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Affiliate Restrictions (formerly the Codes of Conduct)

Historically, when a market-regulated applicant requested authority to make sales of power or ancillary services at market-based rates, the Commission also required the applicant, on a case-by-case basis, to abide by a “code of conduct” to protect captive customers and prevent affiliate abuse.¹ However, these conditions relating to making sales at market-based rates have been revised and codified in section 35.39 and renamed Affiliate Restrictions. In June 2007, the Commission issued Order No. 697, which, among other things, revised and codified the standards for obtaining and retaining market-based rates for public utilities.² In Order No. 697, the Commission stated that there is a need to have restrictions in place to prevent the transfer of benefits from captive customers to stockholders through a company’s market-regulated power sales business.³ The Commission also recognized a need for uniformity and consistency. Therefore in lieu of the case-by-case approach for codes of conduct, the Commission adopted the uniform “Affiliate Restrictions” in section 35.39 of the Commission’s regulations.⁴ The Affiliate Restrictions govern the relationship between a franchised public utility with captive customers and its market-regulated power sales affiliate(s). Section 35.39 states, among other things, that failure to satisfy the conditions of section 35.39 will constitute a violation of the Seller’s market-based rate tariff.

[Click here to link “How To Apply for Market Based Rate Authority.”](#)

Affiliate Restrictions versus Standards of Conduct

Although the Affiliate Restrictions at section 35.39 of the Commission’s regulations focus on power sales and the Standards of Conduct at Part 358 of the Commission’s regulations focus on transmission activities, both sets of requirements generally include similar types of rules governing behavior, including the independent functioning requirement and a posting requirement if non-public information is shared.

The Affiliate Restrictions govern the relationship between the franchised public utility with captive customers⁵ and its market-regulated power sales affiliate.⁶ The

¹ The earliest references to code of conduct requirements are in *Heartland Energy Services, Inc., et al.*, 68 FERC ¶ 61,223 (1994) and *LG&E Power Marketing Inc., et al.*, 68 FERC ¶ 61,247 (1994).

² *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities, Order No. 697*, 72 FR 39904 (Jul. 20, 2007), FERC Stats. & Regs. ¶ 31,252 (2007) (Final Rule), *order on rehearing and clarification*, Order No. 697-A, 123 FERC ¶ 61,055 (2008).

³ Order No. 697 at P 544.

⁴ Order No. 697 at P 544.

⁵ 18 C.F.R. § 35.36(a)(5) and 18 C.F.R. § 35.36(a)(6) (2008).

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Affiliate Restrictions require the public utility's operating personnel to function independently of the market-regulated power sales affiliate and, as revised by Order No. 697-A, imposes a posting requirement if a franchised public utility with captive customers shares non-public market information with a market-regulated power sales affiliate if the sharing could be used to the detriment of captive customers. The Affiliate Restrictions also expressly prohibit power sales between a franchised public utility with captive customers and a market-regulated power sales affiliate without first receiving Commission authorization.⁷

The Standards of Conduct govern the relationships between a Transmission Provider and its Marketing and Energy Affiliates. The Commission revised and recodified these requirements in [Order No. 2004](#) and recently issued a Notice of Proposed Rulemaking to make revisions to the Standards of Conduct, which, among other things, would eliminate the concept of Energy Affiliates.⁸

Affiliate Restrictions (formerly Codes of Conduct) Investigations and Audits

The following cases provide some examples of the types of action the Commission has taken with respect to violations of the Affiliate Restrictions (formerly Codes of Conduct.)

In 2003, the Commission issued an order approving a Stipulation and Consent Agreement revoking the market-based rate authority of a power marketer for its violations of the Codes of Conduct because the power marketer and the utility engaged in sales of power without prior Commission authorization required by the affiliate's market based power sales tariffs and section 205 of the Federal Power Act (2003 Settlement Agreement). The Commission also required the power marketer to pay a civil penalty of \$750,000 for violating section 214 of the Federal Power Act by charging an unduly preferential rate to an affiliate and refund approximately \$2.1 million of unjustly gained profits. *See Cleco Corporation, et al.*, 104 FERC ¶ 61,125 (2003).

On May 25, 2005, the Commission issued an order approving an Audit Report outlining the compliance audit findings and recommendations regarding Florida Power Corporation and Carolina Power & Light Company (Progress Companies). *See Florida Power Corporation, et al.*, 111 FERC ¶ 61,243 (2005). Among other things, the Progress

⁶ 18 C.F.R §35.36(a)(7) (2008).

⁷ Order No. 697 at P 467 and 18 C.F.R. § 35.39 (b) (2008).

⁸ *Standards of Conduct for Transmission Providers – Notice of Proposed Rulemaking*, 122 FERC ¶ 61,263 (2008), 73 Fed. Reg. 16, 228 (Mar. 27, 2008).

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Companies did not comply with the Codes of Conduct by: (1) exchanging market information as part of a strategic evaluation of organizational structures for market operations; and (2) organized its Combustion Turbine Operations group in a manner that created the opportunity for the exchange of market information inconsistent with the Codes of Conduct. The Commission required the Progress Companies to credit \$6.4 million back to its customers; restructure its marketing operations; refile its Codes of Conduct and other remedial activities for its improper activities.