

131 FERC ¶ 61,021
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
and John R. Norris.

Market-Based Rates for Wholesale Sales of Electric
Energy, Capacity and Ancillary Services By Public
Utilities

Docket No. RM04-7-007

ORDER ON REQUEST FOR CLARIFICATION

(Issued April 15, 2010)

1. On March 9, 2009, the Compliance Working Group¹ submitted a request for clarification in the Commission's market-based rate rulemaking proceeding regarding which employees can be shared for purposes of compliance with the Commission's affiliate restrictions codified as part of the market-based rate regulations promulgated in Order No. 697.² On October 28, 2009, the Compliance Working Group submitted an

¹ The Compliance Working Group states that it consists of 27 energy companies, which include integrated electric businesses, merchant generators, marketing and trading businesses, and natural gas distributors, and explains that the group was formed in mid-2008 "to develop a model [Commission] compliance program guide." Compliance Working Group March 9, 2009 Request at 2; Compliance Working Group October 28, 2009 Amended Request at 2. The members of the Compliance Working Group taking part in its request for clarification are: Allegheny Energy, Inc., American Electric Power Company, Inc., Cleco Corporation, Consumers Energy Company, Dominion Resources, Inc., Duke Energy Corporation, Edison International, El Paso Electric Company, Energy East Corp., Entergy Corporation, Exelon Corporation, FirstEnergy Corp., FPL Group, Inc., Pacific Gas and Electric Co., Progress Energy, Inc., Public Service Enterprise Group Incorporated, and Westar Energy, Inc.

² *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, at P 848-50, *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, *clarified*, 124 FERC ¶ 61,055, *order on reh'g*, Order

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amended request for clarification that supplements and restates its original request for clarification. In this order, we provide clarification regarding which employees may not be shared under the market-based rate affiliate restrictions. Concurrently with this order, the Commission is issuing a Notice of Proposed Rulemaking in Docket No. RM10-20-000 in which it proposes to revise these affiliate restrictions in order to reflect the clarification provided herein.³

Background

2. In Order No. 697, the Commission adopted market-based rate affiliate restrictions that govern the relationship between franchised public utilities with captive customers and their “market-regulated” power sales affiliates, i.e., affiliates whose power sales are regulated in whole or in part on a market-based rate basis. These restrictions govern the separation of functions, the sharing of market information, sales of non-power goods or services, and power brokering, and are based on a corporate separation approach to ensure separation of functions between a franchised public utility with captive customers and its market-regulated power sales affiliates. The Commission requires that, as a condition of receiving and retaining market-based rate authority, sellers comply with these affiliate restrictions unless otherwise permitted by Commission rule or order. Failure to satisfy the conditions set forth in the market-based rate affiliate restrictions constitutes a violation of the market-based rate tariff.⁴

3. Under the separation of functions requirement in the market-based rate affiliate restrictions, employees of market-regulated power sales affiliates must operate separately, to the maximum extent practical, from employees of affiliated franchised utilities with captive customers.⁵ Order No. 697 provides for exceptions to the separation of functions requirement for certain categories of employees who are permitted to be shared and gives examples of permissibly “shared employees.” These examples are drawn from Order No. 2004, which established the Standards of Conduct rules that were in effect at the time that Order No. 697 was issued.⁶ For instance, in Order No. 697, the

No. 697-B, FERC Stats. & Regs. ¶ 31,285 (2008), *order on reh’g*, Order No. 697-C, FERC Stats. & Regs. ¶ 31,291 (2009), *order on reh’g*, Order No. 697-D, FERC Stats. & Regs. ¶ 31,305 (2010).

³ *Market-Based Rate Affiliate Restrictions*, 131 FERC ¶ 61,033 (2010).

⁴ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 549-550.

⁵ 18 C.F.R. § 35.39(c)(2)(i) (2009).

⁶ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 561-566 (citing *Standards of Conduct for Transmission Providers*, Order No. 2004, FERC Stats. & Regs. ¶ 31,155, at (continued...))

Commission, referencing Order No. 2004, concluded that senior officers and members of boards of directors that do not participate in “directing, organizing or executing generation or market functions” would not be subject to the separation of functions.⁷

4. Like the market-based rate affiliate restrictions in Order No. 697, the Order No. 2004 Standards of Conduct required the separation of corporate or business unit functions, but permitted certain categories of employees to be shared.⁸ In Order No. 2004, the Commission identified shared support employees and senior officers and directors as the personnel that, notwithstanding the separation of functions between transmission and merchant (in the market-based rate context, the market-regulated power sales affiliate), were allowed to interact as long as “they do not participate in directing, organizing or executing transmission system operations or marketing functions; or act as a conduit to share such information with a Marketing or Energy Affiliate.”⁹

5. Following issuance of Order No. 697, Order No. 2004 was superseded by Order No. 717, the Standards of Conduct Final Rule. The Standards of Conduct Final Rule eliminated the concept of “shared employees” and replaced it with the employee functional approach. This employee functional approach rendered “continuation of the concept of ‘shared employees’ unnecessary” *for purposes of the Commission’s Standards of Conduct* since only those individuals who engage in transmission or marketing functions are required to function independently from one another.¹⁰

P 96, 99-101, 145-146 (2003), *order on reh’g*, Order No. 2004-A, FERC Stats. & Regs. ¶ 31,161 at P 134, *order on reh’g*, Order No. 2004-B, FERC Stats. & Regs. ¶ 31,166, *order on reh’g*, Order No. 2004-C, FERC Stats. & Regs. ¶ 31,172 (2004), *order on reh’g*, Order No. 2004-D, 110 FERC ¶ 61,320 (2005), *vacated and remanded as it applies to natural gas pipelines sub nom. National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831 (D.C. Cir. 2006)).

⁷ *Id.* P 562 (citing 18 C.F.R. § 358.4(a)(5)).

⁸ *Standards of Conduct for Transmission Providers*, Order No. 717, FERC Stats. & Regs. ¶ 31,280, at P 123, 129 (2008) (Standards of Conduct Final Rule), *order on reh’g*, Order No. 717-A, FERC Stats. & Regs. ¶ 31,297, *order on reh’g*, Order No. 717-B, 129 FERC ¶ 61,123 (2009).

⁹ 18 C.F.R. § 358.4(a)(5) (2004); *see also* Order No. 2004-A, FERC Stats. & Regs. ¶ 31,161.

¹⁰ Standards of Conduct Final Rule, FERC Stats. & Regs. ¶ 31,280 at P 129.

Request for Clarification

6. In its March 9, 2009 request for clarification, as supplemented in its October 28, 2009 amended request for clarification, the Compliance Working Group asks the Commission to clarify which employees are permissibly “shared employees” *for purposes of the Commission’s market-based rate affiliate restrictions*. It requests that the Commission interpret these affiliate restrictions to permit sharing of employees who are neither “transmission function employees” nor “marketing function employees” under the Standards of Conduct.¹¹ The Compliance Working Group submits that shared employees under the market-based rate affiliate restrictions are defined by reference to shared employees under the Order No. 2004-era Standards of Conduct. They add that as of the effective date of the Standards of Conduct Final Rule, November 26, 2008, the concept of shared employees is no longer applied in the Standards of Conduct context. According to the Compliance Working Group, this has created a compliance conundrum that needs to be addressed in order to enable companies and their employees to understand, and comply with, the market-based rate affiliate restrictions.

7. The Compliance Working Group states that its requested interpretation pertains to two categories of market-based rate affiliate restrictions, the “separation of functions” requirement and the “information sharing” restriction.¹² They explain that under the separation of functions requirement, employees of market-regulated power sales affiliates must operate separately, to the maximum extent practical, from employees of affiliated franchised utilities with captive customers. They add that the information sharing restriction prohibits a franchised public utility with captive customers from sharing market information with a market-regulated power sales affiliate if such sharing would be detrimental to captive customers, unless the information was simultaneously disclosed to the public.

8. The Compliance Working Group points out that there are exceptions to the separation of functions requirement; certain categories of employees can be permissibly shared. However, they note that in Order No. 697, the Commission declined a request to

¹¹ As discussed below, “transmission function employees” and “marketing function employees” are defined terms under the Standards of Conduct. *See* 18 C.F.R. §§ 358.3(d); 358.3(i) (2009); *see infra* P 35.

¹² Compliance Working Group March 9, 2009 Request at 4 (citing 18 C.F.R. §§ 35.39(c), 35.39(d) (2009)). The Compliance Working Group notes that “the interpretative issue does not bear on the categories of affiliate restrictions that apply purely on a corporate basis, namely the restrictions on affiliate sales of power, 18 C.F.R. § 35.39(b), affiliate sales of non-power goods and services, 18 C.F.R. § 35.39(e), and affiliate brokering, 18 C.F.R. § 35.39(f). *Id.* at n.7.

provide a non-exhaustive list of examples of permissibly shared support employees. The Compliance Working Group notes that all of the examples of permissibly shared employees that Order No. 697 provides are drawn from Order No. 2004-era¹³ Standards of Conduct rules that were in effect at the time that Order No. 697 was issued.

9. The Compliance Working Group acknowledges that the market-based rate affiliate restrictions adopted in Order No. 697 and the Standards of Conduct Final Rule use different approaches to ensure separation of functions for employees of public utilities and their affiliates. It contends that in the context of businesses selling power and transmission service, the three categories of permissibly shared employees identified in the regulatory text of Order No. 697¹⁴ can be broadly construed to include anyone that is not engaged in transmission or marketing functions as designated in the Standards of Conduct Final Rule. The Compliance Working Group also claims that “there is no evidence of employees *outside* these two groups [marketing function and transmission function employees] acting in a way that is consistent with the no-conduit rule, and yet harmful to captive customers.”¹⁵ According to the Compliance Working Group, while the purposes of the Standards of Conduct and the market-based rate affiliate restrictions are different, the implication is that employees and information exchanges that do not pose a significant risk of harm to competitors similarly do not pose a significant risk of harm to captive customers. The Compliance Working Group suggests that “[t]his is sensible because while the *purposes* of the rules may differ, the *root source of potential harm* in both cases is the same – an actual or potential transmission or power market transaction.”¹⁶

10. On this basis, the Compliance Working Group concludes that it is unnecessary to extend protections other than the no conduit rule to personnel other than transmission function employees or marketing function employees. Thus, it contends that no amendment to the regulatory text of the market-based rate affiliate restrictions is required to adopt its requested interpretation.¹⁷ The Compliance Working Group also claims that

¹³ *Id.* at 5-6 (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 562, n.581 and n.582).

¹⁴ The specific enumerated categories of shared employees identified in the regulatory text of Order No. 697 are “support employees,” “field and maintenance employees,” and “senior officers and boards of directors.”

¹⁵ *Id.* at 11 (emphasis in original).

¹⁶ *Id.* at 11-12 (emphasis in original).

¹⁷ *Id.* at 12. The Compliance Working Group also notes that in Order No. 697-B, issued after the Standards of Conduct Final Rule, the Commission found that risk

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its requested interpretation fulfills the objectives of the market-based rate affiliate restrictions, because under its requested interpretation, a franchised public utility with captive ratepayers could not share transmission function employees or marketing function employees with a market-regulated power sales affiliate, and no one, under the no conduit rule,¹⁸ could share the franchised utility's market information with the marketing function employees or transmission function employees of a market-regulated power sales affiliate. The Compliance Working Group contends that these protections are sufficient to prevent the customer harms that the market-based rate affiliate restrictions seek to prevent.¹⁹

11. Further, the Compliance Working Group concedes that the Commission has declined to amend its market-based rate affiliate restrictions to adopt the "employee function" approach of the Standards of Conduct Final Rule.²⁰ However, it argues that while the Standards of Conduct no longer explicitly have a category of "shared" employees, they do explicitly allow sharing of employees who are not transmission function employees or marketing function employees.²¹ It submits that because such employees can be shared under the Standards of Conduct, "they are implicitly and logically the group of 'permissibly shared' employees referred to in Order No. 697, notwithstanding that the category of shared employees has been deemed no longer necessary under the standards of conduct."²² According to the Compliance Working Group, "Order No. 697 sought to ensure consistency between the two rules by holding

management employees could be shared employees, and that no amendment to the regulatory text was necessary to make this interpretation. Compliance Working Group October 28, 2009 Amended Request at 8 (citing Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 at P 59).

¹⁸ The no conduit rule codified in the affiliate restrictions provides that "[a] franchised public utility with captive customers and a market-regulated power sales affiliate are prohibited from using anyone, including asset managers, as a conduit to circumvent the affiliate restrictions in §§35.39(a) through (g)." 18 C.F.R. § 35.39(g) (2009).

¹⁹ Compliance Working Group October 28, 2009 Amended Request at 15-16 (citing *Heartland Energy Servs., Inc.*, 68 FERC ¶ 61,223, at 62,062 (1994)).

²⁰ Compliance Working Group March 9, 2009 Request at 7 (citing Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 at P 55-59).

²¹ *Id.* at 8.

²² *Id.*

that shared employees, for purposes of the affiliate restrictions, would be the *same* as later defined by the Standards of Conduct.”²³ It further argues that an inconsistency later arose because the Standards of Conduct Final Rule ultimately revised the Standards of Conduct by eliminating the concept of shared employees altogether, not because sharing was no longer allowed, but because the Standards of Conduct had been simplified to such an extent that an exhaustive list of shared employees was no longer necessary. The Compliance Working Group thus asserts that the Commission should interpret both the separation of functions requirement and the information sharing restriction in the market-based rate affiliate restrictions to permit sharing of employees who are neither transmission function employees nor marketing function employees under the Standards of Conduct. The Compliance Working Group concludes that “[t]here is now a ‘void’ or ‘null set’ in the Affiliate Restrictions because Order No. 697 defines shared employees with reference to a later rulemaking, Order No. 717 [Standards of Conduct Final Rule], that eliminates that term altogether.”²⁴

12. The Compliance Working Group asserts that in Order No. 697, the Commission “‘clarif[ied] that the types of permissibly shared support employees under the *standards of conduct* are the types of permissibly shared support employees that *will be* allowed under the affiliate restrictions in § 35.39(c)(2)(c).”²⁵ According to the Compliance Working Group, this language indicates that Order No. 697 recognized that the Standards of Conduct would be modified in the future. It states that at the time Order No. 697 was issued, the Court of Appeals in *National Fuel Gas Supply Corp. v. FERC* had struck down portions of the Standards of Conduct and the Commission was in the process of adopting new regulations to comply with the *National Fuel* decision.²⁶ The Compliance Working Group asserts that the intent of Order No. 697 “was to ensure that the Affiliate Restrictions would be *consistent* with the subsequent treatment of shared employees in the revised Standards of Conduct.”²⁷ The Compliance Working Group also states that in

²³ Compliance Working Group October 28, 2009 Amended Request at 2 (emphasis in original).

²⁴ *Id.*

²⁵ Compliance Working Group October 28, 2009 Amended Request at 5 (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 564) (emphasis added by Compliance Working Group).

²⁶ *Id.* at 5-6 (citing *National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831 (D.C. Cir. 2006) (*National Fuel*)).

²⁷ *Id.* at 6 (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 564) (emphasis added by Compliance Working Group).

the Standards of Conduct Final Rule, the Commission declined to address the impact of the elimination of the concept of shared employees on the parallel issue arising under Order No. 697 because the problem was “beyond the scope” of the revised Standards of Conduct rulemaking.²⁸

13. The Compliance Working Group asserts that Order No. 697’s objective is to ensure consistency in the treatment of shared employees as between the market-based rate affiliate restrictions and the Standards of Conduct.²⁹ It contends that its request for clarification fulfills this objective by aligning the treatment of shared employees for purposes of the market-based rate affiliate restrictions with the approach taken in the Standards of Conduct Final Rule. Further, the Compliance Working Group states that the interpretation it requests “would, as is the case under Order No. 717 [the Standards of Conduct Final Rule], define the entire universe of permissibly shared employees, not just ‘support’ employees.”³⁰ Thus, it states that the requested clarification would extend to the other two categories of employees that are identified in the regulatory text of Order No. 697 as permissibly shared, i.e., field and maintenance employees, and officers and directors.

14. The Compliance Working Group argues that when Order No. 697 was adopted the Commission was still considering the remand of the Standards of Conduct by the *National Fuel* decision, in which the D.C. Circuit criticized and vacated the Order No. 2004-era Standards of Conduct because they sought to remedy potential abuses for which there was no actual record of abuse. The Compliance Working Group further states that “the Commission determined that the Standards of Conduct had become too unwieldy to enforce,” and “eliminated the corporate separation approach in favor of a functional approach” because “the corporate separation approach had proven too difficult to implement.”³¹ According to the Compliance Working Group, the same concerns will arise under the market-based rate affiliate restrictions unless the Commission adopts its requested interpretation because failure to adopt the clear separation envisioned by the Standards of Conduct Final Rule will embroil the Commission in making numerous findings on various employee classifications.³² The

²⁸ *Id.* (quoting Standards of Conduct Final Rule, FERC Stats. & Regs. ¶ 31,280 at P 130).

²⁹ *Id.* at 7 (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 564).

³⁰ *Id.*

³¹ *Id.* at 9 (quoting Standards of Conduct Final Rule, FERC Stats. & Regs. ¶ 31,280 at P 2, 9).

³² *Id.*

Compliance Working Group asserts that the market-based rate affiliate restrictions and Standards of Conduct “are difficult enough for the average employee to comprehend” and that “it becomes even more difficult to train employees on two sets of conflicting rules.”³³

15. As an example, the Compliance Working Group states that under the Standards of Conduct, an employee working for a regulated utility can provide support to both transmission and generation functions (including affiliates) because he is neither a transmission function employee nor marketing function employee. However, “if this employee is not on the ‘list’ of shared employees under the Affiliate Restrictions, he cannot interact with market regulated affiliates for purposes of compliance with Order No. 697.”³⁴ Thus, the Compliance Working Group claims that in training this employee, it must be explained to him that he can provide a support function for purposes of compliance with the Standards of Conduct, but cannot provide that same function for purposes of compliance with the market-based rate affiliate restrictions. The Compliance Working Group asserts that this problem can be eliminated by allowing a single system of employee classification that is uniform across both sets of rules, and argues that its requested interpretation aids compliance and enforcement. It concludes that the simplification that benefited the Standards of Conduct will equally benefit the market-based rate affiliate restrictions.

16. In addition, the Compliance Working Group asserts that there are specific situations that create complications that go beyond training. In particular, it argues that under the Standards of Conduct, support employees who work for both a franchised public utility and its market-regulated power sales affiliate could be shared because they do not perform transmission functions or engage in wholesale power sales, but that there is no clear answer under the market-based rate affiliate restrictions because the market-based rate affiliate restrictions authorize the sharing of field and maintenance employees, but not the sharing of outage scheduling personnel.³⁵ According to the Compliance Working Group, this situation means that a conservative company might choose to segregate its operation and maintenance function into two categories: (1) plant managers who might be deemed involved in outage scheduling; and (2) other plant employees supporting these managers who might not be so classified. The Compliance Working Group asserts that this creates a situation “where hundreds of plant employees can be shared but report to managers who *cannot* be shared and hence are ‘walled off’ from each

³³ *Id.* at 10. *See also* Compliance Working Group March 9, 2009 Request at 14.

³⁴ *Id.*

³⁵ *Id.* at 11-12 (citing 18 C.F.R. § 35.39(c)(2)(ii) (2009); *Florida Power Corp.*, 111 FERC ¶ 61,243 (2005)).

other, which, in turn, creates numerous compliance problems and inefficiencies that raise costs to ratepayers.”³⁶ The Compliance Working Group submits that an example of such an inefficiency is that during an outage cycle, the plant manager for the market-regulated power sales affiliate would not be permitted to know where his field and maintenance employees are at any given time because that knowledge might reveal which regulated plant was out at a certain time, thereby conveying market information to that manager.

17. The Compliance Working Group argues that such divisions of the workforce could undermine the reliability of the electric grid because “the definition of ‘market information’ in 18 C.F.R. § 35.36(a)(8) includes ‘generator outages’ and ‘historical generator volumes,’ thereby posing the risk that coordination among plant managers on lessons learned from prior outages or incidents could transfer information that cannot be shared.”³⁷ According to the Compliance Working Group, these problems could be alleviated under their requested interpretation because plant managers who do not engage in the sale of power would not be marketing function employees under the Standards of Conduct, and under the requested interpretation, they could be shared to coordinate the support for outages. The Compliance Working Group further claims that allowing the coordination of plant management among a franchised public utility and its market-regulated power sales affiliate would not result in affiliate abuse because: (1) most plant managers only deal with aspects of outage planning that are not commercially sensitive; and (2) anyone who is conducting a marketing function for a marketing affiliate is prohibited from receiving marketing information from the franchised utility, including outage schedules.³⁸ The Compliance Working Group claims that divisions of the workforce are also problematic for the Commission’s enforcement function because “[t]here is no clear basis for making distinctions in an enforcement context between plant managers, middle managers, or any other employee supporting the operation and maintenance of the generation fleet.”³⁹

18. Finally, the Compliance Working Group suggests that the rule against undue preference will continue to protect captive customers under its requested interpretation of the market-based rate affiliate restrictions. It claims that as with the Standards of Conduct Final Rule, which did not eliminate the protections provided by the prohibition on undue preference in sections 205 and 206 of the Federal Power Act,⁴⁰ its requested

³⁶ *Id.* at 12 (emphasis added by Compliance Working Group).

³⁷ *Id.* at 13.

³⁸ *Id.* at 14.

³⁹ *Id.*

⁴⁰ *Id.* at 17 (citing 16 U.S.C. §§ 824d-824e (2006)).

interpretation does not affect this statutory backstop. The Compliance Working Group argues that the market-based rate affiliate restrictions are, and should remain, prophylactic rules, and that their costs should be weighed against their effectiveness in preventing harm that likely would occur in the absence of the rules.⁴¹

Notice of Filing and Responsive Pleadings

19. Notice of the Compliance Working Group's March 9, 2009 and October 28, 2009 filings was published in the *Federal Register*, 74 FR 66637 (2009), with comments due on or before November 30, 2009. The Transmission Access Policy Study Group (TAPS) submitted comments opposing the Compliance Working Group's request, and the Edison Electric Institute (EEI) submitted comments in support of the Compliance Working Group's request.

20. TAPS states that it has been concerned in the past about the abuse of market power associated with market-based rate authority, and opposes the Compliance Working Group's "proposed radical revision of the Commission's current [market-based rate] Affiliate Restrictions."⁴² TAPS argues that although the Compliance Working Group styled its pleading as a request for clarification, the Compliance Working Group is asking the Commission to modify fundamentally the current market-based rate protections against affiliate abuse. According to TAPS, if the Compliance Working Group's request were granted, the functional effect would be to permit closer and problematic ties between those involved in marketing power under market-based rate authority and those involved in marketing power to captive customers.

21. TAPS argues that the Standards of Conduct restrictions are designed to protect against the particular problem of affiliate transmission abuses, while the market-based rate affiliate restrictions are intended to protect against transferring captive customer benefits to stockholders through a company's non-regulated power sales business.⁴³ According to TAPS, it makes no sense to replace the market-based rate affiliate restrictions with Standards of Conduct intended to protect against the very different problem of affiliate transmission abuse. Further, TAPS argues that "[t]he requested

⁴¹ *Id.* (citing *Nat'l Fuel Gas Supply Corp.*, 468 F.3d at 844; *InterCoast Power Mktg. Co.*, 68 FERC ¶ 61,248, at 62,133 (1994); *Inquiry Into Alleged Anticompetitive Practices Related to Mktg. Affiliates of Interstate Pipelines*, Order No. 497, FERC Stats. & Regs. ¶ 30,820 (1988), *order on reh'g*, Order No. 497-A, FERC Stats. & Regs. ¶ 30,868 at 31,589 (1989), *aff'd*, *Tenneco Gas v. FERC*, 969 F.2d 1187 (D.C. Cir. 1992)).

⁴² TAPS November 30, 2009 Response at 2.

⁴³ *Id.* (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 544).

[Compliance Working Group] relief would largely gut the existing [market-based rate] Affiliate Restrictions and leave no meaningful protections in their place.”⁴⁴ TAPS submits that an example of affiliate abuse is collusion between a market-regulated power sales affiliate and a franchised public utility intended to steer a particular sale to the benefit of the market-based rate seller, as opposed to the affiliate public utility, for the benefit of parent company stockholders, and at the expense of a public utility’s captive customers. TAPS asserts that this kind of collusion, and indeed most if not all of the affiliate abuses targeted by the market-based rate affiliate restrictions, have nothing do with undue preferences relating to transmission.

22. TAPS also states that “[u]nlike the Standards of Conduct, which are intended to prevent the improper sharing of ‘marketing function information’ and ‘transmission functioning information,’ the [market-based rate] affiliate restrictions are intended to prevent the improper sharing of “market information.”⁴⁵ In this regard, TAPS argues that market information is defined functionally, and expansively.⁴⁶ TAPS emphasizes that the definition of “market information” in the market-based rate affiliate restrictions does not encompass transmission information because the Standards of Conduct already protect against the improper sharing of affiliate transmission information.

23. In response to the Compliance Working Group’s argument that because the Commission has eliminated the concept of shared employees under the Standards of Conduct “[t]here is now a ‘void’ or a ‘null set’ in the Affiliate Restrictions[,]” TAPS asserts that “[w]hile it is true that [the Commission] can no longer rely upon the contemplated ‘affiliate restrictions in section 35.39(c)(2)(c)’ to identify specifically the permitted shared employees under the [affiliate restrictions], there is somewhat less of a substantive void than meets the eye given [the Commission’s] elucidation of the kinds of permitted shared support individuals.”⁴⁷ TAPS states that a specific elucidation of permitted shared support employees may be desirable, but this appears to be a defined and limited issue that the Commission can address without the “kind of massive and problematic revisions sought by the [Compliance Working Group].”⁴⁸

⁴⁴ *Id.*

⁴⁵ *Id.* at 5.

⁴⁶ *Id.* at 5 (citing Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 593; 18 C.F.R. § 35.36(a)(8) (2009)).

⁴⁷ *Id.* at 6.

⁴⁸ *Id.*

24. TAPS also argues that the Compliance Working Group uses the supposed inconsistency between the Standards of Conduct and the market-based rate affiliate restrictions as a springboard for radically rewriting the market-based rate affiliate restrictions, and argues that the Compliance Working Group wants the Commission to rely on the transmission provider Standards of Conduct Independent Functioning Rule combined with the no conduit rule, but nowhere addresses or explains why the Commission should abolish the core safeguard of corporate separation.

25. TAPS contends that the Standards of Conduct require the very different separation of individuals involved in transmission functions from those involved in marketing functions. It states that if the Compliance Working Group's proposal were adopted, nothing would prevent the same individual from managing both a franchised utility's standard offer service auction bidding and also managing the market-regulated power sales affiliate's standard offer service offers. According to TAPS, this would be the very kind of affiliate abuse, and disadvantaging of captive customers, that the market-based rate affiliate restrictions are intended to protect against. TAPS further argues that the no conduit rule does not remedy the shortcomings of the Compliance Working Group proposal. It states that it is unclear what would remain of the no conduit rule if the Commission were to abolish the core affiliate restriction of corporate separation. Further, TAPS states that under the Compliance Working Group proposal, the same individual could perform marketing functions for both a franchised utility and a market-regulated power sales affiliate. TAPS states that the Compliance Working Group might argue that this is a violation of the no conduit rule, "but this would require the tortuous interpretation that a particular individual was operating as an improper conduit to himself: one part of his brain impermissibly knew things that another side of his brain was forbidden from knowing."⁴⁹ TAPS argues that the Commission has not relied exclusively upon the no conduit rule as an adequate safeguard in and of itself, either with respect to the market-based rate affiliate restrictions, or to the transmission Standards of Conduct. According to TAPS, with respect to the affiliate restrictions, the prohibition against employee sharing is a primary measure of protection against market-based rate affiliate abuse and there is no good reason to abandon it.

26. TAPS also argues that to the extent the Commission seeks to fill the shared employee "gap" or to adopt an employee functional approach tailored to protecting against market-based rate affiliate abuses, it should do so by means of a separate, narrow, notice and comment rulemaking.

27. EEI states that Compliance Working Group's request for clarification is reasonable and appropriate. EEI states that it supported the simplification of the Standards of Conduct on the issue of shared employees, and agreed strongly with the

⁴⁹ *Id.* at 8.

Commission's adoption in the Standards of Conduct Final Rule of an employee functional approach over the prior corporate separation approach. EEI encourages the Commission to adopt the same functional approach in the market-based rate context, to ensure consistency between the two programs and to align and simplify compliance and enforcement of this aspect of the programs. EEI therefore encourages the Commission to clarify that the separation of function and information sharing provisions of the market-based rate affiliate restrictions do not require corporate separation of employees or use of a specific category of "shared employees," but will be satisfied by compliance with the Independent Functioning Rule as set forth in the Standards of Conduct Final Rule.⁵⁰

28. On December 10, 2009, the Compliance Working Group submitted reply comments in response to TAPS. Therein, it claims that TAPS misconstrues its requested relief. The Compliance Working Group states that it is not asking the Commission to amend the rules, but rather has asked for a new interpretation of an existing exception to the Independent Functioning Rule in light of the fact that the old interpretation is no longer applicable. The Compliance Working Group adds that it is not asking the Commission to allow a single individual to perform marketing functions for both a franchised utility and a market-regulated power sales affiliate. According to the Compliance Working Group, under its proposal, the independent functioning requirement will still apply to prohibit sharing of marketing function personnel. The Compliance Working Group also asserts that neither TAPS nor any other party has offered any evidence of the sort required by *National Fuel* "to justify an interpretation that would make these rules more complex and difficult to comply with and enforce than they need to be."⁵¹

29. On December 22, 2009, TAPS submitted reply comments in response to the Compliance Working Group's reply comments. TAPS argues that the core shortcoming of the Compliance Working Group's approach is that the definition of "marketing

⁵⁰ EEI November 30, 2009 Comments at 2-3. In its comments on the Compliance Working Group's request, EEI also encourages Commission action on EEI's request for rehearing of Order No. 697-C on the issue of sales at the metered boundary of a mitigated market. EEI reiterates its requests for an extension of the deadline for complying with the tariff provision governing sales at the metered boundary of a mitigated market as revised in Order No. 697-C until the Commission issues an order responding to EEI's rehearing request, or following a technical conference if the Commission does intend to retain border sales constraints. *Id.* at 3-4. This issue was addressed in Order No. 697-D. *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697-D, FERC Stats. & Regs. ¶ 31,305.

⁵¹ Compliance Working Group December 10, 2009 Reply Comments at 5 (citing *National Fuel*, 468 F.3d at 843-44).

function” under the transmission Standards of Conduct is specific and narrow, and is defined to encompass only sales. TAPS adds that the market-based rate affiliate restrictions are intended to prevent the improper sharing of “market information,” which TAPS argues is defined functionally, and expansively, and includes information concerning power purchase activities as well as sales activities. TAPS asserts that under the Compliance Working Group proposal, “a franchised utility and an affiliated merchant seller could share an employee who was involved in ‘market’ activities within the meaning of Order No. 697” and that these entities “could share an employee who was involved in power purchasing, an activity which falls outside of the Standards of Conduct ‘[marketing] function’ and ‘transmission function.’”⁵²

Discussion

30. We will deny the Compliance Working Group’s request that the Commission interpret the market-based rate affiliate restrictions adopted in Order No. 697 to permit the sharing of employees who are neither transmission function employees nor marketing function employees under the Standards of Conduct Final Rule. For the reasons discussed below, we find that it would be inappropriate to interpret the market-based rate affiliate restrictions to permit the sharing of employees who are neither transmission function employees nor marketing function employees under the Standards of Conduct. However, we will grant clarification to the extent that we address the Compliance Working Group’s concerns regarding compliance with the market-based rate affiliate restrictions given that the Commission’s rules regarding which employees may be shared under the Standards of Conduct have changed. In order to provide guidance to the industry, and to address the concerns raised by TAPS concerning the potential for affiliate abuse under the Compliance Working Group’s requested interpretation, we will clarify which employees may not be shared under the market-based rate affiliate restrictions.

31. The market-based rate affiliate restrictions adopted in Order No. 697 are based on a corporate separation approach to ensure separation of functions and restrict a franchised public utility with captive customers from sharing market information with its market-regulated power sales affiliates.⁵³ In adopting these affiliate restrictions, the Commission

⁵² TAPS December 22, 2009 Reply Comments at 3.

⁵³ The market-based rate regulations define “market information” as “non-public information related to the electric energy and power business including, but not limited to, information regarding sales, cost of production, generator outages, generator heat rates, unconsummated transactions, or historical generator volumes. Market information includes information from either affiliates or non-affiliates.” 18 C.F.R. § 35.36(a)(8) (2009).

explained that they are intended to guard against the potential for a franchised public utility with captive customers to interact with a market-regulated power sales affiliate in ways that transfer benefits to the affiliate and its stockholders to the detriment of the captive customers.⁵⁴ In contrast, the Standards of Conduct are based on an employee functional model. Their purpose is to prevent transmission providers from giving undue preferences to their marketing affiliates (or wholesale merchant functions).⁵⁵

32. The Compliance Working Group misconstrues Order No. 697 in arguing that the intent of Order No. 697 “was to ensure that the Affiliate Restrictions would be *consistent* with the subsequent treatment of shared employees in the revised Standards of Conduct.”⁵⁶ In Order No. 697, the Commission followed its policy in Order No. 2004 of permitting sharing of certain personnel to take advantage of the efficiencies of corporate integration, and clarified that the “types of permissibly shared support employees under the standards of conduct are the types of permissibly shared support employees that will be allowed under the affiliate restrictions in § 35.39(c)(2)(c).”⁵⁷ In making this statement, the Commission did not indicate that it intended to make the affiliate restrictions consistent with the revised Standards of Conduct, which had not yet been adopted. Rather, in explaining that permissibly shared support employees “include those in legal, accounting, human resources, travel and information technology” the Commission cited to Order No. 2004, which established the Standards of Conduct rules that were in effect at the time that Order No. 697 was issued.⁵⁸

33. We disagree with the Compliance Working Group’s argument that the corporate separation approach is too difficult to implement, and that the Commission should grant the Compliance Working Group’s requested interpretation in order avoid making findings on various employee classifications. While the Commission eliminated “the corporate separation approach *to separating a transmission provider’s transmission function employees from its marketing function employees*” because the corporate separation approach was difficult to implement in the Standards of Conduct context, the

⁵⁴ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 513, 544; Order No. 697-A, FERC Stats. & Regs. ¶ 31,268 at P 188.

⁵⁵ Standards of Conduct Final Rule, FERC Stats. & Regs. ¶ 31,280 at P 23.

⁵⁶ Compliance Working Group October 28, 2009 Amended Request for Clarification at 6 (emphasis added by Compliance Working Group).

⁵⁷ Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 564.

⁵⁸ *Id.* (citing *Standards of Conduct for Transmission Providers*, Order No. 2004, FERC Stats. & Regs. ¶ 31,155, at P 96 (2003)).

Commission has not found that the corporate separation approach as applied in the *market-based rate affiliate restrictions* context is too difficult to implement. Applying the corporate separation approach in the market-based rate affiliate restrictions context is more appropriate than applying the employee functional approach used in the Standards of Conduct. This is because the market-based rate affiliate restrictions are intended to ensure separation of functions and restrict the sharing of market information between separate corporate entities: a franchised public utility with captive customers and its market-regulated power sales affiliates. The purpose of this separation of functions and the restrictions on the sharing of market information in the market-based rate affiliate restrictions is to guard against the potential for a franchised public utility with captive customers to interact with its market-regulated power sales affiliate in ways that transfer benefits to the affiliate's stockholders to the detriment of the *captive customers*. By contrast, the purpose of the Standards of Conduct is to prevent transmission providers from giving *undue preference* to their wholesale merchant and/or marketing functions (as well as separate, affiliated corporate entities) over *non-affiliated customers*.⁵⁹

34. Further, the discussion and clarification provided below⁶⁰ address the issues raised by the Compliance Working Group concerning compliance with the affiliate restrictions given that the Commission's rules regarding which employees may be shared under the Standards of Conduct have changed. In particular, we identify below employees that might fall outside the definition of "marketing function employee" in the Standards of Conduct, and therefore could be shared under the Standards of Conduct, but who may not be shared under the market-based rate affiliate restrictions.

35. Under the Independent Functioning Rule of the current Standards of Conduct, all employees that are neither marketing function employees nor transmission function employees may be shared.⁶¹ As defined under the Standards of Conduct, "marketing

⁵⁹ Standards of Conduct Final Rule, FERC Stats. & Regs. ¶ 31,280 at P 23.

⁶⁰ *See infra* P 39-42.

⁶¹ The Independent Functioning Rule provides that: (a) General rule. Except as permitted in this part or otherwise permitted by Commission order, a transmission provider's transmission function employees must function independently of its marketing function employees.

(b) Separation of functions.

(1) A transmission provider is prohibited from permitting its marketing function employees to:

(i) Conduct transmission functions; or

(ii) Have access to the system control center or similar facilities used for transmission operations that differs in any way from the access available to other transmission customers.

function employee” means “an employee, contractor, consultant or agent of a transmission provider or of an affiliate of a transmission provider who actively and personally engages on a day-to-day basis in marketing functions.”⁶² “Marketing functions” means “in the case of public utilities and their affiliates, the sale for resale in interstate commerce, or the submission of offers to sell in interstate commerce, of electric energy or capacity, demand response, virtual transactions, or financial or physical transmission rights, all as subject to an exclusion for bundled retail sales, including sales of electric energy made by providers of last resort....”⁶³ Thus, the Standards of Conduct definition of “marketing function employee” may be read to be limited to those employees engaged in sales.

36. Under the market-based rate affiliate restrictions, franchised public utilities with captive customers are permitted to share support employees and field and maintenance employees with their market-regulated power sales affiliates. The market-based rate affiliate restrictions also allow the sharing of senior officers and members of boards of directors provided that these individuals do not engage in the functions of directing, organizing and executing the business decisions of either the franchised public utility with captive customers or the marketing affiliate.⁶⁴

(2) A transmission provider is prohibited from permitting its transmission function employees to conduct marketing functions.

18 C.F.R. § 358.5 (2009).

⁶² 18 C.F.R. § 358.3(d) (2009).

⁶³ 18 C.F.R. § 358.3(c) (2009). The Standards of Conduct define a “transmission function employee” as “an employee, contractor, consultant or agent of a transmission provider who actively and personally engages on a day-to-day basis in transmission functions.” 18 C.F.R. § 358.3(i) (2009).

⁶⁴ 18 C.F.R. § 35.39(c)(2)(ii) (2009). Specifically, the market-based rate affiliate restrictions provide that “Franchised public utilities with captive customers are permitted to share support employees, and field and maintenance employees with their market-regulated power sales affiliates. Franchised public utilities with captive customers are also permitted to share senior officers and boards of directors with their market-regulated power sales affiliates; provided, however, that the shared officers and boards of directors must not participate in directing, organizing or executing generation or market functions.” 18 C.F.R. § 35.39(c)(2)(ii) (2009); *see also* Order No. 697, FERC Stats. & Regs. ¶ 31,252 at P 562. Under the information sharing restriction, “[a] franchised public utility with captive customers may not share market information with a market-regulated power sales affiliate if the sharing could be used to the detriment of captive customers,

(continued...)

37. “Marketing function employee” is not a defined term in the market-based rate regulations adopted in Order No. 697.⁶⁵ Further, the restrictions on which employees may be shared under the market-based rate affiliate restrictions are not limited to those employees who are engaged in sales. As the Commission clarified in Order No. 697-A, under the market-based rate affiliate restrictions, “shared employees may not be involved in decisions regarding the marketing or sale of electricity from the facilities, may not make economic dispatch decisions, and may not determine the timing of scheduled outages for facilities.”⁶⁶ The Commission further stated in Order No. 697-A that “to ensure that captive customers are not harmed, shared field and maintenance employees may not make economic dispatch decisions or determine when scheduled maintenance outages (as opposed to emergency forced outages) will occur.”⁶⁷

38. The Compliance Working Group suggests that its requested interpretation could fulfill the objective of the market-based rate affiliate restrictions, which is to guard against the potential for a franchised public utility with captive customers to interact with a market-regulated power sales affiliate in ways that transfer benefits to the affiliate and its stockholders to the detriment of the captive customers. We disagree. As discussed below, the Standards of Conduct definition of marketing function employee does not include certain employees who may not be shared under the market-based rate affiliate restrictions (for instance, employees that make economic dispatch decisions or that determine the timing of scheduled outages). Thus, granting the Compliance Working

unless simultaneously disclosed to the public.” 18 C.F.R. § 35.39(d)(1) (2009). However, “[p]ermissibly shared support employees, field and maintenance employees and senior officers and board of directors under §§ 35.39(c)(2)(ii) may have access to information covered by the prohibition of § 35.39(d)(1), subject to the no-conduit provision in § 35.39(g).” 18 C.F.R. § 35.39(d)(2) (2009).

⁶⁵ In Order No. 697-B, in response to EEI’s request on rehearing that the Commission amend the regulatory text at 18 C.F.R. § 35.39(c) to reflect that all employees who are neither transmission nor wholesale marketing function employees are not within the scope of the independent functioning rule, but remain subject to the no conduit rule, the Commission explained that “the reference in Order No. 697-A to ‘marketing function employees as defined in the standards of conduct’ may have been misleading because the affiliate restrictions address franchised public utilities with captive customers and market-regulated power sales affiliates, not ‘marketing function employees as defined in the standards of conduct.’” Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 at P 59.

⁶⁶ Order No. 697-A, FERC Stats. & Regs. ¶ 31,268 at P 253.

⁶⁷ *Id.*

Group's requested interpretation would permit market-based rate sellers to share certain employees that the Commission has stated may not currently be shared under the affiliate restrictions and therefore would not fulfill the objective of those restrictions.

39. While we do not grant the Compliance Working Group's request, in an effort to provide guidance to the industry to facilitate compliance with the market-based rate affiliate restrictions, we identify below certain employees who cannot be shared under the affiliate restrictions, but who nevertheless might not be "marketing function employees" under the Standards of Conduct.

40. Responsibility for economic dispatch or the timing of scheduled outages, for example, is not a "marketing function" under the Standards of Conduct and, therefore, engaging in these activities would not cause an employee to be a marketing function employee subject to the Independent Functioning Rule (and therefore, those employees could be shared). However, consistent with the Commission's determinations in Order No. 697-A, we clarify that, for purposes of compliance with the market-based rate affiliate restrictions, a franchised public utility with captive customers and its market-regulated power sales affiliates may not share employees that make economic dispatch decisions or that determine the timing of scheduled outages.⁶⁸

41. Similarly, responsibility for resource planning or fuel procurement is not a "marketing function" and, therefore, employees that engage in these activities would not be marketing function employees that are subject to the Independent Functioning Rule (and therefore could be shared). We clarify that franchised public utilities with captive customers are prohibited from sharing employees that engage in resource planning or fuel procurement with their market-regulated power sales affiliates. If the franchised public utility and its market-regulated power sales affiliate are permitted to share employees that make strategic decisions about future generation supply, such as deciding when and/or where to build or acquire generating capacity, such strategic decision-making by a shared employee could result in generation being built or acquired for the benefit of the market-regulated power sales affiliate, and at the expense of the captive customers of the franchised public utility. In this regard, we note that the corporate entity has an inherent incentive to decrease its market-regulated power sales affiliate's costs in order to maximize profits for shareholders.

42. Similarly, a shared employee that procures fuel for both the franchised public utility and the market-regulated power sales affiliate may have the incentive to allocate purchases of lower priced fuel supplies to the market-regulated power sales affiliate while allocating purchases of higher priced fuel supplies to the franchised public utility. By

⁶⁸ *Id.*

contrast, if the two entities are required to independently procure fuel, they would compete for the market's best priced fuel.

43. Given that the definition of marketing function employee under the Standards of Conduct does not specifically address employees that determine the timing of scheduled outages or that engage in economic dispatch, fuel procurement, or resource planning, we clarify that employees engaging in these activities⁶⁹ are prohibited from being shared under the market-based rate affiliate restrictions, absent an explicit waiver from the Commission. We find that for purposes of the market-based rate affiliate restrictions, the Commission should retain its authority to review on a case-by-case basis circumstances where affiliates seek to share employees that may not be shared under these affiliate restrictions. As an example, in a recent order the Commission granted Cleco Power LLC and its affiliate Acadia Power Partners, LLC *limited* waiver of certain affiliate restrictions in order to allow Cleco Power to share with its affiliate Acadia, in addition to support and field and maintenance employees, certain other employees who schedule outages for Cleco Power generation facilities so that those Cleco Power employees may also provide operating and maintenance services to Acadia at a generation facility owned by Acadia.⁷⁰ Under the Compliance Working Group's requested interpretation, no such waiver would have been required. However, it is necessary for the Commission to review such arrangements to ensure that no harm to captive customers would result from the sharing of such employees.

44. We reject the Compliance Working Group's argument that there is no need to extend protections other than the no conduit rule, which prohibits a franchised public utility with captive customers and a market-regulated power sales affiliate from using anyone as a conduit to circumvent the affiliate restrictions, beyond transmission function employees and marketing function employees. We also reject its argument that the rule against undue preference will protect captive customers under the Compliance Working Group's requested interpretation. The Compliance Working Group's claims that the no conduit rule and the prohibition against undue preference are sufficient to protect captive customers essentially challenge the separation of functions and information sharing provisions as codified in the market-based rate affiliate restrictions. In this regard, we agree with TAPS that the Compliance Working Group is asking the Commission to modify fundamentally the current market based rate affiliate restrictions. Such arguments

⁶⁹ The prohibition on sharing employees that engage in resource planning applies only to the sharing of employees between a franchised public utility and its market-regulated power sales affiliate, and is not intended to alter resource planning activities by transmission providers that are permitted under the Standards of Conduct.

⁷⁰ *Cleco Power LLC*, 130 FERC ¶ 61,102 (2010).

constitute an out-of-time attempt to re-litigate the need for these affiliate restrictions after the time for rehearing has expired. Because the Compliance Working Group did not raise these arguments within 30 days of the issuance of Order No. 697,⁷¹ we reject these arguments.

45. In light of the guidance and clarification provided in this order regarding which employees may not be shared under the market-based rate affiliate restrictions, we are proposing to revise the text of the “separation of functions” and “information sharing” provisions of the affiliate restrictions in the regulations in a separate Notice of Proposed Rulemaking, which is being issued concurrently in Docket No. RM10-20-000.⁷²

The Commission orders:

The Compliance Working Group’s request for clarification is hereby granted in part and denied in part, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

⁷¹ 18 C.F.R. § 385.713 (2009) (stating that “[a] request for rehearing by a party must be filed not later than 30 days after the issuance of any final decision or other final order in a proceeding.”).

⁷² *Market-Based Rate Affiliate Restrictions*, 131 FERC ¶ 61,033 (2010).