesale market participants observe all scheduling, operating, reliability, and settlement policies, rules, guidelines, and procedures established in the ERCOT procedures;

(5) clarify prohibited activities in the wholesale markets, including ERCOT-administered markets;

(6) monitor and mitigate market power as authorized by the Public Utility Regulatory Act (PURA) §39.157(a) and prevent market power abuses;

(7) clarify the standards and criteria the commission will use when reviewing wholesale market activities;

(8) clarify the remedies for non-compliance with the Protocols relating to wholesale markets; and

(9) prescribe ERCOT's role in enforcing ERCOT procedures relating to the reliability of the regional electric network and accounting for the production and delivery among generators and all other market participants, and monitoring and obtaining compliance with operating standards within the ERCOT regional network.

(b) **Application.** This section applies to all market entities, as defined in subsection (c) of this section.

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

(1) **Artificial congestion** -- Congestion created when multiple foreseeable options exist for scheduling, dispatching, or operating a resource, and a market participant chooses an option that is not the most economical, that foreseeably creates or exacerbates transmission congestion, and that results in the market participant being paid to relieve the congestion it caused.

(2) **Efficient operation of the market** -- Operation of the markets administered by ERCOT, consistent with reliability standards, that is characterized by the fullest use of competitive auctions to procure ancillary services, minimal cost socialization, and the most economical utilization of resources, subject to necessary operational and other constraints.

(3) **ERCOT procedures** -- Documents that contain the scheduling, operating, planning, reliability, and settlement procedures, standards, and criteria that are public and in effect in the ERCOT power region, including the ERCOT Protocols and ERCOT Operating Guides as amended from time to time but excluding ERCOT's internal administrative procedures. The Protocols generally govern when there are inconsistencies between the Protocols and the Operating Guides, except when ERCOT staff, consistent with subsection (i) of this section, determines that a provision contained in the Operating Guides is technically superior for the efficient and reliable operation of the electric network.

(4) **Excess Revenue --** Revenue in excess of the revenue that would have occurred absent a violation of PURA §39.157 or this section.

(5) **Market entity** -- Any person or entity participating in the ERCOT-administered wholesale market, including, but not limited to, a load serving entity (including a municipally owned utility and an electric cooperative,) a power marketer, a transmission and distribution utility, a power generation company, a qualifying facility, an exempt wholesale generator, ERCOT, and any entity conducting planning, scheduling, or operating activities on behalf of, or controlling the activities of, such market entities.

(6) **Market participant --** A market entity other than ERCOT.

(7) **Resource** -- Facilities capable of providing electrical energy or load capable of reducing or increasing the need for electrical energy or providing short-term reserves into the ERCOT system. This includes generation resources and loads acting as resources (LaaRs).

(d) **Standards and criteria for enforcement of ERCOT procedures and PURA.** The commission will monitor the activities of market entities to determine if such activities are consistent with ERCOT procedures; whether they constitute market power abuses or are unfair, misleading, or deceptive practices affecting customers; and whether they are consistent with the proper accounting for the production and delivery of electricity among generators and other market participants. When reviewing the activities of a market entity, the commission will consider whether the activity was conducted in a manner that:

(1) adversely affected customers in a material way through the use of unfair, misleading, or deceptive practices;

(2) materially reduced the competitiveness of the market, including whether the activity unfairly impacted other market participants in a way that restricts competition;

(3) disregarded its effect on the reliability of the ERCOT electric system; or

(4) interfered with the efficient operation of the market.

(e) **Guiding ethical standards.** Each market participant is expected to:

(1) observe all applicable laws and rules;

(2) schedule, bid, and operate its resources in a manner consistent with ERCOT procedures to support the efficient and reliable operation of the ERCOT electric system; and

(3) not engage in activities and transactions that create artificial congestion or artificial supply shortages, artificially inflate revenues or volumes, or manipulate the market or market prices in any way.

(f) **Duties of market entities.**

(1) Each market participant shall be knowledgeable about ERCOT procedures.

(2) A market participant shall comply with ERCOT procedures and any official interpretation of the Protocols issued by ERCOT or the commission.

(A) If a market participant disagrees with any provision of the Protocols or any official interpretation of the Protocols, it may seek an amendment of the Protocols as provided for in the Protocols, appeal an ERCOT official interpretation to the commission, or both.

(B) A market participant appealing an official interpretation of the Protocols or seeking an amendment to the Protocols shall comply with the Protocols unless and until the interpretation is officially changed or the amendment is officially adopted.

(C) A market participant may be excused from compliance with ERCOT instructions or Protocol requirements only if such non-compliance is due to communication or equipment failure beyond the reasonable control of the market participant; if compliance would jeopardize public health and safety or the reliability of the ERCOT transmission grid, or create risk of bodily harm or damage to the equipment; if compliance would be inconsistent with facility licensing, environmental, or legal requirements;

if required by applicable law; or for other good cause. A market participant is excused under this subparagraph only for so long as the condition continues.

(3) Whenever the Protocols require that a market participant make its "best effort" or a "good faith effort" to meet a requirement, or similar language, the market participant shall act in accordance with the requirement unless:

(A) it is not technically possible to do so;

(B) doing so would jeopardize public health and safety or the reliability of the ERCOT transmission grid, or would create a risk of bodily harm or damage to the equipment;

(C) doing so would be inconsistent with facility licensing, environmental, or legal requirements; or

(D) other good cause exists for excusing the requirement.

(4) When a market participant is not able to comply with a Protocol requirement or official interpretation of a requirement, or honor a formal commitment to ERCOT, the market participant has an obligation to notify ERCOT immediately upon learning of such constraints and to notify ERCOT when the problem ceases. A market participant who does not comply with a Protocol requirement or official interpretation of a requirement, or honor a formal commitment to ERCOT, has the burden to demonstrate, in any commission proceeding in which the failure to comply is raised, why it cannot comply with the Protocol requirement or official interpretation of the requirement, or honor the commitment.

(5) The commission staff may request information from a market participant concerning a notification of failure to comply with a Protocol requirement or official interpretation of a requirement, or honor a formal commitment to ERCOT. The market participant shall provide a response that is detailed and reasonably complete, explaining the circumstances surrounding the alleged failure, and shall provide documents and other materials relating to such alleged failure to comply. The response shall be submitted to the commission staff within five business days of a written request for information, unless commission staff agrees to an extension.

(6) A market participant's bids of energy and ancillary services shall be from resources that are available and capable of performing, and shall be feasible within the limits of the operating characteristics indicated in the resource plan, as defined in the Protocols, and consistent with the applicable ramp rate, as specified in the Protocols.

(7) All statements, data and information provided by a market participant to market publications and publishers of surveys and market indices for the computation of an industry price index shall be true, accurate, reasonably complete, and shall be consistent with the market participant's activities, subject to generally accepted standards of confidentiality and industry standards. Market participants shall exercise due diligence to prevent the release of materially inaccurate or misleading information.

(8) A market entity has an obligation to provide accurate and factual information and shall not submit false or misleading information, or omit material information, in

any communication with ERCOT or with the commission. Market entities shall exercise due diligence to ensure adherence to this provision throughout the entity.

(9) A market participant shall comply with all reporting requirements governing the availability and maintenance of a generating unit or transmission facility, including outage scheduling reporting requirements. A market participant shall immediately notify ERCOT when capacity changes or resource limitations occur that materially affect the availability of a unit or facility, the anticipated operation of its resources, or the ability to comply with ERCOT dispatch instructions.

(10) A market participant shall comply with requests for information or data by ERCOT as specified by the Protocols or ERCOT instructions within the time specified by ERCOT instructions, or such other time agreed to by ERCOT and the market participant.

(11) When a Protocol provision or its applicability is unclear, or when a situation arises that is not contemplated under the Protocols, a market entity seeking clarification of the Protocols shall use the Protocol Revision Request (PRR) process provided in the Protocols. If the PRR process is impractical or inappropriate under the circumstances, the market entity may use the process for requesting formal Protocol clarifications or interpretations described in subsection (i) of this section. This provision is not intended to discourage day to day informal communication between market participants and ERCOT staff.

(12) A market participant operating in the ERCOT markets or a member of the ERCOT staff who identifies a provision in the ERCOT procedures that produces an outcome inconsistent with the efficient and reliable operation of the ERCOT-

administered markets shall call the provision to the attention of ERCOT staff and the appropriate ERCOT subcommittee. All market participants shall cooperate with the ERCOT subcommittees, ERCOT staff, and the commission staff to develop Protocols that are clear and consistent.

(13) A market participant shall establish and document internal procedures that instruct its affected personnel on how to implement ERCOT procedures according to the standards delineated in this section. Each market participant shall establish clear lines of accountability for its market practices.

(g) **Prohibited activities.** Any act or practice of a market participant that materially and adversely affects the reliability of the regional electric network or the proper accounting for the production and delivery of electricity among market participants is considered a "prohibited activity." The term "prohibited activity" in this subsection excludes acts or practices expressly allowed by the Protocols or by official interpretations of the Protocols and acts or practices conducted in compliance with express directions from ERCOT or commission rule or order or other legal authority. The term "prohibited activity" includes, but is not limited to, the following acts and practices that have been found to cause prices that are not reflective of competitive market forces or to adversely affect the reliability of the electric network:

(1) A market participant shall not schedule, operate, or dispatch its generating units in a way that creates artificial congestion.

(2) A market participant shall not execute pre-arranged offsetting trades of the same product among the same parties, or through third party arrangements, which involve no economic risk and no material net change in beneficial ownership.

(3) A market participant shall not offer reliability products to the market that cannot or will not be provided if selected.

(4) A market participant shall not conduct trades that result in a misrepresentation of the financial condition of the organization.

(5) A market participant shall not engage in fraudulent behavior related to its participation in the wholesale market.

(6) A market participant shall not collude with other market participants to manipulate the price or supply of power, allocate territories, customers or products, or otherwise unlawfully restrain competition. This provision should be interpreted in accordance with federal and state antitrust statutes and judicially-developed standards under such statutes regarding collusion.

(7) A market participant shall not engage in market power abuse. Withholding of production, whether economic withholding or physical withholding, by a market participant who has market power, constitutes an abuse of market power.

(h) **Defenses.** The term "prohibited activity" in subsection (g) of this section excludes acts or practices that would otherwise be included, if the market entity establishes that its conduct served a legitimate business purpose consistent with prices set by competitive market forces; and that it did not know, and could not reasonably anticipate, that its actions would inflate prices, adversely affect the reliability of the regional electric

network, or adversely affect the proper accounting for the production and delivery of electricity; or, if applicable, that it exercised due diligence to prevent the excluded act or practice. The defenses established in this subsection may also be asserted in instances in which a market participant is alleged to have violated subsection (f) of this section. A market entity claiming an exclusion or defense under this subsection, or any other type of affirmative defense, has the burden of proof to establish all of the elements of such exclusion or defense.

(i) **Official interpretations and clarifications regarding the Protocols.** A market entity seeking an interpretation or clarification of the Protocols shall use the PRR process contained in the Protocols whenever possible. If an interpretation or clarification is needed to address an unforeseen situation and there is not sufficient time to submit the issue to the PRR process, a market entity may seek an official Protocol interpretation or clarification from ERCOT in accordance with this subsection.

(1) ERCOT shall develop a process for formally addressing requests for clarification of the Protocols submitted by market participants or issuing official interpretations regarding the application of Protocol provisions and requirements. ERCOT shall respond to the requestor within ten business days of ERCOT's receipt of the request for interpretation or clarification with either an official Protocol interpretation or a recommendation that the requestor take the request through the PRR process.

(2) ERCOT shall designate one or more ERCOT officials who will be authorized to receive requests for clarification from, and issue responses to market participants,

and to issue official interpretations on behalf of ERCOT regarding the application of Protocol provisions and requirements.

(3) The designated ERCOT official shall provide a copy of the clarification request to commission staff upon receipt. The ERCOT official shall consult with ERCOT operational or legal staff as appropriate and with commission staff before issuing an official Protocol clarification or interpretation.

(4) The designated ERCOT official may decide, in consultation with the commission staff, that the language for which a clarification is requested is ambiguous or for other reason beyond ERCOT's ability to clarify, in which case the ERCOT official shall inform the requestor, who may take the request through the PRR process provided for in the Protocols.

(5) All official Protocol clarifications or interpretations that ERCOT issues in response to a market participant's formal request or upon ERCOT's own initiative shall be sent out in a market bulletin with the appropriate effective date specified to inform all market participants, and a copy of the clarification or interpretation shall be maintained in a manner that is accessible to market participants. Such response shall not contain information that would identify the requesting market participant.

(6) A market participant may freely communicate informally with ERCOT employees, however, the opinion of an individual ERCOT staff member not issued as an official interpretation of ERCOT pursuant to this subsection may not be relied upon as an affirmative defense by a market participant.

(j) **Role of ERCOT in enforcing operating standards.** ERCOT shall develop and submit for commission approval a process to monitor material occurrences of non-compliance with ERCOT procedures, which shall mean occurrences that have the potential to impede ERCOT operations, or represent a risk to system reliability. Non-compliance indicators monitored by ERCOT shall include, but shall not be limited to, material occurrences of schedule control error, failing resource plan performance measures as established by ERCOT, failure to follow dispatch instructions within the required time, failure to meet ancillary services obligations, failure to submit mandatory bids or offers that may apply, and other instances of non-compliance of a similar magnitude.

(1) ERCOT shall keep a record of all such material occurrences of non-compliance with ERCOT procedures and shall develop a system for tracking recurrence of such material occurrences of non-compliance.

(2) ERCOT shall promptly provide information to and respond to questions from market participants to allow the market participant to understand and respond to alleged material occurrences of non-compliance with ERCOT procedures. However, this requirement does not relieve the market participant's operator from responding to the ERCOT operator's instruction in a timely manner and should not be interpreted as allowing the market participant's operator to argue with the ERCOT operator as to the need for compliance.

(3) ERCOT shall keep a record of the resolution of such material occurrences of non-compliance and of remedial actions taken by the market participant in each instance.

(4) ERCOT shall inform the commission staff immediately if the material occurrence of non-compliance is not resolved after the system operator has orally informed the market participant of the problem. The occurrence is not resolved if:

(A) the same instance of non-compliance is repeated more than once in a six-month period; or

(B) the occurrence continues after ERCOT has first orally notified the operator of the market participant, and subsequently notified, orally or in writing, the supervisor of the operator of the market participant.

(k) **Standards for record keeping.**

(1) A market participant who schedules through a qualified scheduling entity (QSE) that submits schedules to ERCOT on behalf of more than one market participants shall maintain records to show scheduling and bidding information for all schedules and bids that its QSE has submitted to ERCOT on its behalf, by interval.

(2) All market participants and ERCOT shall maintain records relative to market participants' activities in the ERCOT-administered markets to show:

(A) information on transactions, as defined in §25.93(c)(3) of this title (relating to Quarterly Wholesale Electricity Transaction Reports), including the date, type of transaction, amount of transaction, and entities involved;

(B) information and documentation of all planned and forced generation and transmission outages including all documentation necessary to document the reason for the outage;

(C) information described under this subsection including transaction information, information on pricing, settlement information, and other information that would be relevant to an investigation under this section, and that has been disclosed to market publications and publishers of surveys and price indices, including the date, information disclosed, and the name of the employees involved in providing the information as well as the publisher to whom it was provided; and

(D) reports of the market participant's financial information given to external parties, including the date, financial results reported, and the party to whom financial information was reported, if applicable.

(3) After the effective date of this section, all records referred to in this subsection except verbally dispatch instructions (VDIs) shall be kept for a minimum of three years from the date of the event. ERCOT shall keep VDI records for a minimum of two years. All records shall be made available to the commission for inspection upon request.

(4) A market participant shall, upon request from the commission, provide the information referred to in this subsection to the commission, and may, if applicable, provide it under a confidentiality agreement or protective order pursuant to §22.71(d) of this title (relating to Filing of Pleadings, Documents, and Other Material).

(l) **Investigation.** The commission staff may initiate an informal fact-finding review based on a complaint or upon its own initiative to obtain information regarding facts, conditions, practices, or matters that it may find necessary or proper to ascertain in order to evaluate whether any market entity has violated any provision of this section**.**

(1) The commission staff will contact the market entity whose activities are in question to provide the market entity an opportunity to explain its activities. The commission staff may require the market entity to provide information reasonably necessary for the purposes described in this subsection.

(2) If the market entity asserts that the information requested by commission staff is confidential, the information shall be provided to commission staff as confidential information related to settlement negotiations or other asserted bases for confidentiality pursuant to §22.71(d)(4) of this title.

(3) If after conducting its fact-finding review, the commission staff determines that a market entity may have violated this section, the commission staff may request that the commission initiate a formal investigation against the market entity pursuant to §22.241 of this title (relating to Investigations).

(4) If, as a result of its investigation, commission staff determines that there is evidence of a violation of this section by a market entity, the commission staff may request that the commission initiate appropriate enforcement action against the market entity. A notice of violation requesting administrative penalties or disgorgement of excess revenues shall comply with the requirements of §22.246 of this title (relating to Administrative Penalties). Adjudication of a notice of violation requesting both an administrative penalty and disgorgement of excess

revenues may be conducted within a single contested case proceeding. Additionally, for alleged violations that have been reviewed in the informal procedure established by this subsection, the commission staff shall include as part of its prima facie case:

(A) a statement either that –

(i) the commission staff has conducted the investigation allowed by this section; or

(ii) the market participant has failed to comply with the requirements of paragraph (5) of this subsection;

(B) a summary of the evidence indicating to the commission staff that the market participant has violated one of the provisions of this section;

(C) a summary of any evidence indicating to the commission staff that the market participant benefited from the alleged violation or materially harmed the market; and

(D) a statement that the staff has concluded that the market participant failed to demonstrate, in the course of the investigation, the applicability of an exclusion or affirmative defense under subsection (h) of this section.

(5) A market entity subject to an informal fact-finding review or a formal investigation by the commission has an obligation to fully cooperate with the investigation, to make its company representatives available within a reasonable period of time to discuss the subject of the investigation with the commission staff, and to respond to the commission staff's requests for information within a reasonable time frame as requested by the commission staff.

(6) The procedure for informal fact-finding review established in this subsection does not prevent any person or commission staff from filing a formal complaint with the commission pursuant to §22.242 of this title (relating to Complaints) or pursuing other relief available by law.

(m) **Remedies.** If the commission finds that a market entity is in violation of this section, the commission may seek or impose any legal remedy it determines appropriate for the violation involved, provided that the remedy of disgorgement of excess revenues shall be imposed for violations and continuing violations of PURA §39.157 and may be imposed for other violations of this section.

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 §25.503, relating to Oversight of Wholesale Market Participants is hereby adopted with changes to the text as proposed.

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

PUBLIC UTILITY COMMISSION OF TEXAS

_____

DONNA L. NELSON, CHAIRMAN

_____

KENNETH W. ANDERSON, JR., COMMISSIONER

_____

ROLANDO PABLOS, COMMISSIONER

Q:\CADM\TXR-Rules Management\Rules\Rulemaking Projects\Electric\40xxx\40073\40073adt_electric.docx