UNITED STATES OF AMERICA 146 FERC ¶ 63,028
FEDERAL ENERGY REGULATORY COMMISSION

Puget Sound Energy, Inc.

Complainant

v. Docket No. EL01-10-085

All Jurisdictional Sellers of Energy and/or Capacity at Wholesale into Electric Energy and/or Capacity Markets in the Pacific Northwest, Including Parties to the Western Systems Power Pool Agreement

Respondents

# INITIAL DECISION

(Issued March 28, 2014)

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## Glossary

| Term | Definition |
|---|---|
| AB1X | California Assembly Bill 1X, the state statute that created CERS. |
| AESO | Alberta Electric System Operator |
| Avista or Avista Entities | Avista Utilities and Avista Energy, collectively |
| Avista Corporation d/b/a Avista Utilities | Avista Utilities |
| Avista Energy, Inc. | Avista Energy |
| B2B transactions | “Back-to-Back” Transactions in which an entity bought energy and immediately resold the energy |
| BEEP Stack | The ISO’s spot market for imbalance energy |
| BPA | Bonneville Power Administration |
| The California Parties | The People of the State of California ex rel. Kamala D. Harris, Attorney General, the Public Utilities Commission of the State of California, and Southern California Edison Company |
| California Refund Proceeding | Litigation in FERC Docket No. EL00-95 |
| Cargill | Cargill Power Markets, L.L.C. |
| CDWR | The California Department of Water Resources |

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|---|---|
| Centralia | Centralia Generating Station |
| CERS | The California Energy Resources Scheduling division of the California Department of Water Resources |
| CERS Period | The period from January 17, 2001 through June 20, 2001 |
| CFTC | The Commodities Futures Trading Commission |
| COB or Malin | The California Oregon Border trading hub |
| Constellation | Exelon Generation Company, LLC, Successor-In-Interest to Constellation Energy Commodities Group, Inc. and Constellation Power Source, Inc. |
| Coral or Shell Energy | Coral Power LLC (n/k/a Shell Energy North America (US), L.P.) |
| CPUC | The Public Utilities Commission of the State of California |
| day-ahead transactions | Energy transactions in which product delivery occurs during the 24-hour time period following the trading day, or, in the case of weekends, the two or three days following the trading day |
| day-of transactions | Real-time and hour-ahead transactions |
| El Paso | El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.) |
| FPA | Federal Power Act |
| Glendale | City of Glendale, California |

| | |
|---|---|
| IOUs | Investor Owned Utilities. California's Investor Owned Utilities are Pacific Gas and Electric Company; Southern California Edison Company; and San Diego Gas & Electric Company |
| ISO or CAISO | The California Independent System Operator Corporation |
| Mid-C | The Mid-Columbia trading hub, located in Washington State |
| MMCP | The Mitigated Market Clearing Price |
| MMIP | Market Monitoring and Information Protocol |
| MW | Megawatt |
| MWh | Megawatt-hour |
| NOB | The Nevada Oregon Border trading hub |
| NP15 | NP15 comprises the California Independent System Operator's northern congestion zone. The zone is north of the main north-south AC transmission pathway, California Path 15 |
| OOM | Out of Market transactions conducted by the CAISO |
| Order Granting Interlocutory Appeal | *Puget Sound Energy, Inc.*, 141 FERC ¶ 61,248 (2012) |
| Order on Remand | *Puget Sound Energy, Inc.*, 137 FERC ¶ 61,001 (2011) |
| Order on Rehearing | *Puget Sound Energy, Inc.*, 143 FERC ¶ 61,020 (2013) |

| | |
|---|---|
| PG&E | Pacific Gas and Electric Company |
| PNW | Pacific Northwest |
| Portland General or PGE | Portland General Electric Company |
| Powerex | Powerex Corp. |
| PPoA | Power Pool of Alberta |
| PPL or PPL Parties | PPL EnergyPlus, L.L.C. and PPL Montana, L.L.C. |
| PSCo | Public Service Company of Colorado |
| PX or CalPX | The California Power Exchange Corporation |
| QFs | Qualifying Facilities |
| real-time transactions | Energy purchases made after the day-ahead energy market closed |
| SCE or SoCal Edison | Southern California Edison Company |
| SCL | Seattle City Light |
| SDG&E | San Diego Gas and Electric Company |
| Seattle | City of Seattle, Washington |

| | |
|---|---|
| Section 206 Period | The period from December 25, 2000 through June 20, 2001 |
| Section 309 Period | The period from January 1, 2000 through December 24, 2000 |
| SP15 | SP15 comprises the California Independent System Operator's southern congestion zone. The zone is south of the main north-south AC transmission pathway, California Path 15 |
| TransAlta | TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. |
| TransCanada | TransCanada Energy Ltd. |
| Trial Staff | Commission Trial Staff |
| WECC | Western Electricity Coordinating Council |
| WSCC | Western Systems Coordinating Council |
| WSPP | WSPP, Inc. or its predecessor, the Western Systems Power Pool |
| WSPP Agreement | Western Systems Power Pool Agreement |

## I. Statement of the Case

1. This proceeding concerns bilateral wholesale energy contracts entered into by the parties in the Pacific Northwest spot market during 2000 and 2001, involving numerous Commission-jurisdictional and non-Commission-jurisdictional entities.[1] The central issue to be addressed in this proceeding is whether the City of Seattle, Washington (Seattle) and the California Parties[2] have made the necessary showing to avoid or overcome the *Mobile-Sierra* presumption that the bilateral spot market contracts at issue are just and reasonable under section 206 of the Federal Power Act (FPA) or to obtain relief under section 309 of the FPA.

2. Initially this proceeding encompassed a number of other Respondents who have since settled,[3] but whose active participation in earlier stages of this contentious and lengthy litigation have left behind a voluminous and complex record to sift out and weigh.[4] The remaining nine Respondents to Seattle's allegations are: Avista Energy,

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[1] *Puget Sound Energy, Inc*., 137 FERC ¶ 61,001, at P 2 (2011) (Order on Remand), *order on reh'g*, 143 FERC ¶ 61,020, at P 2 (2013) (Order on Rehearing).

[2] The California Parties are the People of the State of California ex rel. Kamala D. Harris, Attorney General, the Public Utilities Commission of the State of California, and Southern California Edison Company.

[3] Since filing their preliminary statement of claims in August 2012, Seattle has entered into settlement agreements with Idaho Power Company and IDACORP Energy, L.P.; Nevada Power Company and Sierra Pacific Power Company; PacifiCorp; Puget Sound Energy, Inc.; MPS Merchant Services, Inc. and MPS Canada Corp.; Dynegy Power Marketing, LLC; TransCanada Energy Ltd.; Morgan Stanley Capital Group Inc.; BP Energy Company; Pinnacle West Capital Corporation and Arizona Public Service Company; American Electric Power Service Corporation; Iberdrola Renewables, LLC; ENMAX Corporation; and Powerex Corp. The California Parties have entered into settlement agreements with Avista Energy, Inc.; Avista Corporation d/b/a Avista Utilities; Powerex Corp.; and TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc.

[4] The Phase I hearing commenced on August 27, 2013 and ended on October 24, 2013, with testimony by 33 witnesses during 24 hearing days over 7 weeks (excluding a two-week recess). The scheduled hearing days and witnesses were substantially reduced as the result of settlements between Powerex Corp. and the California Parties and between Powerex Corp. and the City of Seattle that were reached just prior to and during the hearing, respectively. Settlements post-hearing have been reached between the California Parties and Avista Utilities, Avista Energy, and TransAlta. By stipulation of

(continued…)

Inc. (Avista Energy); Avista Corporation d/b/a Avista Utilities (Avista Utilities); Cargill Power Markets, LLC (Cargill); El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.) (El Paso); Exelon Generation Company, LLC, Successor-In-Interest to Constellation Energy Commodities Group, Inc. and Constellation Power Source, Inc. (Constellation); PPL Montana, LLC and PPL EnergyPlus, LLC (PPL); Public Service Company of Colorado (PSCo); Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral); and TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. (TransAlta). The California Parties have asserted claims against the following two remaining Respondents: TransCanada Energy Ltd. (TransCanada) and Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral).

3. For the reasons discussed herein below, it is the determination of the undersigned that Seattle has not established a basis for abrogating any of the contracts at issue in this proceeding or for receiving any refunds. With respect to the California Parties' claims, the undersigned finds that the California Parties have not established a basis for abrogating any of the contracts at issue with TransCanada in this proceeding or for receiving any refunds with respect to those contracts with TransCanada. The California Parties have established a ***prima facie*** case that at least 47 of the subject contracts with Coral were tainted by False Export activities and that as many as 119 of the subject contracts with Coral may have been tainted by "bad faith." There remain significant questions of fact and law with respect to those transactions that must be resolved in Phase II of this proceeding.[5] In Phase II, Coral may demonstrate that the contracts were not in fact False Exports or tainted by "bad faith" and/or that the rates charged to CERS with respect to these contracts were nonetheless just and reasonable based on Coral's actual costs and market conditions.

4. Subject to review by the Commission on exceptions or on its own motion, as provided by the Commission's Rules of Practice and Procedure: within thirty days from the issuance of the final order of the Commission addressing this Initial Decision, and in

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the parties and the Chief Judge's Order Granting Procedural Relief, issues between those settling parties are not addressed in this Initial Decision. *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Mar. 6, 2014) (Order of Chief Judge Suspending Initial Decision as to the California Parties' Allegations Against Settling Parties and Granting Brief Extension of Initial Decision Date).

[5] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 13, 2012) (Order Confirming Rulings from the September 6, 2012 Prehearing Conference); *Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 14, 2012) (Order of Chief Judge Phasing Proceeding and Suspending Procedural Timelines for Phase II).

accordance with Phase I of this proceeding, the California Parties and Coral are hereby directed to file pre-hearing briefs addressing the issues remaining to be adjudicated in Phase II of this proceeding in accordance with the findings of fact and conclusions of law set forth in this Initial Decision.

## II. Background and Procedural History

### A. Western Energy Crisis

5. This proceeding concerns bilateral spot market transactions in the Pacific Northwest that occurred during the Western Energy Crisis of 2000 and 2001. As such, a brief history of the crisis and the events leading up to it are described below.[6]

6. In 1996, the State of California restructured its electric power markets in order to facilitate competition for the generation and sale of power. The California Legislature enacted Assembly Bill 1890 (AB 1890), which, among other things, created two new wholesale market institutions: the California Independent System Operator (CAISO) and the California Power Exchange (CalPX). The CAISO was the entity responsible for operating and maintaining California's electric transmission grid, including purchasing Ancillary Services and imbalance energy to maintain system reliability. CalPX functioned as California's principle power market, acting as a clearing house for daily and hourly electricity markets. As part of the restructuring, the California Investor Owned Utilities (IOUs)[7] were required sell its generation into and purchase its wholesale electric power from the CAISO and CalPX markets.

7. Specifically, the CalPX operated both day-ahead and hour-ahead single clearing price wholesale auction markets and the CAISO operated single clearing price market for real-time energy and Ancillary Services. When the auction markets were unable to provide sufficient electric power to meet the reliability of California's electric grid, the CAISO tariff permitted the CAISO to procure out-of-market (OOM) electric power. OOM power was solicited through a variety of methods, including phone calls to generators and marketers, and often at prices that exceeded the price caps applicable to the organized markets.

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[6] California Parties witness Taylor provides a more detailed description of the Western Energy Crisis in his Direct Testimony. Ex. CAT-041.

[7] The three California IOUs are Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SoCal Edison), and San Diego Gas and Electric Company (SDG&E).

8. Beginning in the first week of May 2000, real-time prices in Southern California spiked in certain hours to the then applicable price cap of $750/MWh.[8] In late May 2000, the price spikes began occurring in Northern California as well.[9] Due to the high prices, the CAISO lowered the price cap to $500/MWh. Although this alleviated the price spikes temporarily, by the third week in July, prices in both Northern and Southern California began spiking to the price cap again, leading the CAISO to further lower the price cap to $250/MWh on August 7, 2000. From this point through the beginning of October, prices regularly hit the cap in both Northern and Southern California.

9. On November 1, 2000, the Commission issued an Order Proposing Remedies for the California Wholesale Electric Markets.[10] The Commission found that "the electric market structure and market rules for wholesale sales of electric energy in California [were] seriously flawed and that these structures and rules, in conjunction with an imbalance of supply and demand in California, have caused, and continue[d] to have the potential to cause, unjust and unreasonable rates for short-term energy (Day-Ahead, Day-of, Ancillary Services and real-time energy sales) under certain conditions."[11]

10. The November 1, 2000 Order proposed a series of immediate remedies and long-term reforms to ensure just and reasonable rates for wholesale energy in California. With respect to the immediate remedies, the Commission proposed, among other things, (1) eliminating the requirement that California IOUs purchase from and sell into the

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[8] The part of the CAISO south of a major transmission link called Path 15 was designated SP-15 (south of Path 15), while the zone north of the link was designated NP-15 (North of Path 15). Because the transmission link between Northern and Southern California was often congested, NP-15 and SP-15 acted as distinct markets with distinct pricing.

[9] Because the transmission system allows suppliers to sell anywhere in the Western region, prices in the Pacific Northwest and other Western markets also experienced increases energy prices.

[10] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121 (2000), *order on clarification and reh'g*, 97 FERC ¶ 61,275 (2001), *order on further reh'g*, 99 FERC ¶ 61,160 (2002).

[11] *Id*. at 61,349. The Commission also stated that it was unable to reach definite conclusions about the actions of individual sellers, but that "there is clear evidence that the California market structure and rules provide the opportunity for sellers to exercise market power when supply is tight and can result in unjust and unreasonable rates under the FPA." *Id*. at 61,350.

CalPX; (2) modifying of the single price auction so that bids above $150/MWh did not set the market clearing price that is paid to all bidders; and (3) imposing comprehensive reporting and monitoring requirements for sellers bidding above $150/MWh.[12] The November 1, 2000 Order provided interested parties the opportunity to comment on the proposed remedies.[13] On December 15, 2000, the Commission issued an order largely adopting the proposed remedies.[14] Following the Commission's remedial measures, prices fell briefly, but returned to high levels in late December 2000.

11. Furthermore, in December 2000, several credit ratings agencies lowered or put on watch the debt ratings of PG&E and SoCal Edison and their corporate parents. The IOUs were facing liquidity problems as a result of the high costs for wholesale power purchases and a freeze in retail rates.[15] As a result, the two IOUs began having difficulty finding sellers willing to risk sales to them. PG&E's and SoCal Edison's bonds reached "junk status" in January 2001, and on January 16, 2001, SoCal Edison announced that it would not be able to pay more than $500 million it owed creditors. Moreover, because the two California IOUs were primary purchasers from the CalPX, several suppliers withdrew from the California organized markets and the volumes purchased in the CalPX dropped sharply, requiring the CAISO to purchase large volumes of OOM energy.

12. On January 17, 2001, California Governor Gray Davis proclaimed a state of emergency because high energy prices "threatened the solvency of California's major public utilities, preventing them from continuing to acquire and provide electricity sufficient to meet California's energy needs."[16] Governor Davis ordered the California Department of Water Resources (CDWR) to enter into contracts for electric power to

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[12] *Id*. at 61,349-50.

[13] *Id*. at 61,373.

[14] With respect to the three immediate remedies described above, the Commission adopted these remedies without modification. *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,294 (2000).

[15] Because SDG&E was no longer subject to a rate freeze, SDG&E was able to recover high wholesale energy costs through its retail rates.

[16] Ex. CAT-013.

assist in mitigating the effects of the emergency.[17] This new responsibility was to be separate from CDWR's existing power purchasing functions.[18]

13. On January 19, 2001, SB7X was signed into law, establishing the Electric Power Fund for the purpose of making purchases "for sale directly or indirectly to the Independent System Operator, public utilities, or retail end-use customers."[19] SB7X transferred $400 million into the Electric Power Fund and authorized purchasing until February 2, 2001.[20] On February 1, 2001, AB1X was signed into law, which authorized power purchases until December 31, 2002.[21]

14. In order to accomplish this new function, CDWR created a new division, the California Energy Resources Scheduling Division (CERS). CERS would be responsible for purchasing a substantial amount energy that the IOUs previously acquired from the organized markets. When CERS came into existence, the entire "net-short" – the difference between demand and what the IOUs could supply from their own generation – had to be purchased in short-term spot markets because there were no long-term supply contracts in place.[22] Failure to procure the entire "net short" would result in blackouts. From January 17, 2001 through February 16, 2001, the CAISO declared Stage 3 Emergency Conditions every day, twenty-four hours a day.

15. Because of the limited resources in the CalPX and CAISO auction markets, CERS would purchase energy in bilateral markets on the boundaries of the CAISO system, such as the California-Oregon Border trading hub (COB or Malin) in the Pacific Northwest market. However, these bilateral markets outside the CAISO system were not subject to the Commission's price cap. Further complicating CERS's purchasing requirements was the fact that south-to-north transmission congestion on Path 15 often prevented generation in Southern California from serving load in Northern California. Thus, CERS

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[17] *Id.*

[18] *Id.* CDWR purchased electricity for operation of the Salt Water Project.

[19] Ex. CAT-014.

[20] *Id.*

[21] Ex. CAT-015.

[22] Additionally, SB7X did not authorize CERS to enter into long-term contracts. Ex. CAT-014. However, over time, CERS received authority and entered into long-term supply arrangements that reduced its reliance on the spot-market.

had to rely on purchases in the Pacific Northwest market in order to serve load in Northern California.

16. On June 19, 2001, the Commission issued an order implementing a price mitigation plan throughout the Western Electricity Coordinating Council (WECC).[23] The Commission's order established a maximum price for all spot market purchases throughout the WECC, including the bilateral transactions in the Pacific Northwest markets.[24] This "West-Wide Price Cap" effectively ended the crisis.

### B. Procedural History

17. The lengthy and complex procedural history of this decade old litigation has been discussed in detail in the Order on Remand[25] and is also set forth in the "Joint Procedural History" filed by the participants on August 12, 2013, which is adopted herein by the undersigned as follows.

18. This proceeding originated on October 26, 2000 when Puget Sound Energy, Inc. (Puget) filed a complaint petitioning the Commission for an order setting a prospective cap on the prices at which sellers may sell energy or capacity into the Pacific Northwest wholesale power markets.[26] The Commission initially dismissed Puget's complaint,[27] but upon further consideration, ordered a preliminary evidentiary hearing to develop a factual record on whether there may have been unjust and unreasonable charges for spot market bilateral sales in the Pacific Northwest between December 25, 2000 and June 20, 2001.[28]

19. A preliminary evidentiary hearing was conducted before the Honorable Judge Carmen Cintron in September 2001. On September 24, 2001, Judge Cintron recommended that the Commission not order refunds for any bilateral transactions at

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[23] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418 (2001).

[24] *Id.*

[25] Order on Remand at PP 5-15.

[26] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,294, at 61,988 (2000).

[27] *Id*. at 62,019.

[28] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,499-500 (2001).

issue in the Pacific Northwest[29] and determined that sales to CERS were outside the scope of the proceeding.[30]

20. On December 19, 2002, the Commission reopened the record to provide time for additional discovery and permitted refund claimants to submit directly to the Commission additional evidence of alleged market misconduct and proposed new and/or modified findings of fact.[31] In further orders, the Commission allowed parties an opportunity to respond to the newly submitted evidence and extended the deadline for submissions until March 20, 2003, creating the "100-days evidentiary proceeding."[32] On June 2, 2003, the Commission held an oral argument to address all aspects of the proceeding.[33]

21. In a June 25, 2003 order, the Commission determined that it had already provided the relief originally requested by Puget in its June 19, 2001 order that imposed prospective price caps throughout the Western United States.[34] The Commission did not to rule on the ALJ's conclusion that "the Pacific Northwest market for spot sales of electricity was competitive and functional during the relevant period of time."[35] Rather,

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[29] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at P 13, *reh'g denied*, 105 FERC ¶ 61,183 (2003) ("The ALJ recommended to the Commission that no refunds are warranted for wholesale power sales made in the Pacific Northwest between December 25, 2000 and June 20, 2001. In essence, she concluded that evidence demonstrates that the Pacific Northwest market for spot sales of electricity was competitive and functional during the relevant period of time, and prices were not unreasonable.") (internal citations omitted).

[30] *Puget Sound Energy, Inc.*, 96 FERC ¶ 63,044 (2001) (proposed finding of fact no. 30).

[31] *Puget Sound Energy, Inc.*, 101 FERC ¶ 61,304 (2002).

[32] *Puget Sound Energy, Inc.*, 102 FERC ¶ 61,163 (2003); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 102 FERC ¶ 61,194 (2003).

[33] *Puget Sound Energy, Inc*., Docket No. EL01-10-000 (May 21, 2003) (Notice Scheduling Oral Argument).

[34] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at PP 1, 29-30 (2003) (citing *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418 (2001)).

[35] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at P 13 (2003).

the Commission concluded that "even if prices were unjust and unreasonable, it is not possible to fashion a remedy that would be equitable to all the participants in the Pacific Northwest market."[36] In subsequent orders denying rehearing, the Commission agreed with Judge Cintron that sales to CERS were outside the scope of the proceeding.[37] Various parties petitioned for review by the United States Court of Appeals for the Ninth Circuit (Ninth Circuit).

22. In its August 24, 2007 opinion, the Ninth Circuit required the Commission to further consider two issues.[38] First, the Ninth Circuit found that the Commission had abused its discretion in denying relief for transactions involving energy purchased in the Pacific Northwest that was ultimately consumed in California. The Ninth Circuit stated that the Commission must, on remand, consider those purchases, including the purchases of energy made by CERS, in its determination of whether refunds are warranted for sales in the Pacific Northwest spot market.[39] Second, the Ninth Circuit directed the Commission, on remand, to examine in detail the new evidence of market manipulation submitted after the ALJ made factual findings and account for such evidence in any future orders regarding the award or denial of refunds in this proceeding.[40]

23. On October 3, 2011, the Commission issued an Order on Remand establishing an evidentiary hearing to address the issues the Ninth Circuit remanded and directing the Presiding Judge to reopen the record "to permit parties to present evidence of unlawful market activity during the relevant period" of December 25, 2000 to June 20, 2001.[41] Sellers accused of misconduct, in turn, were to be given the opportunity to "submit evidence that the activity in question was, in fact, legitimate business behavior."[42] The Commission also instructed that "contracts like those at issue here are a type of

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[36] *Id.* P 35.

[37] *Puget Sound Energy, Inc.*, 105 FERC ¶ 61,183, at P 42 n.43, *on further reh'g*, 106 FERC ¶ 61,109, at PP 10-13 (2004).

[38] *Port of Seattle v. FERC*, 499 F.3d 1016 (9th Cir. 2007).

[39] *Port of Seattle*, 499 F.3d at 1035.

[40] *Id.*

[41] Order on Remand at P 16.

[42] *Id*. P 22.

agreement to which the Supreme Court has found that the *Mobile-Sierra* presumption [of justness and reasonableness] generally applies, absent language therein to the contrary."[43]

24. The Commission directed the Presiding Judge to "establish which parties engaged in unlawful market activity without a legitimate business reason during the relevant period, and … [to] determine whether the identified unlawful market activity directly affected the negotiation of specific bilateral contracts, resulting in unjust and unreasonable rates."[44] The Commission also directed that the Presiding Judge determine, if necessary, a refund methodology.[45] In accordance with the Order on Remand, the hearing was initially held in abeyance to allow parties to attempt to settle.[46] On May 25, 2012, the Chief Judge ordered that hearing procedures begin, allowing for settlement discussions to continue along a parallel path.[47]

25. On September 13, 2012, the Presiding Judge issued an order bifurcating the proceeding into two phases.[48] In Phase I of the proceeding, the Presiding Judge would determine if (1) an individual seller engaged in unlawful market activity, without a legitimate business reason, that directly affected the particular contract or contracts to which that seller was a party such that the presumption of just and reasonable rates applicable to bilateral contracts under the *Mobile-Sierra* standard no longer applies and (2) for any contract at issue in this case to which the *Mobile-Sierra* standard applies, whether the requirements necessary for modification of a rate under the *Mobile-Sierra*

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[43] *Id*. P 20.

[44] *Id*. P 23.

[45] *Id*.

[46] *Id.* PP 30-31. A number of settlements were reached and have been approved by the Commission.

[47] *Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (May 25, 2012) (Order of Chief Judge Terminating Settlement Judge Procedures as to Some Parties; Continuing Settlement Judge Procedures as to Other Parties; Designating Presiding Administrative Law Judge; and Delaying Track II Procedures for 45 Days).

[48] *Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 13, 2012) (Order Confirming Rulings from the September 6, 2012 Prehearing Conference).

standard have been satisfied. In Phase II of the proceeding, the Presiding Judge would consider the appropriate refund methodology, if necessary.[49]

26. Following submission of Seattle's Direct Case, several Respondents filed Motions for Summary Disposition, requesting that the Presiding Judge dispose of all claims asserted by Seattle. The Presiding Judge denied each of these motions, stating that issues of material fact remain in dispute and summary disposition would be inappropriate based on the record as currently developed.

27. Additionally, in response to an Answer filed by the California Parties, the Presiding Judge rejected the California Parties' assertion that they are entitled to overcome the *Mobile-Sierra* presumption solely by demonstrating that the subject transactions imposed an excessive burden on consumers. The Presiding Judge stated that this assertion "fails to address the specific litigation history of the issues in dispute here as well as the express language of the Commission's mandate regarding the scope of these proceedings as set forth in the Order on Remand."[50] The California Parties subsequently filed a Motion for Interlocutory Appeal, which was granted on December 6, 2012. On December 21, 2012, the Commission issued an Order on Interlocutory Appeal clarifying that "refund claimants in this proceeding may overcome the *Mobile-Sierra* presumption by presenting evidence that a particular contract rate imposes an excessive burden on consumers or seriously harms the public interest."[51]

28. On April 5, 2013, the Commission issued an order granting in part and denying in part rehearing of the October 3, 2011 Order on Remand.[52] Specifically, the Commission denied rehearing of its determination that the *Mobile-Sierra* presumption of justness and reasonableness applies to the contracts in this case, reiterating that the "presumption applies to the contract rates at issue in this proceeding, unless buyers can overcome or

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[49] Additionally, the Presiding Judge would consider "Ripple Claims" in Phase II of the Proceeding. Ripple Claims are sequential claims against a succession of sellers in a chain of purchasers that are triggered if the last wholesale purchase in the chain is entitled to a refund. *Id.*

[50] *Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 8 (Dec. 6, 2012) (Order Denying in Part and Granting in Part California Parties Motion for Clarification or Interlocutory Appeal).

[51] *Puget Sound Energy, Inc.*, 141 FERC ¶ 61,248, at P 1 (2012) (Order Granting Interlocutory Appeal).

[52] *Puget Sound Energy, Inc.*, 143 FERC ¶ 61,020 (2013) (Order on Rehearing).

avoid the presumption."[53] The Commission also stated that the hearing "is [to be] narrowly tailored to address the Ninth Circuit's directives to include the sales to CERS and account for the new evidence of market manipulation."[54] Thus, "[i]n attempting to overcome the Mobile-Sierra presumption, any relevant evidence may be considered, including evidence that specific contract rates imposed an excessive burden on consumers."[55]

29. The Commission also granted rehearing to permit parties to submit evidence on transactions entered into during the period from January 1, 2000 to December 24, 2000. After establishing a refund effective date for Puget's complaint of December 25, 2000,[56] the Commission determined that it may order refunds for earlier transactions under its FPA section 309 authority insofar as any "refund claimants … demonstrat[e] a seller's specific violation of a substantive provision of the FPA or a tariff, compliance with which the Commission can enforce by taking actions 'necessary [or] appropriate.'"[57]

## III. Summary of the Testimony

30. For claims related to the section 206 of the FPA, claimants, the California Parties and the City of Seattle, Washington, submitted their direct testimony on September 21, 2012. On December 17, 2012, Respondents filed answering testimony. Commission Trial Staff filed answering testimony on February 5, 2013, and the claimants filed rebuttal testimony on March 12, 2013. PPL and Constellation were granted leave to file surrebuttal testimony to the City of Seattle's rebuttal testimony.

31. For claims pursuant to section 309 of the FPA, the City of Seattle filed direct testimony on June 3, 2013. Respondents[58] filed answering testimony on June 24, 2013.

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[53] *Id.* P 13.

[54] *Id.* P 25.

[55] *Id.* P 27 (quoting Order Granting Interlocutory Appeal at P 15).

[56] *Id.* P 32.

[57] *Id.* (quoting *Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027 (9th Cir. 2006)).

[58] Respondents for the Section 309 portion of this proceeding are: Avista Corporation d/b/a Avista Utilities and Avista Energy, Inc.; Cargill Power Markets, Inc.; El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.); Exelon Generation Company, LLC (Successor-In-Interest to

(continued…)

Trial Staff submitted answering testimony on July 11, 2013 and the City of Seattle filed rebuttal testimony on July 26, 2013. On August 27, 2013, the Joint Defense Group[59] was granted leave to file surrebuttal testimony to the City of Seattle's rebuttal testimony.

### A. The California Parties Direct Testimony for the Section 206 Claims

32. The California Parties currently assert claims against the following Respondents: Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral) and TransCanada Energy Ltd. The California Parties' claims concern transactions entered into by CERS between January 17, 2001 and June 20, 2001 (CERS Period). In support of their claims, the California Parties presented the testimony and exhibits of ten witnesses in their direct case.

#### 1. Commissioner Michael Peter Florio[60]

33. Commissioner Florio has been a Commissioner of the California Public Utilities Commission (CPUC) since January 25, 2011. Commissioner Florio was an attorney for The Utility Reform Network from 1978 until his appointment to the CPUC. Commissioner Florio submitted testimony and exhibits arguing that the spot market contracts entered into by CERS during the CERS Period place an excessive burden on consumers and impaired the State of California's finances.[61]

34. Commissioner Florio states that CERS was required to make spot market purchases of electricity at prices demanded by Respondents that were significantly higher than the prices paid by the IOUs one year before the crisis. Commissioner Florio notes

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Constellation Energy Commodities Group, Inc.); PPL Montana, LLC and PPL EnergyPlus, LLC; Public Service Company of Colorado; TransAlta Energy Marketing (U.S.) Inc.; and TransAlta Energy Marketing (California) Inc.

[59] The Joint Defense Group includes Avista Corporation d/b/a Avista Utilities and Avista Energy, Inc.; El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.); Exelon Generation Company, LLC (Successor-In-Interest to Constellation Energy Commodities Group, Inc.); PPL Montana, LLC and PPL EnergyPlus, LLC; Public Service Company of Colorado; TransAlta Energy Marketing (U.S.) Inc.; and TransAlta Energy Marketing (California) Inc.

[60] Ex. CAT-001.

[61] *See* Ex. CAT-001 through CAT-011.

that although a government agency was purchasing electricity, the California Legislature made clear that the IOUs customers would ultimately bear the cost burden.

35. Commissioner Florio asserts that in order to cushion the price shock and avert economic disaster, the high costs for spot market energy were spread out over twenty years through the issuance of revenue bonds. Commissioner Florio notes that economic disaster was only narrowly averted in San Diego in 2000 when the crisis began[62] and a much worse statewide economic crisis would have occurred had the IOUs been permitted to passed through the billions of dollars in CERS's overall spot market purchase costs.

36. Commissioner Florio provides anecdotal evidence of the hardship on SDG&E consumers in 2000 as a result of the immediate pass-through of wholesale costs into retail rates. Commissioner Florio notes that some consumers faced energy bills that had doubled or tripled and in some cases been higher than mortgage payments. Commissioner Florio states that he initially was opposed to deferring the costs to the future, but changed his mind after hearing first hand from San Diegans. Commissioner Florio describes specific examples of people who were fearful of losing their homes, of bankruptcy, of layoffs and business closures, and of going without medical care or food.[63]

37. Next, Commission Florio compares the electricity prices in 2000 to those in 2001 and estimates that a similar rate impact would have occurred in 2001 if the costs were immediately passed through to consumers. Specifically, Commissioner Florio notes that the average monthly electricity costs in January 2000 were $32/MWh while the average costs in January 2001 were $185/MWh. Therefore, the state correctly spread the costs of wholesale purchases over twenty years.

### 2. Mr. Raymond Hart[64]

38. Mr. Hart was the Deputy Director of CERS from January 17, 2001 through August 2001. Mr. Hart's testimony and exhibits describe the circumstances under which CERS purchased energy during the CERS Period.

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[62] Because SDG&E was no longer subject to a retail rate freeze, SDG&E passed through its dramatically increased wholesale purchase power costs to its customers in their monthly bills.

[63] Commissioner Florio notes that in August 2000, the CPUC partially capped the SDG&E rates, but believes that these rate caps were largely ineffective.

[64] Ex. CAT-012.

39. Mr. Hart first provides general background information concerning the formation of CERS. Mr. Hart notes that prior to the creation of CERS, CDWR maintained a small staff familiar with electrical utility operations, but was not prepared for the demands placed upon it. Mr. Hart states that any prior experience the CERS personnel had was not sufficient because from the start, CERS was required to purchase several thousand megawatts of electricity in a given hour, becoming one of the largest purchasers of electricity overnight.

40. Mr. Hart describes CERS's primary mission as acquiring enough energy to avoid blackouts. Mr. Hart notes that Governor Davis's January 17, 2001 proclamation specifically mentions blackouts and that blackouts present immediate public safety concerns and can cause significant economic loss. However, Mr. Hart states that blackouts occurred during three of the first five days of CERS operations, and that in many instances, CERS traders had no choice but to purchase high cost energy. Mr. Hart notes that on the sixth day of operations, CERS's purchases totaled approximately 6,000 MWh and $40 million.

41. Next, Mr. Hart describes the funding of CERS. Mr. Hart states that CERS was initially transferred $400 million dollars for purchases until February 2, 2001, but was later given additional funding. Mr. Hart states that CERS spent more than $1 billion per month on spot market purchases. As a result of the declining credit of the IOUs, Mr. Hart avers that CERS was required to purchase more energy than initially planned and accomplish the more complex task of maintaining a portfolio of long and short-term contracts.

42. Mr. Hart states that CERS lacked several elements that a power buyer would have had in a functioning competitive market: (1) CERS lacked personnel and infrastructure; (2) CERS had little choice in the hour-ahead and real-time markets; and (3) CERS lacked time to negotiate and analyze the market. Mr. Hart asserts that sellers knew of CERS's position and took advantage of it by holding out until the last minute to get the highest price. Mr. Hart further argues that this was particularly problematic because CERS could not simply not buy the electricity. Mr. Hart states that the difficulties were compounded because some market participants refused to sell to CERS at all because of perceived credit risks. Mr. Hart argues that sellers should not have had credit concerns because CERS was receiving funding from California's General Fund. Additionally, Mr. Hart notes that when sellers cut off sales to CERS without notice, the remaining sellers had increased leverage in their dealings with CERS. Mr. Hart contends that these circumstances provided sellers to CERS with a bargaining advantage in their dealings.

43. Next, Mr. Hart describes CERS's revenue recovery mechanism. Mr. Hart states that CERS received deposits from the California General Fund and this money was supplemented by a portion of the utility bill payments received by the IOUs. Additionally, Mr. Hart notes that CERS received a bridge loan in late June 2001. Mr. Hart states that through the use of revenue bonds, CERS would pay back both the

money used from the General Fund and the money acquired through the bridge loan. Mr. Hart notes that this allowed the costs to be recovered over twenty years, rather than immediately passed through to consumers.

44. Lastly, Mr. Hart states that the requirement in AB1X that CERS certify that costs be "just and reasonable" was not an admission of "just and reasonable" prices under the Federal Power Act. Mr. Hart avers that CERS's determination was only that the costs were "reasonable" under the specific circumstances at the time, including CERS's goal to avoid blackouts.

### 3. Ms. Susan Lee[65]

45. Ms. Lee began working as a consultant for CERS in January 2001. From April 16, 2001 through December 31, 2001, Ms. Lee was Manager of Trading and Scheduling at CERS. Ms. Lee's testimony describes CERS's spot market trading during the CERS Period.

46. Ms. Lee begins her testimony by describing the circumstances under which CERS was created.[66] Ms. Lee notes that CERS's mission was to meet the "net short" for California's three large IOUs because the IOUs were on the brink of insolvency and unable to acquire energy.

47. Ms. Lee states that CERS faced disadvantages that other market participants did not face because CERS did not have a portfolio of contracts to ensure supply stability. Therefore, CERS was forced to purchase the entire net short on the spot market while also trying to build a portfolio of long-term contracts. Ms. Lee also states that many sellers refused to sell to CERS and therefore, CERS was forced to buy energy from a small number of sellers. Ms. Lee notes that sellers were aware of CERS's position in the market and knew CERS had to purchase energy in the spot market to ensure no blackouts occurred. Therefore, Ms. Lee argues that CERS was at a huge disadvantage in negotiating with sellers.

48. Ms. Lee states that CERS tried to purchase the net short first in the day-ahead market, then in the hour-ahead market, and as a last resort, in the real-time market. Ms. Lee states that CERS tried to avoid the hour-ahead and real-time markets because the prices were generally higher. Additionally, Ms. Lee notes that CERS tried to make monthly purchases when it could.

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[65] Ex. CAT-022.

[66] *See supra* Section III.A.2.

49. For day-ahead purchases, CERS developed a list of sellers that typically had energy and would call those sellers each day. Ms. Lee states that these sellers often only had small quantities of energy available and therefore, CERS would have to make a large quantity of transactions at high prices. Ms. Lee states that if the prices were significantly higher than expected, CERS would contract with a different seller and only go to the highest-priced seller when all other options were exhausted. For those sellers who had large quantities to sell, Ms. Lee states that CERS typically made the purchase knowing it would not be able to procure large blocks of power from other suppliers.

50. For real-time purchases, Ms. Lee states that traders had a five to forty-five minute window to complete transactions. The trader would then use information from the previous shifts regarding who had power available and at what price to contact sellers. CERS would attempt to contract for the lowest price, but may eventually have to purchase from high-cost providers depending on the amount of energy needed. Because many sellers refused to sell to CERS because of a perceived credit risk,[67] only a few sellers, including Coral were available. Thus, Ms. Lee states that CERS had little opportunity to bargain because the market participants knew the position CERS was in and that CERS's bargaining strength decreased as the time frames got shorter.

51. Next, Ms. Lee describes the blackouts that occurred during the CERS Period. Ms. Lee states that despite CERS's best efforts, rolling blackouts occurred on three days in mid-January and two days in early May. Ms. Lee further notes that the ISO declared a Stage III emergency every day during the first month of operations.

52. Ms. Lee also notes that ISO grid congestion, particularly south to north, added to CERS's problems. Ms. Lee states that this congestion made it more likely that CERS would have to make purchases in the Pacific Northwest, primarily at COB. Ms. Lee notes that CERS's purchases in the Pacific Northwest needed to come from counterparties with transmission rights to get the energy to COB because CERS was unable to purchase its own transmission rights to COB because the capacity was already committed.

53. As exhibits to her testimony, Ms. Lee includes CERS's transaction records with Respondents from the time. Ms. Lee notes that the "recorded date" on these transactions records were often far later than the actual transaction date because CERS did not have a record keeping protocol when it first started operating. However, Ms. Lee contends that the data are accurate and were verified based on billing information.

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[67] Ms. Lee states that there was no credit risk because CERS was receiving money from the State's General Fund.

### 4. Mr. John Pacheco[68]

54. Mr. Pacheco is currently the Acting Deputy Director of CERS. During 2001, Mr. Pacheco's primary responsibility at CERS was to negotiate with the California IOUs to collect revenue that the IOUs received through their retail rates. Mr. Pacheco's testimony addresses (1) how California paid for CERS's spot market purchases; (2) how the state recovered the amount spent on CERS's purchases; and (3) how any refunds ordered in this proceeding will "flow" to ratepayers.

55. Mr. Pacheco begins his testimony by stating that seventy-six percent (based on cost) of CERS's purchases during the CERS Period occurred in the spot market with forty percent of those purchases in the Pacific Northwest. Mr. Pacheco notes that because CERS had no portfolio of contracts when it began operating, CERS was required to make purchases in the spot market to meet the net short. Mr. Pacheco states that as of June 20, 2001, CERS spent $6.95 billion on electricity purchases, of which, $2.67 billion was spent on spot market purchases in the Pacific Northwest.

56. Mr. Pacheco states that spot market purchases were funded primarily through transfers from California's General Fund into the Electric Power Fund (EPF).[69] Mr. Pacheco states that on January 19, 2001, the initial $400 million deposit into the EPF occurred. On February 1, 2001, Assembly Bill 1X (AB 1X) was enacted and allowed for further transfers from the General Fund into the EPF. Mr. Pacheco states that on February 1, 2001, approximately $496 million more dollars were transferred to the EPF. Mr. Pacheco asserts that from February 2001 to June 2001, $500 million transfers occurred approximately every two weeks. In total $6.1 billion were transferred from the General Fund to the EPF. Mr. Pacheco states that the last transfer of General Funds to the EPF occurred in early June 2001. CERS was then funded through a $4.3 billion interim loan from a variety of lenders and the IOU transfers.

57. Mr. Pacheco states that although the IOUs were supposed to reimburse the EPF with revenues received from the electricity that was purchased, only a small fraction of money in the EPF came from the California IOUs. Mr. Pacheco avers that this is because the IOUs operated with retail rate caps, which prevented the IOUs from fully recovering the costs.

58. Next, Mr. Pacheco describes how California recovered the General Fund transfers to the EPF. Mr. Pacheco states that AB 1X established the framework for recovering

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[68] Ex. CAT-037.

[69] The IOUs also made some transfers into the Electric Power Fund.

costs associated with CERS's purchases and provided that the CPUC would determine the portion of each IOUs retail rate to allocate to CERS. Additionally, CDWR could issue revenue bonds to spread out the recovery costs over a longer period of time. With respect to these revenue bonds, Mr. Pacheco states that AB 1X provided that CDWR and CPUC would enter into an agreement to ensure that retail customers would be pledged to repay the funds so that the CDWR bonds could be sold at investment grade ratings.

59. Mr. Pacheco states that based on the AB 1X framework, CDWR issued bonds in 2002 to pay back the $6.1 billion in General Fund transfers and $4.3 billion interim loan. The bonds will be paid back over twenty years through a "Bond Charge" collected on the IOUs end user electric bills. For CERS's long-term purchases, Mr. Pacheco states that the CPUC instituted a separate "Power Charge."[70] Mr. Pacheco states that California chose to spread the costs out over a twenty year period because of the experience in San Diego in the Summer of 2000 when the high costs were immediately passed on to customers.[71] Lastly, Mr. Pacheco asserts that if refunds are ordered in this proceeding, those refunds will be deposited into the EPF, resulting in a decrease in the Power and Bond Charges.

### 5. Mr. Gerald Taylor[72]

60. Mr. Taylor is an expert witness for the California Parties. Mr. Taylor provides testimony regarding (1) CERS's role as a "buyer of last resort" for the California IOUs and (2) whether the *Mobile-Sierra* presumption should apply to contracts CERS entered into with the Respondents for spot market purchases in the Pacific Northwest.

61. Mr. Taylor begins his testimony by describing the events leading up to the Western Energy Crisis. Although the majority of this portion of Mr. Taylor's testimony provides only factual background information, Mr. Taylor does allege that sellers exploited the price constraints in the CalPX for profit. Specifically, Mr. Taylor contends that some sellers withdrew from the CalPX, resulting in Stage 3 Emergencies and blackouts in December 2000. Additionally, Mr. Taylor argues that marketers took advantage of the price caps in the organized markets to buy energy out of the California markets at the price cap and reimport that energy to California through bilateral sales at higher prices. Mr. Taylor claims that this activity violated the CAISO tariff, the seller's

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[70] In support of the Bond Charge and Power Charge, CDWR submits annual revenue requirements to the CPUC to revise the charges.

[71] *See* Ex. CAT-001.

[72] Ex. CAT-041.

market-based rate authorization, and hastened the financial collapse of the California IOUs.

62. Next, Mr. Taylor discusses the circumstances CERS faced when first created. Mr. Taylor notes that CERS, which was required to purchase the IOUs' net short, began operations in the midst of two days of rolling blackouts. Moreover, from January 17, 2001 through February 16, 2001, the CAISO declared Stage 3 Emergencies every day, twenty-four hours a day. Additionally, Mr. Taylor notes that because there were no long-term contracts, CERS was required to procure the entire net-short in the spot market, and often largely in the real-time market. Therefore, CERS was "racing the clock" each hour to procure enough energy to avoid blackouts. Mr. Taylor asserts that this problem was further exacerbated by the fact that CERS was dealing with credit limitations with sellers, particularly those sellers able to provide large blocks of energy.

63. Next, Mr. Taylor describes CERS's bilateral purchases to meet the net short. Mr. Taylor states that because the organized California markets were limited, CERS purchased energy in the bilateral markets on the boundaries of the CAISO system, particularly COB in the Pacific Northwest and Palo Verde in the Southwest. Mr. Taylor states that Northern and Southern California are interconnected through a transmission system called Path 15. However, because Path 15 was often constrained in the South to North direction – forty-five percent of the days during the CERS Period had congestion – the Northern California market and Southern California market were essentially separated, requiring CERS to purchase energy for Northern California in the Pacific Northwest.[73]

64. Mr. Taylor states that because of the Path 15 transmission constraint, prices in the Pacific Northwest were consistently higher than prices in Southern California.[74] Additionally, Mr. Taylor notes that from January 2001 through April 2001, a majority of all CERS purchases, approximately seventy percent, were acquired to serve load in Northern California.

65. Mr. Taylor states that on a volume basis, approximately two third of CERS's total purchases were acquired in the bilateral spot markets in day-ahead, hour-ahead, real-time,

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[73] In addition to not being able to access the Southwest markets to meet Northern California demand, much of California's generation was located in Southern California and was similarly unavailable to meet Northern California demand.

[74] The average price differential during the CERS Period was $137/MWh.

or balance-of-month transactions.[75] Mr. Taylor states that these purchases totaled $5.7 billion.

66. Next, Mr. Taylor argues that the *Mobile-Sierra* presumption should not apply to Respondents contracts with CERS because negotiation of the contracts, and the resulting prices, were adversely affected by duress, fraud, bad faith, and market manipulation. Mr. Taylor states that in making this determination, he considered two types of evidence: (1) evidence of duress, fraud, or bad faith affecting the formation of the contract and (2) evidence of manipulative activity.

67. With respect to evidence of duress, fraud, and bad faith, Mr. Taylor states that the testimonies of Mr. Hart and Ms. Lee demonstrate that CERS entered into negotiations in a weak bargaining position and was exploited by some Respondents. Mr. Taylor states that CERS's weak bargaining position was the result of CERS needing to procure large amounts of energy to avoid blackouts, leaving CERS in the position of either paying what the seller demanded or "letting the lights go out." Mr. Taylor states that CERS's priority regarding the reliability of the CAISO power grid is demonstrated by documents that show that CERS traders were authorized to purchase energy at any price when CAISO was in emergency conditions. Mr. Taylor states that the problems were exacerbated by the fact that many suppliers refused to sell to CERS due to perceived credit risks and supply became more concentrated among a few sellers, which limited the supply available to CERS.

68. Mr. Taylor states that Respondents took advantage of this situation to extract high prices from CERS. With respect to Coral, Mr. Taylor states that internal emails among Coral traders demonstrate that Coral used an increase in their credit limit to CERS to extract higher margins. Additionally, Coral would use the emergency conditions in the ISO to extract high prices. Mr. Taylor also describes how Coral would "launder" energy. Mr. Taylor states that this involved Coral parking energy that originated in California with a third-party outside California and then reselling that energy back to CERS. Mr. Taylor alleges that Coral learned this tactic from Enron traders that came to work for Coral and that this activity was furthered through a marketing arrangement between Coral and the City of Glendale, California (Glendale).

69. Additionally, Mr. Taylor claims that Coral aggregated supply and marked its purchases up by very large amounts for resale to CERS. Mr. Taylor cites to Coral emails that state that Coral was receiving margins of $200/MWh or higher during CAISO Stage 3 Emergencies for sales of energy that were originally bought from a third party.

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[75] Eighty-two percent of these transactions were either real-time or day-ahead transactions.

Mr. Taylor states that this is confirmed by Dr. Fox-Penner's analysis, which demonstrates that for real-time transactions, Coral charged CERS $211/MWh more than other buyers (on average).

70. Mr. Taylor also alleges that Coral waited until real-time to sell to CERS. Mr. Taylor states that by waiting until real-time, Coral was able to extract high prices because if CERS did not make purchases immediately, California would experience blackouts. Thus, CERS traders were unable to negotiate prices under these conditions. Mr. Taylor asserts that waiting until real-time was profitable for Coral because Coral was still able to pay "parking fees" to third parties in order to shift energy from day-ahead to real-time.

71. Mr. Taylor also alleges that TransCanada engaged in similar activity as Coral, but to a lesser extent. Mr. Taylor cites to TransCanada's "deal tickets" which show TransCanada achieved margins of over $100/MWh by parking day-ahead energy and selling it to CERS in real-time.

72. Next, Mr. Taylor states that there is evidence that the Respondents engaged in manipulative activities that contributed to the market dysfunction and affected the prices of the contracts with CERS. Specifically, Mr. Taylor claims that Respondents engaged in False Export transactions and withholding of supplies.[76]

73. Mr. Taylor defines False Export as (1) a supplier filing a day-ahead or hour-ahead export schedule with the ISO; (2) "parking" the energy outside California (finding a sink); and (3) selling the energy as an import in the real-time market at an elevated price.[77] Mr. Taylor states that these transactions create the illusion that power generated or purchased within the ISO was actually generated from a source outside the ISO.[78] Mr. Taylor notes that the energy would not actually "flow" in and out of California because the import and export schedules would cancel each other out. Mr. Taylor further

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[76] Mr. Taylor states that other California witnesses have provided evidence of price discrimination. Because those witnesses provide extensive analyses, a discussion of these activities is found *infra*. However, Mr. Taylor did note that internal emails corroborated Dr. Fox-Penner's findings regarding price discrimination.

[77] The "sink" would return the energy to the original buyer, who would then sell the energy to CERS.

[78] Mr. Taylor compares this strategy to others gaming strategies – Ricochet and False Imports – that the Commission has previously admonished.

notes that these False Export transactions were often more complex and involved multiple parties and transactions.[79]

74. Mr. Taylor contends that the False Export strategy had the same effect as withholding power from the day-ahead market and increased sellers' bargaining power in real-time. Additionally, Mr. Taylor claims that the False Export strategy impacted reliability because CERS was desperately trying to acquire enough energy to avoid blackouts and any shortage in the day-ahead market increased the amount CERS had to purchase in real-time.

75. Mr. Taylor contends that False Exports violated the Market Monitoring and Information Protocol (MMIP) of the CAISO tariff, the scheduling and bidding requirements of the CAISO tariff, and the seller's tariff. Mr. Taylor argues that the MMIP was intended to prevent the exercise of market power and to provide protection against abuses that may undermined the effective functioning of the CAISO markets. Therefore, MMIP targeted "anomalous market behavior," including withholding capacity and unusual behavior relating to the imports or exports of power. With respect to the scheduling provisions, Mr. Taylor states that implicit in the requirement to file a schedule is that the schedule not be false or misleading. Therefore, purposeful inaccurate schedules violate the tariff. Lastly, since the sales to CERS were based upon fraudulent representations that the energy was sourced outside the CAISO, the sales also violated the seller's tariff.

76. Next, Mr. Taylor discusses his analysis of transaction and CAISO data that identified instances where a Respondent engaged in False Exports.[80] Based on this screening analysis, Mr. Taylor asserts that Coral engaged in False Exports in 256 hours for a total of 5,455 MWh. Mr. Taylor states that parties that engaged in South to North False Exports did this to take advantage of the price differential between day-ahead energy in Southern California and real-time energy in the Pacific Northwest.

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[79] Mr. Taylor cites a Coral email, which describes the use of Glendale, Portland General Electric, and Coral to facilitate a False Export.

[80] Mr. Taylor states that he examined the day-ahead and hour-ahead export schedules for each market participant and then compared those schedules to the real-time sales to CERS, accounting for scheduled wheeling through the ISO and interzonal transactions during congestion periods. The amount of False Export was the lesser of the real-time sales to CERS and the Respondent's day-ahead or hour-ahead export from the ISO.

77. Mr. Taylor also states that the manipulative activity affecting prices in California also affected prices in the Pacific Northwest. Mr. Taylor cites a Commission Staff Report that discusses the relationship between the sellers' activities in California and the Pacific Northwest prices. Mr. Taylor also argues that the evidence of prices in California and the Pacific Northwest moving in lock-step, despite CAISO price caps, further support the linkage between the markets.

78. Next, Mr. Taylor discusses his hourly database which demonstrates which contracts[81] were the result of negotiations affected by fraud, duress, bad faith, or manipulative activity.[82] Mr. Taylor determined if the evidence supports a finding that the *Mobile-Sierra* presumption should not apply to the contract. For each Respondent, Mr. Taylor found that a large percentage of the contracts with CERS were affected by fraud, duress, bad faith, or manipulative activity.[83]

79. Lastly, Mr. Taylor contends that the contract prices should be revised because the prices are against the public interest. First, Mr. Taylor notes that the contracts at issue in this case do not have the same types of benefits that the Supreme Court considered in *Morgan Stanley*.[84] Mr. Taylor states that long-term agreements provide protection from spot price volatility and future price certainty promotes needed investment. Because these are spot contracts, those benefits are not present here. Mr. Taylor also states that because of the unique circumstances (wrongdoing of the participants) of this period, providing relief would not pose a threat to the contract sanctity in the power industry and that the markets have evolved to prevent the same problems from happening in the future.

80. Second, Mr. Taylor argues that there are public interest considerations that support providing relief. Mr. Taylor states that the contracts and rates paid in these transactions are the result of wrongdoing and prices that were unduly discriminatory. Mr. Taylor

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[81] Mr. Taylor considers the "contracts" for this proceeding to be evidenced by the confirmations (as required by the WSPP) for the sale of power in real-time, day-ahead, hour-ahead, and balance of month.

[82] In addition to the evidence and analyses discussed above, Mr. Taylor used a price screen to determine if there was evidence of fraud, duress, or bad faith.

[83] Because Mr. Taylor revised his database to respond to criticisms in the Respondents' Answering Testimony, a final summary of Mr. Taylor's conclusions can be found in the summary of Mr. Taylor's rebuttal testimony.

[84] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008).

states that the Commission has provided relief for similar contracts in the past. Lastly, Mr. Taylor notes the hardship on the customers who have to pay high rates.

### 6. Dr. Peter Fox-Penner[85]

81. Dr. Fox-Penner is an expert witness for the California Parties. Dr. Fox-Penner provides testimony regarding (1) price discrimination and (2) the cost of blackouts.

82. Dr. Fox-Penner analyzes whether price discrimination occurred by comparing the price of purchases by CERS with the price of purchases by other non-CERS buyers in the Pacific Northwest. Based on this comparison, Dr. Fox-Penner calculates a CERS Premium to quantify the degree of price discrimination. Dr. Fox-Penner states that his analysis accounts for differences between the CERS and non-CERS transactions.[86] Based on his analysis, Dr. Fox-Penner calculated an average CERS Premium for the entire CERS Period of $211/MWh for Coral and $54/MWh for TransCanada.

83. Dr. Fox-Penner states that although his analysis does not indicate that CERS paid a premium in every transaction, there is a large premium, on average, over the course of the CERS Period. Dr. Fox-Penner asserts that this indicates that sellers charged CERS higher prices than other buyers in the market.

84. Next, Dr. Fox-Penner states that other factors may have contributed to the cost differential between CERS and other buyers. For example, CERS purchased more energy than any other buyer and if the marginal cost of acquiring this energy was significantly higher, it could explain some of the difference. Another factor could be a different credit risk between CERS and other buyers. However, as discussed more fully below, Dr. Fox-Penner concludes that these factors do not explain or justify the large differentials.

85. With respect to volume differences, Dr. Fox-Penner first notes that most Respondents sold similar quantities to CERS and non-CERS buyers. Additionally, Dr. Fox-Penner conducted a regression analysis of each Respondent's day-ahead and day-of purchases and found that the statistical relationship between volume and price was not broad or deep enough to justify the premiums charged to CERS.

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[85] Ex. CAT-161.

[86] These differences include: (1) the duration of the transaction; (2) if the transaction was day-ahead or day-of; (3) delivery location; (4) if the transaction was firm or non-firm; (5) differences in volume; and (6) creditworthiness of the buyers.

86. Dr. Fox-Penner also argues that any justifiable credit risk premium was negligible. First, Dr. Fox-Penner notes that most sales to CERS were under the terms of the WSPP Agreement.[87] Second, Dr. Fox-Penner states that sellers managed their credit risk by imposing credit limits on CERS. In order to quantify a "justifiable" credit premium, Dr. Fox-Penner calculates a credit premium assuming a CERS default rate based on BB-rated non-investment grade corporate bonds (junk bonds). Using this calculation, Dr. Fox-Penner calculates a credit premium 1.06 percent.

87. Moreover, Dr. Fox-Penner does not believe that CERS's lack of a bond rating justified heightened concerns of non-payment because CERS was "backed" by the California General Fund. With respect to the sellers who refused to sell to CERS because of a perceived credit risk, Dr. Fox-Penner dismisses these decisions because the perceptions were not accurate and does not prove that the high premiums were justified.

88. Next, Dr. Fox-Penner describes his analysis for determining if the discrimination is "undue" on a broad, multi-transaction basis.[88] Generally, Dr. Fox-Penner states that for an undue price discrimination finding, the differences in price cannot be attributable to the difference in supplying different buyers.[89] Additionally, Dr. Fox-Penner considers a variety of economic efficiency factors, such as whether the price is less than the short-run marginal cost of the supplier. Broadly, Dr. Fox-Penner finds that the prices charged to CERS involved economically undue price discrimination.

89. Next, Dr. Fox-Penner addresses the cyclical nature of energy prices. Dr. Fox-Penner states that when supply is tight, short-run prices increase, leading to more capacity being added. Typically, too much capacity will be added and the short-run

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[87] Under the WSPP Agreement, the longest period that seller would have to assume credit risk was approximately thirty-five days.

[88] Dr. Fox-Penner acknowledges that there is no "simple cut-and-dry" definition of undue levels of price discrimination. Additionally, Dr. Fox-Penner states that his analysis concerns economically undue discrimination, as opposed whether or not the price differentials were "fair." Dr. Fox-Penner states that a fairness determination must be made by the regulatory body.

[89] Dr. Fox-Penner states that there was not a difference in buyer characteristics (based on his credit risk analysis) or products sold to justify the price differences. Dr. Fox-Penner acknowledges that CERS had a larger need for power with limited options, but states that economic efficiency does not justify charging CERS higher prices given this dynamic, particularly in light of the low fixed costs of Respondents and the fact that prices exceeded both short-run and long-run marginal costs.

prices will drop below the marginal costs; supply will then tighten again and restart the cycle. Dr. Fox-Penner asserts that over an entire cycle, the seller will earn their costs plus a competitive level of profits. However, Dr. Fox-Penner argues that prices charged to CERS in the Pacific Northwest market during the CERS Period far exceeded the price levels necessary to add capacity. Therefore, Dr. Fox-Penner concludes that the prices charged to CERS were far above the normal competitive price level and were not justified by economic efficiency.[90]

90. Dr. Fox-Penner also analyzed the short-run costs for each of the Respondents using the trading data and compared these costs to the prices sold to CERS. The analysis also adjusted for any long-run costs, energy storage costs, and generation costs, if applicable. For each Respondent, the analysis showed that the profit margins were small for non-CERS sales and much higher for sales to CERS. Dr. Fox-Penner concludes that this is evidence of price discrimination.

91. Next, Dr. Fox-Penner evaluated whether undue discrimination occurred in specific transactions. Dr. Fox-Penner considered the following five factors: (1) the CERS Premium when compared to non-CERS buyers of identical products;[91] (2) a visible pattern in prices charged to CERS and non-CERS buyers; (3) average price charged to non-CERS buyers at a given time and location; (4) the dispersion of prices in the market at a given time and location (standard deviation); and (5) if the prices charged to CERS were statistically different. For discrimination to be considered "undue," Dr. Fox-Penner sets two baselines: (1) for non-CERS average prices above $125/MWh, the CERS premium must be greater than $50/MWh and (2) for prices below $125/MWh, the CERS premium must be greater than forty percent.

92. To measure price dispersion, Dr. Fox-Penner uses the Commission's data set from Docket No. PA02-2.[92] Because the PA02-2 Data do not show the hour of delivery,

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[90] Dr. Fox-Penner further supports his conclusion by stating that a hypothetical generator operating during this time in the Pacific Northwest spot markets would have received profits far exceeding the normal competitive earnings (4.2 times its yearly profits during the 155 day CERS Period).

[91] In determining matching transactions for a CERS Premium, Dr. Fox-Penner uses the transaction's actual premium if there was a matching transaction on the same day. If there were no non-CERS matching transaction, Dr. Fox-Penner uses the other factors to reach conclusions regarding undue discrimination.

[92] Dr. Fox-Penner describes this data as the most complete set of spot market sales, but recognizes that the data do not indicate the hours of delivery within a day.

Dr. Fox-Penner uses the average daily price. Using this data, Dr. Fox-Penner calculates an average price to non-CERS buyers and standard deviation for each day. Dr. Fox-Penner uses this analysis to determine if the CERS prices are within a particular number of standard deviations and makes a judgment based on this determination.

93. In total, Dr. Fox-Penner concluded that Coral engaged in undue discrimination in 595 sales to CERS and TransCanada engaged undue discrimination in 26 sales to CERS.

94. Lastly, Dr. Fox-Penner discusses the costs of blackouts. Dr. Fox-Penner notes that there were seven blackouts during the CERS period, totaling more than 22 hours. Dr. Fox-Penner asserts that blackouts cause both direct and indirect costs.[93] Dr. Fox-Penner estimates the direct costs of blackouts using the Value of Lost Load (VOLL) methodology.[94] Dr. Fox-Penner asserts that generally, system-wide VOLL has been estimated to be $10-$20/kWh.[95]

95. Based on the $18.24/kWh estimate, Dr. Fox-Penner concluded that the direct costs of blackouts during the CERS Period were greater than $295 million. Moreover, if the summer outages would have occurred, as predicted by the ISO in March, an additional $10 to $40 billion in costs would have been incurred. Dr. Fox-Penner notes that this estimate, which is in-line with other estimates done, understate the actual costs because they do not account for indirect costs. Dr. Fox-Penner argues that Respondents were aware that their actions would lead to blackouts and extracted high prices from CERS under this threat.

### 7. Dr. Carolyn Berry[96]

96. Dr. Berry is an expert witness for the California Parties. Dr. Berry provides testimony comparing the sales Respondents made to CERS with (1) sales made to the CAISO by CERS and (2) sales made generally within the CAISO and CalPX prior to the creation of CERS.

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[93] Dr. Fox-Penner cites the United States Office of Technology Assessment, which developed a table describing different direct and indirect costs.

[94] VOLL is the value one or more customers place on avoiding an outage.

[95] This is based on EIA publications and other trade journal publications. Additionally, PG&E conducted a study in 2005 and found that the cost for a one hour outage to be $18.24/kWh.

[96] Ex. CAT-213.

97. Dr. Berry begins by summarizing the Commission's findings in Docket No. EL00-95. Dr. Berry states that the Commission found that out of market bilateral sales through the CAISO were unjust and unreasonable and ordered a mitigation of these sales to the Mitigated Market Clearing Prices (MMCP). Dr. Berry notes that the Commission required CERS's own OOM sales to the ISO be mitigated to the MMCP.

98. Dr. Berry states that CERS's bilateral transactions with Respondents at issue in this proceeding were the exact same transactions as CERS's sales to the CAISO. That is, CERS was merely the financial intermediary between the Respondents and the ISO and sold to the ISO at the same quantities and price. Dr. Berry notes that this is corroborated by the CAISO's transaction data.[97] Dr. Berry avers that the purpose of this proceeding is to determine if the initial contract between CERS and Respondents was unjust and unreasonable and that there is no economic justification for treating the CERS-Respondent transaction differently from the CERS-CAISO transaction.

### 8. Dr. Romkaew Broehm[98]

99. Dr. Broehm's testimony concerned the allegation that Respondents sold non-firm energy as firm. Because the California Parties do not assert this claim against any of the remaining Respondents, Dr. Broehm's testimony is not summarized below.

### 9. Dr. Robert Reynolds[99]

100. Dr. Reynolds is an expert witness for the California Parties. Dr. Reynolds' testimony evaluates whether there was evidence of the exercise of market power during the CERS Period.[100] Dr. Reynolds only reviewed in detail the data of TransAlta, which subsequently settled all its claims with the California Parties. However, Dr. Reynolds provided some general analyses that are described below.

101. Dr. Reynolds states that during the CERS Period, prices for short term power were the result of bilateral negotiations between CERS and suppliers. Dr. Reynolds states that

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[97] Specifically, Dr. Berry matched 97.5 percent of Coral's sales and 99.9 percent of TransCanada's sales (based on MWh).

[98] Ex. CAT-237.

[99] Ex. CAT-264.

[100] Dr. Reynolds only reviewed in detail the data of TransAlta, which subsequently settled all its claims with the California Parties. However, Dr. Reynolds provided some general analyses that are described below.

from CERS's standpoint, the cost of not procuring power depended on the magnitude of the resultant shortfall, which was extremely high because of the large negative consequences of blackouts.[101] Therefore, if CERS needed to bargain with "large suppliers," failure to complete a single purchase from a large supplier could result in large negative consequences. Dr. Reynolds notes that if the "large suppliers" were broken up into many smaller suppliers, the consequences of not purchasing from a single supplier would be less.

102. Based on this market situation, Dr. Reynolds generally concludes that (1) larger suppliers will tend to achieve higher day-of prices; (2) as the day-of market becomes more concentrated, CERS will pay higher prices; and (3) suppliers can profit by aggregating smaller supplies and then selling a large amount of energy to CERS.

103. Next, Dr. Reynolds examines the empirical evidence of market power during the CERS Period. Dr. Reynolds first conducts a statistical analysis to demonstrate that there was a difference in price paid to large and small suppliers. Dr. Reynolds states that this analysis demonstrates that CERS paid higher price to large suppliers.

104. Dr. Reynolds also conducted a regression analysis to test whether higher prices were paid by CERS in more concentrated markets. Dr. Reynolds asserts that the regression analysis confirms that the price paid by CERS increased as the market became more concentrated. Dr. Reynolds concludes that because market power existed and was exercised, a seller with market power could extract a premium (i.e. monopoly rent) in each transaction with CERS. However, Dr. Reynolds did not conduct a transaction by transaction analysis.

105. Lastly, Dr. Reynolds states that CERS did not exercise buyer market power, which if it existed, may have kept the prices from small suppliers low. Dr. Reynolds notes that unlike most situations where buyer market power exists, CERS was not able to reduce the quantity it purchased because CERS had an obligation to meet a certain demand.

### 10. Dr. Peter Berck[102]

106. Dr. Berck is an expert witness for the California Parties. Dr. Berck testifies regarding the impact of high wholesale energy prices on the California economy.

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[101] Dr. Reynolds notes that this is particularly the case in the day-of market because unlike shortages in the day-ahead market, there was no opportunity to procure energy in other markets.

[102] Ex. CAT-267.

Dr. Berck modeled the changes in real state personal income[103] and employment that would have occurred had California immediately passed through to consumers the costs of the CERS purchases.[104]

107. Specifically, Dr. Berck analyzed the effects of (1) a $4.97 billion pass through – the amount of all overcharges alleged; (2) a $2.11 billion pass through – the amount of all overcharges alleged in the Pacific Northwest market; and (3) a $1.05 billion pass through – the amount of overcharges from the Respondents in the Pacific Northwest.[105] The following Chart summarizes the conclusions of Dr. Berck's analysis:[106]

| | **$4.97 Billion Pass Through** | **$2.11 Billion Pass Through** | **$1.05 Billion Pass Through** |
|---|---|---|---|
| **Savings in Real State Personal Income by not Immediately Passing Through Costs** | $15.19 Billion | $6.31 Billion | $3.11 Billion |
| **Savings in Jobs by not Immediately Passing Through Costs**[107] | 105,000 | 44,300 | 21,900 |

108. Dr. Berck concludes that there is considerable evidence that pass through of overcharges to consumers in 2001 would have been deleterious to California and imposed extraordinary burdens on consumers.

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[103] Real state personal income is personal income, which includes all income beyond just wages, divided by the consumer price index.

[104] The model was not developed specifically for this proceeding, but rather, is a model used by the University of California to look at the effects of various legislative proposals.

[105] The third scenario includes sales made by Powerex, TransAlta, and the Avista Entities, which have subsequently settled with the California Parties.

[106] Dr. Berck also alleges that because of the size of the California economy, "there was an excellent chance" that the problems would spread to other states.

[107] For reference, at the beginning of 2001, there were 806,000 persons unemployed in California.

### B. The City of Seattle, Washington Direct Testimony for the Section 206 Claims

109. The City of Seattle, Washington (Seattle) has asserted claims against the following Respondents for spot market transactions during the Section 206 Period: Avista Corporation d/b/a Avista Utilities; Avista Energy, Inc.; Cargill Power Markets, Inc.; El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.); Exelon Generation Company, LLC (Successor-In-Interest to Constellation Energy Commodities Group, Inc.); PPL Montana, LLC and PPL EnergyPlus, LLC; Public Service Company of Colorado; Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C.; and TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. In support of their claims, Seattle presented the testimony and exhibits of Mr. Phillip Q. Hanser.[108]

110. Mr. Hanser is an expert witness for Seattle and his testimony addresses the following issues: (1) whether sellers in the Western market engaged in actions that violated the FPA, Commission regulations, seller tariffs, or the WSPP Agreement; (2) whether those violations affected the prices paid by Seattle; and (3) whether the violations impacted the price Seattle charged its retail customers.

111. First, Mr. Hanser provides general background information on Seattle City Light (SCL), a municipal utility owned by the citizens of Seattle and governed by the Seattle City Council. SCL operates Seattle's electrical, generation, transmission, and distribution facilities and provides power to customers in its 131 square mile service territory. Mr. Hanser describes SCL's strategic focus as utilizing its physical resources to provide low cost, reliable power to its customers after meeting its public responsibilities for fisheries enhancement, recreation, flood control, and coordinated river operations.

112. Mr. Hanser states that historically, fifty-five percent of SCL's load was served by its hydroelectric resources. SCL planned on average generation, expecting revenue shortfalls in low water years to be compensated by above average generation in other years. Mr. Hanser states that approximately one percent of SCL's load was procured on the spot market in 2000.

113. Next, Mr. Hanser discusses the structure of the Pacific Northwest and California markets. Mr. Hanser notes that all the transactions in the Pacific Northwest wholesale market during Section 206 Period were conducted under the WSPP Agreement. In California, Mr. Hanser states that there were three primary short-term wholesale markets during the period leading up to the Section 206 Period: (1) the CalPX day-ahead, day-of,

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[108] Ex. SCL-1.

and hour-ahead organized market; (2) the CAISO real-time market; and (3) CAISO bilateral Out of Market (OOM) purchases.

114. Mr. Hanser further states that that because of strong transmission interties, wholesale markets in the Pacific Northwest and California have taken advantage of a unique power trading relationship. Mr. Hanser notes that during the winter, when hydroelectric production is low, power from California is transmitted north to the Pacific Northwest. During the summer, the Pacific Northwest is able to transmit power south to California to support its high electric demand.

115. Mr. Hanser also describes SCL's participation in the Pacific Northwest and California wholesale markets. Mr. Hanser states that SCL has participated in the Pacific Northwest and California wholesale markets through bilaterally negotiated trades under the WSPP Agreement. During the Section 206 Period, Mr. Hanser states that SCL followed the same trading pattern that it historically had – buying energy to address winter deficits in hydroelectric production and selling surplus energy. Mr. Hanser also notes that SCL used the market to optimize the value of its hydroelectric resources. SCL would purchase energy during the lower priced off-peak periods and use and/or sell its resources during the high priced periods. However, Mr. Hanser asserts that because of low water conditions in 2000 and 2001, SCL's ability to optimize its resources was greatly limited.

116. Next, Mr. Hanser alleges that numerous sellers in the Western markets engaged in violations of the FPA, the Commission's regulations, tariffs, and the WSPP Agreement in 2000 and 2001. Reviewing his previously filed testimony from the California Refund Case, Mr. Hanser asserts that certain sellers, none of which are currently Respondents in this proceeding, engaged in the physical withholding of energy. Mr. Hanser argues that this withholding of energy raised prices and made it difficult for the CAISO to maintain reliability.

117. Mr. Hanser also examined eight gaming strategies that the Commission previously found were violations of the CAISO's Market Monitoring and Information Protocols (MMIP). After reviewing the testimony and filings made previously in this and other proceedings, Mr. Hanser concluded that certain sellers engaged in the gaming strategies in the Western markets in 2000 and 2001.[109] Mr. Hanser avers that these unlawful activities elevated prices.

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[109] Mr. Hanser does not allege specific conduct by any of the remaining Respondents in this proceeding, but does note that Avista had a long-term parking arrangement with Chelan County Public Utility District.

118. Next, Mr. Hanser asserts that the unlawful actions by sellers in Western markets directly affected the prices that SCL paid for wholesale power during the Section 206 Period. Mr. Hanser conducted a statistical analysis (Cointegration Analysis) to determine that the prices in the Pacific Northwest reflected the unlawful actions of sellers and other market dysfunction.[110] Mr. Hanser examined prices at the two major hubs in the Pacific Northwest Market – Mid-C and COB – and the NP-15 price in California. Mr. Hanser used one-month, two-month, and three-month ahead price data.

119. Specifically, Mr. Hanser's cointegration analysis consisted of (1) testing if the prices at Mid-C and COB were cointegrated and (2) testing if the prices at COB and NP-15 were cointegrated. Mr. Hanser states that if two price series are cointegrated, they are considered to fluctuate according to a stable long-term relationship – the prices are driven by common fundamentals. Mr. Hanser contrasts correlation with cointegration, stating that cointegration implies a more stable long-term relationship between two variables, regardless of time. Therefore, cointegration more accurately indicates that the same fundamentals drive the price of the two variables.[111]

120. Mr. Hanser found for each data series, in all but one instance,[112] the prices were cointegrated. Thus, Mr. Hanser concludes that the prices paid by Seattle at Mid-C were driven by the same fundamentals as the prices in California.

121. Lastly, Mr. Hanser avers that SCL's wholesale costs and retail rates reflect unlawful actions by sellers and market dysfunction that existed in California. Mr. Hanser first notes that the largest portion of SCL's costs has historically been for power purchased in the wholesale market. Mr. Hanser states that in 2000 and the first nine months of 2001, SCL was required to purchase large amounts of wholesale power because of unusually poor water conditions. This, coupled with the high prices during 2000 and 2001, required SCL to exceed its wholesale power budget estimate by almost $600 million.

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[110] The Cointegration Analysis only examines the period from January 18, 2001 through May 18, 2001. For the period from May 19, 2001 through June 20, 2001, Mr. Hanser conducted a "visual inspection" of the pricing data.

[111] With respect to Mr. Hanser's "visual inspection" of prices, Mr. Hanser states that the three prices moved substantially close together, indicating that the prices were closely related and cointegrated over the time period.

[112] The three-month forward price analysis for COB and NP-15 did not meet the threshold for cointegration. However, Mr. Hanser states that the results were extremely close to a finding of cointegration.

122. Mr. Hanser next describes how the Seattle City Council sets SCL's retail rates. Mr. Hanser notes that the Seattle City Council adheres to the following principles when setting SCL's rates: (1) rates reflect the cost of serving the customer and (2) rates are set to cover SCL's operating costs and not to generate profits. Mr. Hanser states that due to the high costs of wholesale purchases, caused by seller unlawful activity and market dysfunction, SCL passed five separate rate increases to recover the costs.[113] In all, the increases totaled $23/MWh, or 58 percent, for the average SCL customer. Mr. Hanser alleges that these rate increases resulted in serious harm to the SCL's retail customers.

### C. TransCanada Energy Ltd. Answering Testimony for the Section 206 Claims

123. TransCanada's Answering Testimony responds to claims asserted by the California Parties. TransCanada presented the testimony and exhibits of two witnesses in their direct case.

#### 1. Dr. John Morris[114]

124. Dr. Morris is an expert witness for TransCanada. Dr. Morris's testimony analyzes the allegations by the California Parties that (1) TransCanada engaged in price discrimination; (2) TransCanada sold energy to CERS at excessively high prices; and (3) TransCanada's sales to CERS seriously harmed the public interest.[115]

125. Dr. Morris begins by providing a general background on the Pacific Northwest market during the CERS Period. Dr. Morris states that the Pacific Northwest market was inherently competitive with many buyers and sellers. Dr. Morris notes that most retail load obligations were fulfilled with long-term contracts, and that short-term transactions were done via bilateral contracts. Dr. Morris states that this minimizes the likelihood of sellers exercising market power because a single transaction does not set the market price.

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[113] The rate increases are as follows: January 1, 2001 – 9.9 percent surcharge; March 1, 2001 – additional 9 percent surcharge and elimination of 9.1 percent summer discount; October 1, 2001 – 10.5 percent increase due to increase in BPA transmission rates; July 2001 – additional 9.3 percent increase.

[114] Ex. TRC-1.

[115] Dr. Morris also discusses the California Parties' allegation that TransCanada sold non-firm energy as firm. However, this allegation was subsequently withdrawn.

126. Dr. Morris next discusses the general conditions that led to abnormally high prices during the CERS Period. Dr. Morris contends that the high prices were due to a variety of factors, including lower than normal hydroelectric resources,[116] an abnormally warm and dry summer in 2000, limited natural gas supplies, and overall supply and demand conditions that made the Pacific Northwest a net importer of energy. Dr. Morris notes that utilities in the Pacific Northwest would meet their retail obligations and trade energy opportunistically to reduce their net operating expenses.

127. Dr. Morris further asserts that price differences between the Pacific Northwest and California markets indicate that the high prices were driven by the supply and demand conditions in the Pacific Northwest. Dr. Morris notes that prices were sixty-three percent higher at COB and twenty-three percent higher at Mid-C compared to NP15 prices in California. Additionally, Dr. Morris contends that the sustained price difference between markets indicates that the two markets are separate geographic markets.

128. Next, Dr. Morris discusses the overall supply and demand conditions in California specifically. Dr. Morris first notes that hydroelectric production in California declined by thirty-seven percent from 1999 to 2001. Additionally, demand exceeded supply by twenty-five percent.

129. Dr. Morris also describes California's market restructuring and its effects on the overall market conditions. Dr. Morris notes that the retail rate caps, which were below the cost of wholesale power, contributed to the shortage conditions because demand did not change in response to the wholesale cost increases.[117] Dr. Morris states that this also lead to financial distress of the California IOUs, further decreasing the supply produced from Qualifying Facilities.[118] Furthermore, Dr. Morris states that very little new generation was added in California in the ten years prior to the energy crisis. Dr. Morris also avers that PG&E and SoCal Edison failed to build up their natural gas storage inventory in late 2000, reducing the amount of natural gas available to produce electricity.

130. Dr. Morris further argues that the high prices paid by CERS in the Pacific Northwest were part of a policy where CERS would pay higher prices and buy greater

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[116] From 1999 to 2001, hydroelectric production declined forty-two percent.

[117] Dr. Morris notes that a ten percent reduction in retail consumption would have reduced CERS's wholesale demand by 2,500 MW on average.

[118] Nonpayment to Qualifying Facilities began as early as November 2000 and by early 2001 as many as one third of the Qualifying Facilities ceased operating.

quantities outside California in order to drive prices down in California. Dr. Morris states that the Commission has also found that CERS was granted undue preference in its acquisition of power because it had access to CAISO information that other market participants did not have.

131. Dr. Morris next contends that retail rate increases would not have been onerous on ratepayers. Dr. Morris states that rate increases to reduce consumption can be crafted so that overall rates do not increase significantly. Dr. Morris cites California's thirty percent increase in March 2001 and a 20/20 conservation program adopted in May 2001.[119] Dr. Morris notes that together, these two programs raised prices by 110 percent for the last twenty percent of consumption.

132. Next, Dr. Morris provides background information specific to TransCanada's sales to CERS. Dr. Morris states that TransCanada is an energy marketer and did not own or control generation assets during the CERS Period.[120] Dr. Morris notes that the vast majority of energy sold to CERS was sourced from real-time purchases out of the Power Pool of Alberta (PPoA). Additionally, because TransCanada had limited rights to export energy out of Canada, TransCanada was not a major participant in West Coast power markets.[121] Dr. Morris states that TransCanada often had the ability to sell up to fifty MWh of energy from Canada to entities in the United States, but this was limited by TransCanada's ability to obtain transmission.

133. Dr. Morris states that there were several differences in TransCanada's sales to CERS and sales to non-CERS buyers. First, Dr. Morris notes that virtually all of TransCanada's sales to CERS occurred at COB, whereas other parties purchased energy at other locations on the BPA system. Dr. Morris notes that prices at COB were $37.22/MWh greater on average than other locations on BPA.[122] Second, Dr. Morris

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[119] Consumers would receive a twenty percent rebate if they reduced consumption by twenty percent.

[120] Affiliates of TransCanada did own a modest amount of generation within Canada.

[121] Dr. Morris calculates TransCanada's market shares in the Pacific Northwest as typically below 0.4 percent and never above 1 percent. This was calculated by dividing TransCanada's total sales in the Pacific Northwest by the total consumption in the Pacific Northwest for each day TransCanada sold power.

[122] When analyzing price discrimination claims, Dr. Morris states that the value of transmission is this price differential. Moreover, Dr. Morris alleges that the price

(continued…)

states that the timing of transactions with CERS was different. Dr. Morris notes that (1) when a transaction was agreed to; (2) the duration of the transaction; and (3) the delivery hour may impact price. Dr. Morris states that Dr. Fox-Penner's price discrimination analysis only accounts for the delivery hour. Third, Dr. Morris states that there was greater risk selling to CERS due to creditworthiness. Dr. Morris notes that the Commission has imposed a credit risk adder due to the risk associated with selling to certain counterparties. Dr. Morris further notes that when CERS was created, the California Legislature did not include appropriate funding mechanisms to ensure CERS's creditworthiness. As a result, TransCanada imposed credit limits on CERS to minimize its risks.[123] Dr. Morris states that the likely effect of the credit limit on CERS was that smaller quantities would be sold at a given time (because TransCanada would not want to use its entire credit on low profit sales) and the prices charged to CERS would be higher.

134. Dr. Morris also states that TransCanada's transactions with CERS had the additional risk of TransCanada not knowing the price to acquire energy in real-time from the PPoA. This was particularly true for transactions for multiple hours because TransCanada would not know the PPoA price until after it made its purchases for resale to CERS. Dr. Morris also notes that in Dr. Fox-Penner's price discrimination analysis, Dr. Fox-Penner compared transactions with CERS that had an average duration of 10.25 hours with non-CERS transactions of a single hour.

135. Dr. Morris further argues that sellers faced a litigation risk when transacting with CERS. Dr. Morris contends that Dr. Fox-Penner improperly ignored this litigation risk when comparing prices.

136. Next, Dr. Morris addresses the California Parties' claims of price discrimination in more detail. Dr. Morris states that price discrimination occurs when a seller sells identical goods or services to different, but similarly situated, buyers at different prices that are not accounted for by a difference in the cost of supplying the buyers. With respect to "undue" price discrimination, Dr. Morris contends that Dr. Fox-Penner employs arbitrary criteria to make a distinction between due and undue discrimination.

137. Dr. Morris states that five criteria must be met for price discrimination to occur: (1) sales to two or more buyers; (2) buyers must be similarly situated; (3) the price for

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differential is so great that one would generally conclude that there are separate geographic markets and that no valid comparison can be made.

[123] Initially CERS's credit limit was $3 million. It was later increased to $23 million in March 2001. Dr. Morris also cites trader tapes describing TransCanada's ongoing credit concerns.

one buyer is greater than the price for another buyer; (4) the same product must be sold; and (5) the seller must have a mechanism preventing the lower priced buyer from reselling at the higher price. Dr. Morris further notes that just because the seller sells at different prices to different customers, it does not indicate seller market power. Rather, other explanations, such as buyer market power, may account for the difference.

138. Moreover, Dr. Morris states that TransCanada did not have the ability to price discriminate because it could not prevent non-CERS buyers from reselling the energy to CERS at the higher price. Dr. Morris contends that because TransCanada had a small market share, any other seller would be similarly situated and sell to CERS.

139. Dr. Morris also discusses price discrimination by a buyer and the correlated factors that must be shown: (1) two or more sellers; (2) similarly situated sellers; (3) the price from a seller is different than the price from another seller; (4) the same product; and (5) a mechanism to prevent the selling to a higher priced buyer. With respect to CERS, Dr. Morris alleges that as a buyer, CERS had a mechanism that prevented sellers from reselling the energy from California to other buyers. Dr. Morris states that this activity would have been considered a "False Export" and therefore, allowed CERS to pay only low prices in California. Dr. Morris states that unless CERS was exercising buyer market power in California, there was no incentive to engage in the alleged "False Export" transactions. Thus, Dr. Morris alleges that CERS had buyer market power. Dr. Morris further argues that unlike seller price discrimination, buyer discrimination decreases market efficiency because there is less energy available to sell.

140. Next, Dr. Morris specifically addresses Dr. Fox-Penner's price discrimination analyses. Dr. Morris notes that Dr. Fox-Penner presented two types of analyses: (1) an analysis based on average prices and (2) an analysis based on individual transactions. Dr. Morris avers that Dr. Fox-Penner improperly used broad average prices and ignored the specifics of each transaction, such as duration, firmness, location, volume, and credit terms. Thus, Dr. Morris concludes that the average price analysis provides no probative information because the buyers may not be similarly situated.

141. Dr. Morris asserts that using a five-month average among different buyers ensures that transactions are not similarly situated. Dr. Morris notes that there was a wide range of average prices for different buyers during the five month period and that these differences are not attributable to price discrimination. Rather, the prices vary depending on a variety factors associated with the individual transactions. For instance, during the CERS Period, TransCanada's average price to CERS was only the fifth highest among all buyers of day-of energy.

142. Dr. Morris also criticizes the data used by Dr. Fox-Penner for this average price analysis. Dr. Morris notes that Dr. Fox-Penner used TransCanada's monthly profit statements and that there were errors transcribing the data into Dr. Fox-Penner's workpapers, such as erroneously including transactions that facilitated transmission and

did not involve the buyer maintaining control of the energy. Additionally, Dr. Morris notes that the non-CERS "monthly" sales include longer-term contracts. Thus, to a degree, Dr. Fox-Penner is comparing long-term sales with spot market sales to CERS. Accounting for the data errors, Dr. Morris states that the average price to CERS over the entire CERS Period was $322, compared to $281 for non-CERS buyers. Dr. Morris states that accounting for credit risk[124] and locational differences,[125] CERS actually paid less, on average, than the non-CERS buyers. Additionally, Dr. Morris notes that TransCanada's average price to CERS (roughly $301) is approximately the same as the average price paid by non-CERS buyers to Powerex ($309) and Coral ($294).

143. With respect to Dr. Fox-Penner's transaction-based analysis, Dr. Morris contends that this analysis is also flawed. First, Dr. Morris notes that in most instances there was not an identical sale to a non-CERS buyer.[126] For the remainder of the hours, Dr. Morris notes that Dr. Fox-Penner claims price discrimination in only 22 of the 2,596 hours. Thus, Dr. Morris notes that in over 99 percent of the hours, there is no claim of price discrimination. Dr. Morris states that this conclusion supports his position that TransCanada was incapable of price discriminating during the CERS Period.

144. For the twenty-two instances of alleged price discrimination where there was not an identical transaction, Dr. Morris contends that Dr. Fox-Penner did not logically explain how price discrimination could occur without a similarly situated buyer. Rather, Dr. Fox-Penner found price discrimination if the price was more than six standard deviations from the average non-CERS price at COB during the day. To demonstrate the problems with this type of analysis, Dr. Morris notes that in one instance, for another Respondent, even though the price to CERS was forty-two standard deviations above the mean, Dr. Fox-Penner appropriately concluded no price discrimination occurred because there was a "matching transaction" that was only $8 less than the price to CERS. Dr. Morris asserts that this demonstrates that using a standard deviation test based on

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[124] Dr. Morris uses a ten percent adder, which was used by the Commission for calculating refunds in California. Dr. Morris contends that this ten percent adder is conservative and estimates that the risk premium to CERS was approximately twenty-four percent (based on the CERS/non-CERS price difference at COB among all sellers).

[125] The Locational Difference is the difference in price of non-CERS sales at COB with the average price on BPA's system, other than COB.

[126] There are only fourteen hours with allegedly identical transactions and Dr. Fox-Penner makes a price discrimination claim in only four of those hours.

average daily prices fails to account for specific market conditions associated with each transaction.

145. Moreover, Dr. Morris notes that the twenty-two hours of alleged price discrimination all occurred within a single day – February 22, 2001. Dr. Morris states that the hours on this day met Dr. Fox-Penner's screen because the standard deviation on that particular day was abnormally low. Therefore, even though the price difference to CERS was lower than the adjacent days, Dr. Fox-Penner found price discrimination.

146. With respect to the four instances where Dr. Fox-Penner found "matching transactions" and price discrimination, Dr. Morris states that Dr. Fox-Penner did not account for differences in the transactions. Dr. Morris further notes that in five of the hours with matching transactions, CERS actually paid less than the non-CERS buyer.[127] Moreover, Dr. Morris contends that had Dr. Fox-Penner conducted an analysis across all fourteen "matching" transactions, he would not have concluded that TransCanada engaged in price discrimination because there was not a statistically significant difference in prices to CERS.

147. Moreover, Dr. Morris contends that the CERS and non-CERS buyers were not similarly situated because (1) the transactions had different delivery locations, (2) the transactions were conducted at different times and for different durations, and (3) the buyers had different risk profiles. With respect to credit risk, Dr. Morris argues that Dr. Fox-Penner's "after-the-fact" analysis of CERS's credit risk does not appropriately account for the risk perceived at the time. Dr. Morris notes that accounting only for the delivery location and adding ten percent for CERS's credit risk, the differential in price is entirely negated and CERS paid a lower value than the non-CERS buyer in matching transaction.

148. Dr. Morris next states that Dr. Fox-Penner incorrectly makes four additional claims regarding matching transactions in May and June 2001. Dr. Morris states that these additional transactions improperly compare non-firm sales to CERS with firm sales to non-CERS buyers. Additionally, for two transactions in May 2001, the price to CERS was significantly lower than the non-CERS prices. Lastly, Dr. Morris notes that the remaining two transactions from June 2001 improperly compare single hour day-of sales to CERS with an off-peak eight hour day-ahead transaction to a non-CERS buyer. Dr. Morris further states that Dr. Fox-Penner admits that the evidence does not support a claim of price discrimination against TransCanada in June 2001.

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[127] In four more hours, the difference was $5/MWh or less.

149. In closing, Dr. Morris notes that CERS would have paid no more than 0.3 percent higher prices from TransCanada even assuming that all twenty-six allegations of price discrimination were true.

150. Next, Dr. Morris discusses the California Parties' allegation that TransCanada charged CERS excessive prices. First, Dr. Morris states that there is no economic definition of "excessive price." Dr. Morris states that the only definition of excessive prices provided by the California Parties was Mr. Taylor's response to a data request that excessive prices are prices that exceed what would be experienced in a workably competitive market or prices that substantially exceed prices charged to other similarly situated customers. Dr. Morris avers that prices in the Pacific Northwest were at workably competitive levels given the supply and demand conditions.

151. Dr. Morris also asserts that TransCanada lacked market power. Dr. Morris contends that after accounting for the location of the sales, risk associated with selling to CERS, and other factors, the prices from TransCanada were not excessive compared to other sellers. Moreover, Dr. Morris notes that the California Parties presented no evidence, such as withholding, that TransCanada market power influenced prices in the Pacific Northwest market. Rather, Dr. Morris repeats his assertion that the high prices were caused by a variety of factors, including poor hydroelectric conditions, supply and demand, limited supply of natural gas, and other fundamental market conditions. Dr. Morris further notes that TransCanada's market share was between 0.4 and 1 percent, far below the amount that would indicate market power.

152. Dr. Morris also addresses Dr. Fox-Penner's assertion that the high prices served no useful economic purpose. Dr. Morris avers that the high prices served four legitimate purposes: (1) indicated that the buyer who valued the energy most was able to purchase it; (2) attracted additional supplies; (3) compensated suppliers for the additional risk of selling to CERS; and (4) incentivized CERS to shift to long-term contracts.

153. Dr. Morris also discusses Dr. Fox-Penner's claim that prices were "inefficiently high" because the prices exceeded the price sufficient to pay for the entry of new combustion turbine facilities in 2001. First, Dr. Morris asserts that Dr. Fox-Penner wrongly calculated revenues to cover capital costs for only a 4.2 year period because capital recovery is usually calculated for a 15 to 20 year time frame. Dr. Morris notes that combustion turbines typically have utilization rates of only three percent; therefore, the financial data used by Dr. Fox-Penner do not indicate that prices were high enough to attract new entry. Second, Dr. Morris avers that Dr. Fox-Penner used costs that appear to be too low because he does not consider start-up costs or emission costs. Third, Dr. Morris states that Dr. Fox-Penner did not consider California's market structure, which did not have a capacity market at the time. Dr. Morris states the California market was designed such that only net profits would incentivize new entry. Dr. Morris states that the new entry of generation following the CERS Period, when prices were lower,

was the result of CERS and the IOUs entering into long-term contracts, not the result of spot market prices.

154. With respect to Mr. Taylor's claim of excessive prices, Dr. Morris contends that Mr. Taylor is inconsistent and does not present an economically rational basis. Dr. Morris notes that Mr. Taylor used the *Power Markets Week* high price at Mid-C plus $75 as a benchmark to compare prices even though Mr. Taylor admitted that those prices were substantially higher than workably competitive prices.

155. Additionally, Dr. Morris states that Mr. Taylor wrongly claims that parking energy is a manipulative activity. Dr. Morris notes that parking is a normal trading activity and that Mr. Taylor is actually alleging that sellers withheld energy in the CalPX and CAISO markets. With respect to TransCanada, Dr. Morris notes that TransCanada never sold in either the CalPX or CAISO markets.

156. Dr. Morris also responds to Mr. Taylor's claims that TransCanada should have sold more energy in the day-ahead markets and that TransCanada held out for higher prices in real-time. Dr. Morris states that TransCanada typically did not have the ability to guarantee day-ahead delivery because of transmission scheduling. Moreover, Mr. Taylor admitted that TransCanada was under no obligation to sell in day-ahead markets. Dr. Morris further asserts that there was no guarantee that the real-time price would exceed the price in the day-ahead market, particularly if CERS purchased day-ahead energy in excess of its real-time needs. Dr. Morris states that the fact that real-time prices were often higher only indicates that CERS did a poor job managing its day-ahead and long-term trading strategies. Therefore, by shifting demand to the day-of market, CERS drove the real-time prices higher and the day-ahead prices relatively lower.[128]

157. Dr. Morris argues that Mr. Taylor wrongly alleges that TransCanada was at a significant bargaining advantage with CERS. Dr. Morris notes that TransCanada often had the lowest price compared to other sellers to CERS and that trader tapes demonstrate that CERS would often not complete transactions with TransCanada due to price. Moreover, Dr. Morris states that TransCanada cannot be considered a "pivotal supplier" because it only provided small quantities of energy to CERS. Dr. Morris also notes that CERS hired experienced traders and had access to ISO information other traders did not have and were not at an "inexperience disadvantage." Dr. Morris notes that CERS's

[128] Dr. Morris states that this strategy actually lowered CERS' overall acquisition costs even though the day-of prices were higher. Dr. Morris estimates this to be as much as $800 million.

inability to enter into long-term contracts was the result of California statute, not TransCanada.

158. Next, Dr. Morris contends that CERS benefited from the real-time sales due to the costs of blackouts, which exceeded the price that TransCanada sold energy, particularly because TransCanada's average price was lower than the "supplier of last resort." Dr. Morris notes that CERS's benefit far exceeded the benefit TransCanada received by supplying CERS, indicating that CERS had market power in its transactions.

159. Next, Dr. Morris addresses the documents cited by Mr. Taylor that Mr. Taylor claims show duress, fraud, bad faith, and market manipulation. The first document cited by Mr. Taylor is Mr. Hart's direct testimony.[129] Dr. Morris notes that TransCanada is only mentioned once and that Mr. Hart only states that TransCanada sold "substantial quantities to CERS in real time at very high prices." Dr. Morris states that Mr. Hart does not allege any specific inappropriate behavior on the part of TransCanada. With respect to Mr. Hart's claim that sellers were holding out until the last minute, Dr. Morris argues that if sellers were actually withholding, the price in the day-ahead market would rise until it became economical to sell in the day-ahead market. Because this did not occur, Dr. Morris concludes that CERS was likely under buying in the day-ahead market.

160. Dr. Morris contends that the remaining documents cited by Mr. Taylor either don't mention TransCanada at all or do not support allegations of duress, fraud, or other wrongdoing. For example, one document cited by Mr. Taylor is a memorandum detailing CERS's purchasing strategy; another document is an email chain describing CERS's general credit issues with suppliers. Dr. Morris states that other documents purport to show that TransCanada bought energy in the day-ahead market from other suppliers and sold energy to CERS in real-time. Dr. Morris argues that there is nothing illegal about these actions and TransCanada did not violate any regulation or tariff rule.

161. Next, Dr. Morris discusses Mr. Taylor's use of price as evidence of duress, fraud, or bad faith.[130] Dr. Morris first notes that high prices are not evidence of wrongdoing, but rather a reflection of market conditions. Moreover, Dr. Morris states that the benchmark used by Mr. Taylor is an average and does not consider peak demand periods.

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[129] Ms. Lee makes the same allegations as Mr. Hart in her direct testimony, which is also cited by Mr. Taylor.

[130] Mr. Taylor compares the price to CERS with the *Power Markets Weekly* price plus $75/MWh. Mr. Taylor also finds evidence of duress, fraud, or bad faith if Dr. Fox-Penner found price discrimination.

Lastly, Dr. Morris contends that there is nothing improper in accepting a price that CERS was willing to pay.

162. Dr. Morris also argues that Mr. Taylor improperly used Dr. Fox-Penner's price discrimination analysis. As discussed above, Dr. Morris notes that this analysis contained serious flaws. Moreover, Dr. Morris states that Mr. Taylor concluded price discrimination for an entire day even when Dr. Fox-Penner only found price discrimination in one or two hours.

163. Dr. Morris further asserts that Mr. Taylor wrongly relied on the CAISO Emergency Status because CAISO emergencies were the result of CERS failing to procure enough energy in the day-ahead market. Therefore, the emergency status does not reveal that CERS was under duress when purchasing or that TransCanada caused any emergency.

164. Therefore, Dr. Morris concludes that Mr. Taylor's 1(A) and 1(B) determinations lack evidentiary support. Moreover, Dr. Morris notes that Mr. Taylor admitted that his determinations are subjective judgments and there is no way of replicating the results.

165. Lastly, Dr. Morris asserts that Mr. Taylor wrongly alleges that TransCanada's sales to CERS seriously harmed the public interest and caused an excessive burden on consumers. As discussed above, Dr. Morris states that TransCanada's sales benefited CERS by expanding the energy supplies and sold to CERS at prices lower than other providers. Additionally, Dr. Morris notes that had TransCanada's sales been at the market clearing price, CERS's total expenditure would have only decreased by one half of one percent.

166. Dr. Morris further states that California's decision to finance the high costs of energy over a longer period of time has been done in similar situations, such as Maryland in 2006. Dr. Morris notes that relative to average prices in the United States, California prices remain approximately twenty-seven percent higher, the same level as in 1990.

167. Dr. Morris contends that abrogating the contracts in this proceeding would set a bad precedent for future markets where supply is tight and suppliers will be incentivized to avoid making sales during such shortages. Moreover, the wrongdoing of third parties should not affect the contracts entered into between CERS and TransCanada.

### 2. Mr. Kenneth Kunz[131]

168. Mr. Kunz was the Manger of Financial Market Trading at TransCanada during the CERS Period. Currently, Mr. Kunz is TransCanada's Vice President of Western Power and a Board Member of the WECC. Mr. Kunz's testimony addresses allegations of (1) undue discrimination; (2) duress, fraud, and bad faith; and (3) TransCanada being described as a "pivotal supplier."[132]

169. Mr. Kunz begins his testimony by describing the relevant history regarding transactions between TransCanada and CERS. Mr. Kunz states that TransCanada first began selling energy to CERS on January 31, 2001. The source of the energy was either (1) 50 MWh or less purchased from the Power Pool of Alberta (PPoA)[133] or (2) energy purchased in the Pacific Northwest market at the urging of CERS traders. Mr. Kunz notes that TransCanada never purchased energy from California to resell to CERS.

170. With respect to energy initially purchased in the PPoA, Mr. Kunz states that the pricing mechanism and price volatility created challenges for TransCanada. Specifically, Mr. Kunz notes that the PPoA was a deregulated market and the hourly pool price is not known until the hour is over, after all the transactions have occurred. Therefore, TransCanada did not know what price it would pay for energy until after the energy was already resold to CERS. Mr. Kunz asserts that Dr. Fox-Penner failed to consider this in his analyses.

171. Next, Mr. Kunz evaluates the California Parties' claim of undue discrimination on the basis that TransCanada charged excessive prices on February 22, 2001. Mr. Kunz states that the transactions for this period followed the typical pattern dealings between TransCanada and CERS. Specifically, TransCanada contacted CERS offering non-firm energy; CERS then made a bid; TransCanada countered; and finally, the two parties agreed on a price "in the middle." Mr. Kunz states that the price agreed to ($325/MWh) was similar to the prices CERS was paying from other suppliers.[134] Mr. Kunz states that

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[131] Ex. TRC-77.

[132] Mr. Kunz also discusses the California Parties' allegation that TransCanada sold non-firm energy as firm. However, this allegation was subsequently withdrawn.

[133] This source accounts for approximately ninety percent of the transactions between TransCanada and CERS.

[134] A second agreement was made for peak hour delivery at $350/MWh and this energy was subsequently "rolled over" into later hours at mutually agreed upon prices. However, each price was "within the range" of prices paid by CERS.

this pattern of dealing continued the following day and was typical of all transactions between TransCanada and CERS.

172. Next, Mr. Kunz discusses the California Parties' allegations of duress, fraud, and bad faith. Mr. Kunz states that TransCanada has reviewed over 350 tape recordings of negotiations between TransCanada and CERS and found no evidence of wrongdoing. Mr. Kunz notes that in many instances, CERS turned down offers if the price was too high and negotiated lower prices. Other times, CERS simply turned down TransCanada's offer. Mr. Kunz also states that the non-firm energy could be turned down by CERS at any moment, including after the initial agreement was reached.

173. Mr. Kunz also argues that California Parties wrongly claim that TransCanada parked and withheld energy until real-time to extract higher prices. Mr. Kunz states that the timing of TransCanada's sales to CERS was consistent with CERS and TransCanada's general practice. Mr. Kunz notes that in light load hours, CERS would not accept offers until shortly before the time periods. With respect to the two transactions where parking actually occurred, Mr. Kunz notes that neither transaction involved purchasing energy from California; rather the energy was either bought at the Oregon/Washington border or the U.S./Canada border.

174. Lastly, Mr. Kunz addresses California Parties' allegation that TransCanada was a "pivotal supplier" to CERS. Mr. Kunz notes that TransCanada typically sold 50 MWh or less to CERS in each hour and CERS was purchasing up to 6,500 MW per hour. Mr. Kunz also notes that CERS often turned down TransCanada when it did not need any more energy.

### D. TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. Answering Testimony for the Section 206 Claims

175. TransAlta's Answering Testimony responds to claims asserted by the California Parties and City of Seattle. Because TransAlta and the California Parties have settled all outstanding claims, the testimony related to those claims is not summarized below. TransAlta presented the testimony and exhibits of three witnesses.

#### 1. Mr. Wes Harrigan[135]

176. Mr. Harrigan is currently Manger-West Team Trading for TransAlta Corporation. During the relevant period, Mr. Harrigan was West Cash Trader, primarily focused on

[135] Ex. TAE-1.

day-ahead trading, for TransAlta. Mr. Harrigan's testimony provides general background information about the state of the market and how the market influenced TransAlta's behavior.

177. First, Mr. Harrigan describes the overall market conditions during the relevant period. Mr. Harrigan states that the supply and demand conditions were "pretty tight" at the start of the relevant period due to high winter demand in the Pacific Northwest market and below average snowpack and precipitation. Mr. Harrigan states that this required BPA to conservatively manage their hydro resources and limit the generation output.[136] Additionally, California was experiencing energy shortages north of Path 15, requiring California to rely on Pacific Northwest power. Mr. Harrigan notes that California's reliance on Pacific Northwest resources led to more competition in the Pacific Northwest markets and higher prices.

178. Mr. Harrigan asserts that this unique supply and demand condition led to trading patterns that had not previously occurred. Mr. Harrigan states that typically Mid-C was always the lowest priced markets; however, during the relevant period, prices in California and the Desert Southwest were lower than prices in the Pacific Northwest.

179. Mr. Harrigan states that these market conditions had a direct impact on TransAlta. Mr. Harrigan notes that TransAlta owned two 670 MW generating units (Centralia) with long-term sales commitments and did not have diversity in its generation sources. Therefore, if one unit had an outage, TransAlta had to procure power to keep its obligations. Mr. Harrigan notes that TransAlta procured energy from other markets to be sold in the Pacific Northwest market in order to minimize risk and benefit economically. TransAlta also competed in the transmission market to wheel power from SP15, Palo Verde, and NP15 into the Pacific Northwest market.

180. During the relevant period, Mr. Harrigan states that TransAlta engaged in proprietary trading and managing its Centralia generation asset. Mr. Harrigan notes that TransAlta was active in the real-time, day-ahead, and long-term markets, but not active in market speculation because of the high volatility and internal risk limits. Mr. Harrigan states that most of the trading was done against transmission rights held by TransAlta or through marketing agreements that allowed TransAlta to source power at one location and sink it at another based on the price difference between locations. For the real-time and day-ahead markets, Mr. Harrigan asserts that TransAlta was primarily interested in

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[136] Mr. Harrigan states that BPA was also mandated by the Department of Energy to send energy to California. Mr. Harrigan states that this required BPA to buy additional megawatts at Mid-C to meet demand.

selling its uncommitted output from the Centralia plant, making up for any shortages in its long-term commitments and hedging risk against a plant outage.[137]

181. Mr. Harrigan states that when TransAlta first acquired Centralia, the previous owners must have slowed down operations at the adjacent coal mine because there were not sufficient coal reserves to operate the plant as baseload. Therefore, TransAlta optimized operation of the plant by allocating the output to the highest priced periods. Additionally, Mr. Harrigan states that there were several outages at Centralia, leaving TransAlta vulnerable to high real-time prices. Mr. Harrigan states that in order to minimize the risks associated with the outages, TransAlta traders were instructed to sell everything on a unit-contingent basis if possible. TransAlta sold the Centralia output on firm and unit-contingent basis and left a portion unsold to mitigate against unplanned outages. Mr. Harrigan notes that because of the high prices, TransAlta "self-insured" its sales from Centralia by purchasing in the day-ahead market. Mr. Harrigan notes that this allowed TransAlta to mitigate any shortage from Centralia and to sell any excess energy it may have in real time.

182. With respect to TransAlta's transmission arrangements, Mr. Harrigan states that TransAlta's contracting strategy was to sell power at the plant gate, but for some short-term sales TransAlta arranged for transmission to a particular location.

183. Next, Mr. Harrigan states that TransAlta's trading operations not related to the Centralia plant were based on locational price spreads, which provided traders an indication of where there was excess power and where there was shortage or power.[138] Mr. Harrigan states that the majority of power bought by TransAlta was either (1) forward transactions from before the relevant period; (2) power bought with the intention of selling in higher priced markets; or (3) power to cover Centralia.

184. With respect to the trading associated with managing risk at Centralia, Mr. Harrigan states that TransAlta would evaluate the risk daily based on real-time and day-ahead prices and Centralia's obligations. Mr. Harrigan notes that because prices were lower in the Desert Southwest and SP15 markets, TransAlta would often buy in these lower priced markets to cover Centralia.

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[137] TransAlta entered into long-term contracts for a portion of the output from Centralia. Approximately seventy percent of the sales from Centralia were long-term contracts.

[138] Mainly, TransAlta would purchase from Desert SW and SP15, where the price was lower than the Pacific Northwest market. Mr. Harrigan also notes that LADWP often had available South to North transmission which helped move the energy.

### 2. Mr. A. Joseph Cavicchi[139]

185. Mr. Cavicchi is an expert witness for TransAlta. Mr. Cavicchi's testimony concerns allegations made Seattle regarding TransAlta's market behavior during the relevant period. Generally, Mr. Cavicchi concludes that Seattle provided no evidence that TransAlta's actions affected prices paid by Seattle.

186. Mr. Cavicchi first provides background information on TransAlta. As discussed in Mr. Harrigan's testimony, TransAlta was a power marketer and also controlled the Centralia generation plant. Mr. Cavicchi notes that TransAlta was granted market-based rate authority in 1998 and 1999.

187. Mr. Cavicchi states that energy marketers provide liquidity and efficiency to the wholesale market by buying and reselling energy. Additionally, marketers provide value-added service by tailoring products to specific sellers. Mr. Cavicchi also repeats Mr. Harrigan's testimony regarding TransAlta's role in managing Centralia. Mr. Cavicchi notes that TransAlta had minimum monthly load factor requirements for its sales from Centralia, which required TransAlta to supply power even in the event of outages.

188. Mr. Cavicchi states that in order to hedge against Centralia outages, TransAlta would carefully manage its power supply portfolio. Mr. Cavicchi notes that seventy-three percent of TransAlta's purchases were done more than one week ahead of delivery and eighty-three percent more than one day ahead. TransAlta also diversified its supply portfolio by acquiring a variety of transmission rights in California, the southwest, and Pacific Northwest. Mr. Cavicchi states that this was done to manage the risk associated with Centralia outages, noting that the risk was particularly great during the relevant period because of the high price of spot market energy. Mr. Cavicchi states that any excess energy purchased to hedge against a Centralia outage would be resold to balance its portfolio. Mr. Cavicchi also notes that TransAlta also marketed production from Centralia that was not already sold by seeking opportunities to maximize the value of Centralia's output.

189. Lastly, Mr. Cavicchi describes TransAlta's marketing and trading. Mr. Cavicchi states that TransAlta sought profitable sales opportunities, risk management, and any arbitrage opportunities. Mr. Cavicchi states that this was often done based on price differentials between regions.

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[139] Ex. TAE-8.

190. Mr. Cavicchi also describes the overall market conditions during the CERS Period. As stated by other witnesses, Mr. Cavicchi describes the reduced hydroelectric generation output and increased demand as the primary reason for energy shortages and high prices.

191. Lastly, Mr. Cavicchi responds to the claims asserted by the City of Seattle. Mr. Cavicchi contends that Seattle provided no analysis of specific transactions. Mr. Cavicchi notes that Mr. Hanser describes a number of market manipulation practices, but does not allege that TransAlta engaged in any of them. Additionally, TransAlta has never been found to have engaged in such activity.

192. Mr. Cavicchi notes that Seattle similarly sold energy in the Pacific Northwest market during the relevant period. Mr. Cavicchi states that for hours where both Seattle and TransAlta were selling power, Seattle sold at a higher price more often than TransAlta (151 versus 38).

193. Additionally, Mr. Cavicchi notes that Seattle includes longer term transactions in its data which are not part of the "spot" market sales in this proceeding. These longer term transactions represent seventy eight percent of the revenue of sales between TransAlta and Seattle.

#### 3. Mr. Christopher Cavanagh[140]

194. Mr. Cavanagh's testimony only concerned claims asserted by the California Parties against TransAlta.

### E. Shell Energy North America (U.S.), L.P., d/b/a Coral Power, L.L.C. Answering Testimony for the Section 206 Claims

195. Coral's Answering Testimony responds to claims asserted by the California Parties. Coral presented the testimony and exhibits of two witnesses.

#### 1. Ms. Beth Bowman[141]

196. Ms. Bowman is currently Senior Vice President at Shell Energy North America (U.S.), LP. During the relevant period, Ms. Bowman was responsible for the management and oversight of Coral's marketing and power trading operations in the WECC. Ms. Bowman's testimony provides general background information about

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[140] Ex. TAE-18.

[141] Ex. SNA-1

Coral's activities in the bilateral markets in the Pacific Northwest during the relevant period.

197. Ms. Bowman states that Coral was a marketing and trading company that purchased and resold energy with many parties across the Western United States. With the exception of twenty-eight megawatts within the ISO, Coral did not own or control any generation assets. Ms. Bowman states that Coral employed a staff whose sole responsibility was to negotiate, manage, and maintain transaction enabling agreements[142] with other energy counterparties and service agreements with generators and transmission owners. Ms. Bowman notes that Coral evaluated counterparties' credit in order to enable instantaneous transactions pursuant to an enabling agreement.

198. Ms. Bowman states that Coral would monitor the gas and power markets to locate temporal, locational, or market discontinuities in order to capture profits based on price differentials. Ms. Bowman notes that the enabling agreements allowed Coral to act quickly on any price differential. Ms. Bowman also states that Coral would contract with generation and transmission owners to facilitate and optimize sales from these assets.

199. Ms. Bowman asserts that the transactions conducted with CERS were back-to-back (B2B) transactions. In a B2B transaction, Coral would buy power in the market and resell that specific purchase to CERS at the same location. To minimize risk, these transactions were conducted almost simultaneously.

200. Ms. Bowman states that the Coral credit department would conduct a financial risk assessment for each counterparty. The credit department would then set a credit limit based on the company's financial health. The credit limit would be for the company's entire business with Coral across the United States and include both power and gas transactions. Ms. Bowman states that the trade desk would try to optimize each party's line of credit by evaluating whether the counterparty could engage in a particular transaction based on its current credit limit. Ms. Bowman notes that Coral traders would often ask the credit department to reevaluate companies to increase a party's line of credit. Ms. Bowman further states that as prices get higher, a company's line of credit would be used up faster. Ms. Bowman further notes that Coral consistently applied its credit limits to all counterparties, including CERS.

201. With respect to establishing CERS's credit limit, Ms. Bowman notes that there were two unique aspects to CERS: (1) the source of CERS's funding and (2) the large balances CERS carried required more frequent evaluation. Ms. Bowman states that these

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[142] Enabling agreements are contracts under which parties agree to execute a transaction according to specific terms, with the exception of price, location, and term.

unique credit issues factored into the prices Coral offered CERS. Specifically, Coral would impose a "risk premium" on counterparties based on the amount of credit that was currently utilized and the anticipated future market conditions. Part of this process included examining how other parties in the market were treating the counterparty. Ms. Bowman next explains that Coral viewed CERS, as a counterparty, and California, as a market, to be particularly high risk. Ms. Bowman notes that when CERS entered the market, it had no financial or market history to determine creditworthiness.[143]

202. Further, Ms. Bowman notes that the legislation creating CERS did not alleviate all credit concerns. Ms. Bowman states that the legislation specifically refused to place the state's full faith and credit behinds CERS's energy purchases. Moreover, there was no guarantee how long CERS would continue to be funded.

203. Ms. Bowman also notes that there were significant regulatory risks at the time. Ms. Bowman states that parties had already begun filing complaints with FERC and prices may be altered by the Commission. Additionally, the CPUC required PG&E and SoCal Edison to cooperate in its efforts to obtain refunds on sales to the CalPX, ISO, and CERS. The California Legislature was also considering a bill on windfall profits from energy suppliers. Further, Ms. Bowman states that Coral was concerned that CERS was going to use its statutory authority to declare prices unreasonable and refuse to pay with funds that had already been allocated.

204. Because of these risks, Ms. Bowman states that Coral only agreed to do business with CERS under very tight credit constraints and with high risk premiums.[144] Additionally, Ms. Bowman notes that at times, Coral refused to sell to CERS because of risk of non-payment. Ms. Bowman states that the problems were further exacerbated by CERS's refusal to provide accelerated payment or letters of credit because Coral was such as small supplier to CERS. Ms. Bowman asserts that CERS often refused to purchase from Coral because the risk premium charged. Ms. Bowman notes that Coral sold to CERS in only approximately twenty-five percent of the hours during the CERS Period.

205. Next, Ms. Bowman responds to Mr. Taylor's allegation that Coral raised its margin (risk premium) when increasing CERS's credit limit. Ms. Bowman states that Coral used a combination of credit limits and risk premiums to minimize risk. Therefore,

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[143] Ms. Bowman notes that when CERS entered the market, Coral only knew that CERS was taking over purchasing due to the insolvency of CAISO and CalPX.

[144] Ms. Bowman states that the credit limit was between $20 and $50 million and the risk premium was between $50 and $175 per MWh.

any increase in CERS's credit limit would generally require an increase in the risk premium. Ms. Bowman notes that Coral "fined tuned" these measures throughout the CERS Period based on the risk associated with the sales.

206. Ms. Bowman also responds to Mr. Taylor's allegation that Coral exercised market power by withholding energy in the day-ahead market and selling it in real-time at higher prices. Ms. Bowman states that because CERS had such a great credit risk, Coral did not want to purchase energy in advance of any sale. Therefore, Ms. Bowman states that the transactions with CERS were back-to-back (B2B) transactions at COB.[145] Additionally, Ms. Bowman states that CERS's demand appeared more in the real-time market. Ms. Bowman asserts that Coral never misrepresented to CERS the source of the power.

207. Ms. Bowman states that Mr. Taylor wrongly connects the "term strategies" document with the Master Service Agreement (MSA) between Coral and the City of Glendale. Ms. Bowman states that the "term strategies" document is just a draft, brainstorming document that Coral discussed with Glendale. Ms. Bowman notes that the document was never formalized into an agreement. Ms. Bowman also notes that the MSA did not require Coral to act as the scheduling coordinator for Glendale's transactions. Rather, Coral initiated some transactions for Glendale and Glendale initiated others on its own.

208. With respect to the margins Coral received on its B2B transactions, Ms. Bowman states that these margins reflect the risk premium charged by Coral. Additionally, the prices were reflective of the market conditions in the Pacific Northwest and the prices other sellers were charging CERS.

### 2. Mr. Jeffrey Tranen[146]

209. Mr. Tranen is an expert witness for Coral. Mr. Tranen's testimony responds to allegations made by the California Parties.[147]

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[145] This is in contrast to Mr. Taylor and Dr. Fox-Penner's statement that Coral made sales to CERS from a portfolio of purchased energy.

[146] Ex. SNA-9.

[147] Mr. Tranen's testimony also discusses the California Parties' allegation that Coral sold non-firm energy as firm. However, this allegation was subsequently withdrawn.

210. First, Mr. Tranen responds to Mr. Taylor's allegation that Coral engaged in False Exports. Mr. Tranen argues that Mr. Taylor failed to show a connection between City of Glendale (Glendale)[148] and Coral's exports and Coral's sales to CERS.[149] Mr. Tranen states that Mr. Taylor simply assumes a connection between the transactions if the import and export occurred in the same hour. Mr. Tranen notes that at deposition, Mr. Taylor admitted that his screen does not track the actual flow of electrons. Moreover, Mr. Tranen states that Mr. Taylor admitted that there was no contractual linkage between transactions because energy trading companies purchased a portfolio of energy products. Mr. Tranen states that although other Respondents may have used a portfolio of energy products, Coral's sales to CERS were all B2B transactions at COB. Mr. Tranen states that this fact demonstrates that the sales to CERS were not exported out of the CAISO.

211. Mr. Tranen states that Mr. Taylor admitted that the documentary evidence (Coral internal emails) does not relate to specific exports from the CAISO and sales to CERS. Mr. Tranen notes that Ms. Bowman's testimony demonstrates that the emails do not show any intent on Coral to link exports from the CAISO to sales to CERS.

212. Mr. Tranen states that there was no connection between Coral and Glendale exports from SP-15 and sales to CERS in the Pacific Northwest. Mr. Tranen avers that the B2B sales to CERS at COB were completely independent of any export transactions, as confirmed by Coral's transaction data. Mr. Tranen notes that the transaction data demonstrate that for seventeen hours of alleged False Export, there was no final hour-ahead export from either Coral or Glendale. Additionally, in 227 of the 256 hours, the "export" transaction identified by Mr. Taylor was part of a block transaction of many hours. Mr. Tranen argues that he would not expect any linkage between a multi-hour export transaction and a single-hour sale to CERS. Mr. Tranen also states that during seventy-two hours, there was hour-ahead south to north congestion on Path 15, which Mr. Taylor admits should be eliminated from the screening.

213. Moreover, Mr. Tranen states that Mr. Taylor wrongly included hours in which Glendale was the exporter because of the MSA. As Ms. Bowman notes in her testimony, Mr. Tranen states that Coral did not manage all of Glendale's exports from the ISO. Mr. Tranen states that the California Parties did not provide any evidence that Coral was associated with any of the Glendale exports.

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[148] Mr. Taylor assigns exports made by Glendale to Coral because of the MSA between the two parties.

[149] With respect to Mr. Taylor's multi-party False Export claims, Mr. Tranen contends that of the nineteen allegations, twelve contained no export at all.

214. Mr. Tranen further states that both Coral's trading records and the CAISO's records demonstrate that Coral and/or Glendale exports were never the source of energy for sales to CERS. Mr. Tranen avers that in eighteen of nineteen alleged multi-party False Exports the source of power was Glendale power at Meade. For the remaining hour, the source was Glendale power at Mid-C. As stated above, in twelve of the nineteen hours, there was not any export of power from the CAISO by either Glendale or Coral. Mr. Tranen states that in the six remaining hours, the exports were made by Glendale as part of a 32-hour block of power. For the final hour, which was scheduled by Glendale, the amount of power does not match the volume of sale by Glendale to Portland General Electric at NOB.

215. Mr. Tranen next notes that Mr. Taylor does not allege that the transactions between Coral and CERS violated the WSPP tariff, the tariff under which all sales were made. Rather, Mr. Taylor alleges that the False Exports violated the ISO Market Monitoring and Information Protocol (MMIP), other CAISO tariff provisions, and Coral's market-based rate authority. With respect to the MMIP, Mr. Tranen contends that Mr. Taylor provided no evidence that a False Export resulted in Coral exercising market power. Nor did Mr. Taylor show that Coral was withholding any generation capacity. Mr. Tranen notes that Coral was a marketer and had no obligation to sell energy to CERS. Similarly, Mr. Tranen argues that Mr. Taylor provided no evidence of wrongful conduct by Coral in scheduling the exports.

216. With respect to violations of Coral's market-based rate authority, Mr. Taylor argues that Coral violated this authority by misrepresenting the source of the power. Mr. Tranen asserts that Coral told CERS traders the source of the power any time CERS inquired. Moreover, as stated above, there was no linkage between the exports of energy and sales to CERS. Lastly, Mr. Tranen states that Coral's sales to CERS had no adverse reliability or economic impact. Mr. Tranen notes that this allegation is based on an assumption that the exports and sales to CERS were linked, which they were not.

217. Next, Mr. Tranen addresses Mr. Taylor's allegations that Coral (1) shifted energy from day-ahead or hour-ahead to real-time as part of a False Export strategy and (2) chose to wait to make sales to CERS until real-time even though Coral had a portfolio of energy that it could have sold in the day-ahead or hour-ahead markets.

218. Mr. Tranen first notes that Coral did not have a portfolio of energy products to sell to CERS. Rather, as discussed above, all of Coral's sales to CERS were B2B transactions. Mr. Tranen also notes that Coral did not engage in any False Export strategy in order to withhold supplies from CERS. Mr. Tranen states that Coral was under no obligation to sell energy to CERS and notes that Mr. Taylor admitted that those firms that chose not to sell to CERS were not "withholding" energy.

219. Mr. Tranen contends that Coral's market activities actually benefited CERS because Coral provided CERS energy when it was needed. Mr. Tranen notes that forty

percent of the energy supplied by Coral to CERS came from firms that refused to deal with CERS.

220. Next, Mr. Tranen contends that Dr. Fox-Penner's price discrimination analysis is flawed. Mr. Tranen asserts that Dr. Fox-Penner was unaware that Coral engaged in B2B transactions and just assumed that all sellers sold energy to CERS from a portfolio of products. Therefore, Mr. Tranen concludes that it would be inappropriate to use an average "portfolio" price when comparing sales to CERS because there was a specific product at a specific price that was first bought and then resold to CERS.

221. Mr. Tranen also argues that Dr. Fox-Penner wrongly used prices at different locations to compare to sales to CERS at COB. Mr. Tranen acknowledges that Dr. Fox-Penner adjusts the price to account for transmission costs, but notes that Dr. Fox-Penner failed to investigate whether the transmission was even available. Mr. Tranen notes that when no transmission is available between two locations, the price difference between locations can be substantially larger than the cost of transmission.

222. Moreover, Mr. Tranen states that Dr. Fox-Penner wrongly used an average price paid by all non-CERS buyers at COB when there was no matching transaction. Mr. Tranen contends that this is not an accurate comparison because Dr. Fox-Penner is not using only Coral sales to compare and because the data used by Dr. Fox-Penner includes both day-of and day-ahead pricing. Moreover, Mr. Tranen contends that Dr. Fox-Penner's thresholds for finding price discrimination are arbitrary.

223. Using Coral's data, Mr. Tranen calculated the "mark-up" associated with each B2B transaction. Assuming that the entire mark-up is the CERS Premium, Mr. Tranen states that Dr. Fox-Penner overstates the premium by almost a factor of two. Mr. Tranen contends that the premium charged to CERS was justified due to the risks associated with selling to CERS.

224. Mr. Tranen also notes that Dr. Fox-Penner did not even consider the credit risk CERS presented. Mr. Tranen states that Dr. Fox-Penner's $1/MWh "risk adder" drastically understates the credit risk of CERS. Mr. Tranen asserts that an after-the-fact assessment of CERS's credit does not accurately describe how companies perceived the risk at the time and that many sellers refused to make any sales to CERS because of credit risk.

225. Mr. Tranen notes that two ways of dealing with credit risk are (1) imposing lower credit limits and (2) increasing the price through a risk premium. Mr. Tranen notes that Coral was not a major provider to CERS and received no special payment terms or letter of credit. Mr. Tranen argues that in light of the circumstances, the risk perceived by Coral was justified.

226. Mr. Tranen also addresses Mr. Taylor's allegation that Coral charged CERS excessive prices based on unfair negotiation and unequal bargaining power. Mr. Tranen first notes that Mr. Taylor provided no methodology, and admitted that none existed, for determining what constitutes an excessive price. However, Mr. Tranen states that at deposition, Mr. Taylor admitted that he used the *Power Markets Week* publication of day-ahead prices at COB and Mid-C plus $75/MWh as a comparison.

227. Mr. Tranen argues that Mr. Taylor's comparison is not valid. First, Mr. Tranen notes that Mr. Taylor did not even reveal this comparison until his deposition, after the initial testimony was filed. Second, Mr. Tranen contends that Mr. Taylor's threshold is arbitrary. Mr. Tranen states that Mr. Taylor relies on Coral emails regarding maintaining price above a certain margin and states that "suppliers involved in withholding and manipulation games are trying to maintain their margins above $75/MWh." As stated above, Mr. Tranen notes that Coral engaged in no manipulative activity, including withholding power. Mr. Tranen further asserts that Coral's attempt to keep prices above a certain level reflected the risk premium associated with CERS. Third, Mr. Tranen avers that the *Power Markets Week* prices may not be accurate because the prices are "assessments" and not "weighted averages."

228. With respect to allegations that Coral exercised market power in its sales to CERS, Mr. Tranen contends that there is no basis to allege that Coral exercised market power and that Dr. Reynolds admitted that he did not even examine Coral specifically. Mr. Tranen states that Dr. Reynolds merely stated that high prices are consistent with the exercise of market power. Mr. Tranen notes that there are other explanations for the high prices Coral charged to CERS, such as CERS bought larger volumes on peak when prices were higher.

229. Mr. Tranen states that Coral was not a major supplier of spot energy to CERS. Coral ranked just twenty-third overall and ninth in the Pacific Northwest based on volume sold to CERS. Moreover, less than one percent of Coral's sales to CERS were over the 500 MW threshold for large sellers.

230. With respect to Mr. Taylor's claim of unequal bargaining power, Mr. Tranen states that Mr. Taylor admitted that unequal bargaining power alone would be insufficient to abrogate the contracts. Additionally, Mr. Tranen asserts that Mr. Taylor conducted no contract specific analysis regarding the parties' bargaining power. Mr. Tranen further notes that CERS had access to CAISO information that other parties did not and thus, had a competitive advantage in negotiations. Mr. Tranen also notes that CERS certified that all its transactions were reasonable based on the circumstances that existed at the time.

231. Lastly, Mr. Tranen analyzes Mr. Taylor's contract by contract review. First, Mr. Tranen notes that Mr. Taylor does not identify all of Coral's contracts with CERS. Mr. Tranen also states that it is unclear why a particular document is relevant to Mr. Taylor's analysis and that Mr. Taylor provides no explanation of assigning evidence

to a particular contract. Mr. Tranen further states that Mr. Taylor admitted that his 1(A) and 1(B) determinations are not the result of a repeatable methodology. Mr. Tranen also argues that Mr. Taylor failed to establish a relationship between unlawful activity by Coral and a particular sale to CERS.

### F. Avista Corporation d/b/a Avista Utilities Answering Testimony for the Section 206 Claims

232. Avista Utilities' Answering Testimony responds to claims asserted by the California Parties and the City of Seattle. Because Avista Utilities and the California Parties have settled all outstanding claims, the testimony related to those claims is not summarized below. Avista Utilities presented the testimony and exhibits of two witnesses.

#### 1. Ms. Kimberly Mattern[150]

233. Ms. Mattern is currently the Manager for Real-Time and Preschedule at Avista Utilities. During the relevant period, Ms. Mattern was a preschedule trader for Avista Utilities. Ms. Mattern's testimony provides background information regarding Avista Utilities and its operations during the relevant period and responds to the City of Seattle.

234. Ms. Mattern states that Avista Utilities is a state-regulated, load-serving utility serving customers in eastern Washington, Northern Idaho, and Oregon. Avista Utilities owns a mix of hydroelectric and thermal generation, as well as transmission and distribution facilities. Ms. Mattern states that Avista Utilities' power sales activity is ancillary to its primary mission of delivering energy to its retail customers.

235. During the relevant period, Avista Utilities participated in the power markets to supplement the generation it owns and to sell excess power in the wholesale market.[151] Ms. Mattern notes that because load and resource conditions change, Avista Utilities often bought and sold energy in all markets, including hour-ahead and real-time. Ms. Mattern states that Avista Utilities does not distinguish between power purchased and power it generates. Avista Utilities would arrange for transmission back to it for any purchases and this total amount of energy would be included in its total system resources. Therefore, Ms. Mattern asserts that there was no attempt to link a purchase with a subsequent sale.

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[150] Ex. AVI-1.

[151] Avista Utilities received market-based rate authority for these transactions.

236. Next, Ms. Mattern addresses claims made by the City of Seattle. Ms. Mattern first notes that Seattle did not specifically allege any wrongdoing against Avista Utilities, nor did Seattle reference any bilateral trades between Avista Utilities and Seattle. Therefore, Ms. Mattern concludes that Seattle failed to meet the requirements of the Order on Remand, which mandated that claimants make allegations regarding specific contracts.

237. Ms. Mattern states that during the relevant period, Avista Utilities transacted with Seattle in the buying and selling of spot market power.[152] Based on Avista Utilities' records, Ms. Mattern states that Avista Utilities sold to Seattle 10,241 MWh of sport market power for $1,921,400. Avista Utilities also bought 1,305 MWh of spot market power for $301,300.

238. Ms. Mattern contends that Seattle knowingly accepted the financial risk of relying on spot-market power during the relevant period. Ms. Mattern states that Seattle's heavy reliance on spot market power during a time when prices were volatile and high was the result of their own resource planning and risk management decisions. Moreover, Ms. Mattern argues that by supplying power to the market, Avista Utilities benefited Seattle's ratepayers.

239. Ms. Mattern also notes that the average price of spot sales from Seattle was actually higher than the spot sales to Seattle ($187.62/MWh versus $230.88/MWh). Ms. Mattern states that this is a clear indication that Avista Utilities' sales to Seattle were not unfairly high.

240. Lastly, Ms. Mattern discusses the prior investigations into Avista Utilities' market conduct. Ms. Mattern states that in 2002, Commission Staff investigated Avista Utilities in Docket No. EL02-115, culminating in a settlement agreement which concluded that there was no evidence Avista Utilities and Avista Energy engaged in improper trading strategies or manipulated the Western energy markets.

### 2. Mr. Lloyd Reed[153]

241. Mr. Reed's testimony only concerned claims asserted by the California Parties against Avista Utilities.

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[152] Ms. Mattern defines spot market power as power sales with a duration of twenty-four hours or less. Ms. Mattern notes that Avista Utilities and Seattle also contracted for longer term transactions.

[153] Ex. AVI-63.

### G. Avista Energy, Inc. Answering Testimony for the Section 206 Claims

242. Avista Energy's Answering Testimony responds to claims asserted by the California Parties and the City of Seattle. Because Avista Energy and the California Parties have settled all outstanding claims, the testimony related to those claims is not summarized below. Avista Energy presented the testimony and exhibits of one witnesses, Mr. Lloyd C. Reed.[154] Mr. Reed notes that during the relevant period, Avista Energy was a marketing and trading company and did not own any generation assets.

243. First, Mr. Reed responds to the direct testimony submitted by Seattle. Mr. Reed asserts that Seattle made no specific allegations against Avista Energy and failed to identify any specific transactions between Avista Energy and Seattle.

244. Based on data contained in Avista Energy's database, Mr. Reed states that Avista Energy made 16,530 MWh of spot sales to Seattle in the Pacific Northwest market during the relevant period.[155] Mr. Reed states that these sales occurred in 322 hours at prices between $20/MWh and $600/MWh.[156] The weighted average price was $250.12/MWh. Mr. Reed notes that in Seattle's September 2012 Statement of Claims, Seattle included month-long and quarter-long terms sales.

245. Mr. Reed asserts that Mr. Hanser made no allegations against Avista Energy in his direct testimony. Mr. Reed contends that Mr. Hanser's testimony primarily consists of generalized accusations of manipulative activity by unnamed sellers. Mr. Reed states that Mr. Hanser never uses the term Respondents in his testimony nor alleges any wrongdoing by Avista Energy. Further, Mr. Reed notes that although Mr. Hanser attached previously filed testimony and exhibits of experts, Mr. Hanser never makes any specific allegation against Avista Energy or any other Respondent.[157] Mr. Reed also states that much of the previously filed testimony deals with parties that are not Respondents in this case or with events that occurred outside the relevant period.

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[154] Ex. AVE-1.

[155] Mr. Reed defines spot sales as a sale for a period of twenty-four hours or less made the day of or the day before delivery.

[156] Mr. Reed states that based on Seattle's Statement of Claims, it would be seeking refunds for all transactions, including those at $20/MWh.

[157] Mr. Reed also provided the answering testimony to the allegations made by other witnesses in this and other prior proceedings.

246. Mr. Reed states that Mr. Hanser mentions Avista Energy only once, when describing a long-term contract between Avista Energy and Chelan County Public Utility District. Even in this one mention, Mr. Reed states that Mr. Hanser mischaracterized the agreement as a parking arrangement. Mr. Reed states that a parking arrangement is only possible if Avista Energy conveyed physical control rights, which it did not. Regardless, Mr. Reed contends that Mr. Hanser did not even attempt to link the Chelan contract with any spot market sale with Seattle. In fact, Mr. Reed states that Mr. Hanser failed to link any specific unlawful conduct by Avista Energy to the formation of a specific contract with Seattle.

247. Next, Mr. Reed notes that the transactional data provided by Mr. Hanser is the quarterly WSPP transaction reports, but these reports cover a time frame longer than the relevant period and includes sales that were not "spot sales." Mr. Reed further avers that the WSPP reports do not contain specific day and hour information. Therefore, Mr. Reed states that it is not possible to use the information submitted by Seattle to determine which spot sales were made during the relevant period.

248. Mr. Reed notes that Seattle also made sales to Avista Energy during the relevant period. Mr. Reed states that Avista Energy made 5,510 MWh of spot purchases from Seattle during the relevant period at prices between $50/MWh and $325/MWh.[158] The weighted average price of the sales by Seattle to Avista Energy was $184.46/MWh. Mr. Reed asserts that Seattle's sales to Avista Energy were at prices comparable to the sales by Avista Energy to Seattle.

249. Next, Mr. Reed responds to Mr. Hanser's cointegration analysis. Mr. Reed states that this is the type of analysis that the Commission specifically excluded from the hearing. Mr. Reed notes that no specific spot market purchase by Seattle is incorporated in the analysis and that Mr. Hanser failed to show how the prices he used compared to the prices actually incurred by Seattle from Avista Energy.

250. Mr. Reed also argues that the analysis contains several flaws that make its findings unreliable: (1) the analysis is based on monthly term sales at Mid-C, not spot sales from specific sellers; (2) the analysis relies on broker quotes rather than actual sales prices and ignored available evidence that reflects actual spot market sales prices; (3) the broker quotes are only for on-peak hours even though thirty-five percent of Avista Energy's sales to Seattle occurred during off-peak hours; and (4) the analysis used only Mid-C

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[158] Mr. Reed notes that although Mr. Hanser fails to mention that Seattle made sales to Avista Energy, in previously submitted testimony, Seattle witnesses did acknowledge that its sales would be subject to refunds.

pricing even though Avista Energy sold to Seattle at other locations, such as the Seattle City Light system.[159]

### H. PPL Montana, LLC and PPL EnergyPlus, LLC Answering Testimony for the Section 206 Claims

251. PPL's Answering Testimony responds to claims asserted by the City of Seattle. PPL presented the testimony and exhibits of two witnesses.

#### 1. Ms. Rosemarie Spear[160]

252. Ms. Spear is currently the Director of Trading and Marketing for PPL EnergyPlus, LLC. During the relevant period, Ms. Spear Manager, Trading and Operations at PPL EnergyPlus, LLC. Ms. Spear's testimony describes the nature of PPL's trading in the Pacific Northwest during the relevant period and explains why PPL did not engage in unlawful activity.

253. Ms. Spear states that PPL EnergyPlus acted as PPL Montana's agent and made sales on behalf of PPL Montana in the Pacific Northwest market. Ms. Spear notes that PPL EnergyPlus and PPL Montana both received market-based rate authority. Ms. Spear states that during the relevant period, PPL had a full requirements contract with Montana Power, with the primary obligation to meet Montana Power's fluctuating load demands. Ms. Spear states that PPL would buy wholesale energy to both meet Montana Power's load and for later resale. PPL would also sell any excess energy from PPL's own generation.

254. With respect to selling and exporting energy, Ms. Spear notes that PPL had no long-term firm transmission rights to Mid-C. Therefore, the amount of energy that could be sold in the wholesale markets depended on (1) PPL's Generation; (2) Montana Power's Load; and (3) transmission availability. Ms. Spear states that excess power generally occurred during off-peak hours when Montana Power required less energy.

255. Ms. Spear states that potential buyers were known to PPL traders and located throughout the Pacific Northwest and the Rocky Mountain Region. Ms. Spear notes that PPL traders had the discretion on which buyers to reach out to and that there was no

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[159] Mr. Hanser states that all the purchases Seattle is seeking refunds for occurred at Mid-C, but provided no documentary evidence regarding the location of these purchases.

[160] Ex. PPL-1.

systematic method for determining who to sell excess energy to. Ms. Spear avers that traders would consider recent transactions and trading patterns to determine who to contact first.[161] Ms. Spear notes that all of the sales to Seattle were negotiated bilateral agreements pursuant to PPL's market-based rate authority.

256. In determining prices for bilateral sales, Ms. Spear states that the price could be proposed by either party and then negotiated based on market prices and conditions. Ms. Spear notes that real-time price information was not available to traders in advance of negotiating the sales. Price indices were only available after the fact and traders sometimes used previous day or hour pricing in negotiating. Traders would also attempt to survey the market to determine the price.

257. Ms. Spear further notes that PPL did not have the ability to dictate prices in the Pacific Northwest market because there were multiple buyers and sellers, including sellers with far more energy to sell. Ms. Spear asserts that PPL was further limited because of its full requirements contract and lack of firm transmission from generation in Montana to the Pacific Northwest market. Lastly, as a purchaser of energy, Ms. Spear notes that PPL paid similar and sometimes higher prices than the prices received when selling energy.

258. With respect to sales to Seattle, Ms. Spear notes that PPL sold energy to Seattle on the spot market and through three term forward contracts.

259. Next, Ms. Spear avers that Seattle made no specific allegation against PPL regarding violations of market-based rate authority, violations of any tariff, manipulation of the Pacific Northwest market, or exercising market power. Ms. Spear further contends that PPL did not engage in any "Enron-style" market manipulation because such activities do not apply to the Pacific Northwest bilateral agreements and because PPL never bought energy from the CAISO or from sellers within the CAISO control area. Ms. Spear also notes that PPL never received any congestion revenues, sold non-firm energy as firm, or submitted false schedules as part of a manipulation scheme. Lastly, because PPL had a limited amount of energy to sell, Ms. Spear states that it could not have exercised market power in the competitive Pacific Northwest market.

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[161] Ms. Spear states that PPL may have also engaged brokers to find buyers and execute sales.

### 2. Mr. A. Joseph Cavicchi[162]

260. Mr. Cavicchi is an expert witness for PPL. Mr. Cavicchi provides testimony that responds to Mr. Hanser's direct testimony on behalf of the City of Seattle.

261. First, Mr. Cavicchi generally describes the Pacific Northwest market during the relevant period. Mr. Cavicchi states that the Pacific Northwest market is a large regional market where the power is primarily supplied by hydroelectric generation controlled by public power agencies, such as BPA. Mr. Cavicchi states that there is an active and liquid bilateral trading market governed by the WSPP Agreement. Mr. Cavicchi notes that it is reasonable to expect that thousands of megawatts were traded daily.

262. Next, Mr. Cavicchi evaluates whether PPL could have engaged in physical or economic withholding in the Pacific Northwest market during the relevant period. Mr. Cavicchi notes that for a withholding strategy to be effective, the party would have to possess market power.[163] Mr. Cavicchi asserts that PPL was limited in the amount of energy it could sell because of its full requirements contract. Additionally, PPL's lack of firm transmission prevented PPL from physically withholding power because the amount of power it could supply varied depending on the available transmission.

263. With respect to economic withholding, Mr. Cavicchi avers that PPL could not have engaged in the practice because PPL was only selling excess energy at market prices. PPL was not bidding into an organized market and affecting prices or acquiring energy for later resale. Moreover, Mr. Cavicchi states that even if PPL were withholding energy, there were numerous sellers that would have made this strategy ineffective.

264. Next, Mr. Cavicchi states that the transactional data submitted by Seattle confirms that PPL was only responding to prevailing market prices. Mr. Cavicchi notes that PPL and Seattle were selling energy at comparable prices. Additionally, in 696 instances, Seattle sold energy at a price higher than the price it bought energy from PPL. Mr. Cavicchi argues that Seattle was acting in a similar fashion as PPL, buying and selling energy to maximize its profits and resources.

265. Mr. Cavicchi also contends that PPL did not engage in "Enron-style" manipulative activities. Mr. Cavicchi first notes that these types of activities have been associated with the organized CAISO and CalPX markets, and in fact, require an organized market.

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[162] Ex. PPL-4.

[163] Mr. Cavicchi notes that during the relevant period, PPL had market-based rate authority, indicating that it lacked market power.

Mr. Cavicchi asserts that Seattle has made no claims that PPL used these activities in an effort to effect prices in the Pacific Northwest market, and therefore, have no relevance to this case. Lastly, Mr. Cavicchi notes that PPL has never been alleged to have engaged in these strategies.

266. Next, Mr. Cavicchi argues that Seattle was an active participant in the Pacific Northwest market and could have mitigated its market exposure. Mr. Cavicchi avers that Seattle was a sophisticated market participant and should have known its risk in relying on the spot market. For example, Mr. Cavicchi notes Seattle sold its own generation resources, the Centralia facility, despite forecasts that hydroelectric power would be lower in 2001. Moreover, Mr. Cavicchi states that in 2000, Seattle made forward purchases to hedge against volatility in the spot market, but did not do so in 2001. Mr. Cavicchi further notes that the Commission has recognized that Pacific Northwest purchasers had a variety of options to hedge and balance energy portfolios.

267. Lastly, Mr. Cavicchi asserts that Seattle's transactional data inappropriately includes three PPL transactions that did not occur on the spot market.[164] For example, certain transactions are listed for March 12, 2001, even though delivery did not occur until later in March or April 2001. Mr. Cavicchi notes that these longer term forward sales account for more than twenty-five percent of the total revenue associated with sales to Seattle during the relevant period.

### I. El Paso Power Marketing Company, LLC Answering Testimony for the Section 206 Claims

268. El Paso's Answering Testimony responds to claims asserted by the City of Seattle. El Paso presented the testimony and exhibits of one witnesses, Mr. Dennis Price.[165] Mr. Price is currently Vice President at EP Energy LLC and responsible for commodity trading and marketing. In 2001, Mr. Price became Managing Director of Trading and Risk Management for El Paso Global Networks.

269. Mr. Price first describes El Paso's role in the Pacific Northwest market during the relevant period. Mr. Price states that El Paso held modest interests in generation facilities

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[164] Mr. Cavicchi states that spot market sales are either day-ahead or shorter. Mr. Cavicchi states that this definition is consistent with the definition used in all organized markets in the United States.

[165] Ex. EP-1.

throughout the United States, but none in the Pacific Northwest.[166] Rather, El Paso was a marketer of purchased power. Mr. Price states that El Paso did not purchase power for its own use or for service of any native load. Mr. Price also notes that El Paso did not own any interest in any electric transmission facilities.

270. Mr. Price also states that marketers generally bought energy on a "portfolio basis" and sold that energy to other entities. Mr. Price asserts that a marketer's success depends on the entity's ability to manage and assume risk in the long and short term markets. Mr. Price states that marketers benefit the overall market by increasing the number of available options to buyers and creating a more "liquid" market.

271. Mr. Price states that El Paso's transactions in the Pacific Northwest market were done pursuant to its market-based rate authority. Mr. Price further notes that between the time El Paso was granting market-based rate authority and the relevant period, no changes occurred that would have altered the Commission's conclusion that El Paso could not exercise market power. Mr. Price further asserts that El Paso did not engage in any activities in violation of its market-based rate tariff and the conditions imposed on El Paso by the Commission.

272. Mr. Price defines spot market transactions for the purpose of this proceeding as any transaction with a duration of twenty-four hours or less that is prescheduled no more than twenty-four hours in advance of delivery.[167] Mr. Price states that this definition is consistent with common commercial practices and the Commission's definition. Mr. Price notes that spot market transactions allow entities to immediately balance resources to actual obligations, but generally should not be used to address predictable events.

273. Next, Mr. Price describes the El Paso's transactions in the Pacific Northwest during the relevant period. Mr. Price states that El Paso conducted its buy and sell transactions with a variety of participants through bilateral agreements. Mr. Price notes that marketing and trading activity was "vibrant and robust" with multiple parties buying and selling energy. Mr. Price avers that Seattle had many options, stating that Seattle's transaction template indicates that Seattle transacted with over sixty different entities during the relevant period. Moreover, Mr. Price states that Seattle was also a wholesale power seller during the relevant period and often sold energy at a price higher than what it paid.

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[166] Mr. Price notes that during the relevant period, El Paso made no sales in the Pacific Northwest market for generation it had an interest in.

[167] Mr. Price notes that there are exceptions for weekends and holidays.

274. Mr. Price asserts that El Paso could not set the "market price" for transactions in the Pacific Northwest market because there were many buyers and sellers of energy. Mr. Price notes that El Paso was often "undercut" by another seller when negotiating with buyers.

275. With respect to Mr. Hanser's allegation that Pacific Northwest prices were affected by illegal activity in California, Mr. Price states that he was not aware that the prices were affected at the time. Mr. Price further asserts that there were no allegations of wrongdoing by El Paso at the time and that Seattle has failed to provide any evidence of wrongdoing in this proceeding.

276. Lastly, Mr. Price argues that refunds should not be awarded in this proceeding because parties freely contracted with each other in a competitive market and requiring refunds will increase prices in the future because sellers will have to factor in the risk of a future refund.

### J. Cargill Power Markets, LLC Answering Testimony for the Section 206 Claims

277. Cargill's Answering Testimony responds to claims asserted by the City of Seattle. Cargill presented the testimony and exhibits of one witnesses, Mr. David Toole.[168] Mr. Toole is currently Trading Manager for Cargill.

278. Mr. Toole states that Cargill is a power marketer that did not own any generation or transmission facilities. Mr. Toole states that the Pacific Northwest spot market generally operated through bilateral sales under the terms and conditions of the WSPP Agreement.[169] Mr. Toole notes that this is different from the California spot market at the time, which had a centralized power market and utilized a market clearing price.

279. Mr. Toole states that Mr. Hanser alleges the following unlawful market activities by sellers: (1) Sempra, PacifiCorp, and an unnamed California generator engaged in unlawful Ricochet transactions and (2) Idaho Power Company and BPA, through energy exchange transactions, submitted bid price spikes that resulted in substantial overcharging for energy sold into California. Mr. Toole notes that Mr. Hanser made no allegations against Cargill, and Cargill did not engage in any unlawful market activities.

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[168] Ex. CPM-1.

[169] As with other Respondent witnesses, Mr. Toole defines the spot market as transactions lasting twenty-four hours or less and entered into the day prior or the day of delivery.

Moreover, Mr. Toole states that Mr. Hanser does not make any specific reference to Cargill in his initial testimony.

280. Mr. Toole contends that Mr. Hanser improperly relies on testimony in a separate proceeding that occurred almost ten years ago. Mr. Toole states that this was improper because (1) the prior testimony concerns sales into California rather than the Pacific Northwest market and (2) Mr. Hanser failed to verify the factual accuracy or reliability of the testimony.

281. Mr. Toole argues that Mr. Hanser never discusses any connection between a particular seller's activity and specific contract negotiations in the Pacific Northwest spot market. Rather, Mr. Toole asserts that Mr. Hanser only attempts to connect the market dysfunction in California to the prices paid by Seattle in the Pacific Northwest. Mr. Toole argues that this cointegration analysis is flawed because (1) it does not include transaction-specific information; (2) it fails to address Seattle's own role in negotiating contracts; and (3) it uses forward contract prices rather than spot market prices.

282. Mr. Toole avers that Seattle had the opportunity to negotiate lower prices in its spot market transactions and was not forced to enter into any transaction. Mr. Toole contends that Mr. Hanser's failure to address Seattle's role in the transactions is a fatal flaw to his analysis. Mr. Toole further states that in transactions with Seattle, Cargill was often a "price taker" and Seattle would set the prices of the transaction.

283. Mr. Toole analyzes the transaction data and refund amounts claimed by Seattle. Mr. Toole notes that the total amount of spot market sales to Seattle from Cargill was $7,716,006 based on Cargill's data.[170]

284. Lastly, Mr. Toole addresses Seattle's resource planning strategy leading up to and during the relevant period. Mr. Toole notes that Seattle relied on purchases in the wholesale market to satisfy its load obligations. Mr. Toole states that Seattle admitted that it plans to make up losses in years where its hydroelectric resources are limited with revenues from years where its resources are above average. However, Mr. Toole notes that Seattle sold one of its five hydroelectric production facilities in 2000, resulting in Seattle having fewer resources than were previously available. The remaining four facilities could provide only sixty-three percent of Seattle's total energy needs in 2000.

285. Mr. Toole states that Seattle's strategy of relying on wholesale markets during "short water" years is associated with the following business risk. If Seattle did not properly hedge against its load requirements and its production was less than anticipated,

[170] Seattle's data indicates a total of $7,128,572.

Seattle would be required to purchase spot market energy to meet demand. Mr. Toole states that this is what happened to Seattle in 2000 and 2001. Mr. Toole states that Seattle production decreased dramatically from 965.1 MW in 1999 to 760.8 MW in 2000 to just 449.9 MW in 2001. Mr. Toole avers that this decrease occurred because (1) Seattle sold a 78.7 MW facility and (2) Seattle experienced low water years in 2000 and 2001 due to weather conditions.[171]

286. Mr. Toole argues that Seattle could have anticipated and mitigated the risks associated with its resource strategy. Mr. Toole notes that Seattle was well aware of its reliance on hydroelectric sources and willingly accepted the risks associated with its resource plan, which relied heavily on wholesale markets in low water years. Mr. Toole further notes that following 2001, Seattle subsequently changed its resource plan by purchasing more energy from BPA.

### K. Public Service Company of Colorado Answering Testimony for the Section 206 Claims

287. PSCo's Answering Testimony responds to claims asserted by the City of Seattle. PSCo presented the testimony and exhibits of one witnesses, Mr. Thomas A. Imbler.[172] Mr. Imbler is currently Vice President, Commercial Operations at Xcel Energy Inc., the parent company of PSCo. During the relevant period, Mr. Imbler was responsible for electric trading and generation dispatch for PSCo and Southwestern Public Service Company.

288. Mr. Imbler states that PSCo, an investor owned utility that operates in portions of Colorado, made sales throughout the Western Interconnect to a variety of purchasers, including Seattle, using energy sourced from its own system and through purchases PSCo made from other utilities. Mr. Imbler states that during the relevant period, PSCo had 5,296 megawatts of available capacity.[173] Mr. Imbler notes that PSCo added new resources prior to the relevant period as part of its planning reserve requirements, which indicated higher than expected load growth. Thus, PSCo had additional capacity to sell during the 2000-2001 Period.[174] Mr. Imbler further states that PSCo considered

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[171] Mr. Toole notes that Seattle's water level in 2001 was the lowest in sixty years.

[172] Ex. PSC-1.

[173] Sixty-two percent of the capacity was owned directly by PSCo and thirty-eight percent was acquired through long-term purchases.

[174] With respect to any profits obtained through short-term sales, Mr. Imbler states that PSCo has had a profit sharing arrangement with retail customers since 2000.

applicable emission limits when making off-system sales. Mr. Imbler notes that PSCo could not simply pay a financial penalty for exceeding twelve-month rolling limits, but had to manage its resources to stay within specified limits.

289. Mr. Imbler next states that PSCo is relatively isolated, on the edge of the WSCC, and little transmission was available to make sales to other markets within the WSCC. Additionally, the transmission that was available was generally non-firm.

290. Mr. Imbler also provides a general overview of the Pacific Northwest spot market.[175] Like other witnesses, Mr. Imbler states that the spot market operated through bilateral sales under the terms and conditions of the WSPP Agreement. Mr. Imbler notes that this is different from the California spot market at the time, which had a centralized power exchange and utilized a market clearing price.

291. Mr. Imbler states that Mr. Hanser alleges the following unlawful market activities by sellers: (1) Sempra, PacifiCorp, and an unnamed California generator engaged in unlawful Ricochet transactions and (2) Idaho Power Company and BPA, through energy exchange transactions, submitted bid price spikes that resulted in substantial overcharging for energy sold into California.[176] Mr. Imbler notes that Mr. Hanser made no allegations against PSCo, and PSCo did not engage in any unlawful market activities. Moreover, Mr. Imbler states that Mr. Hanser does not make any specific reference to PSCo in his initial testimony or analyze any specific contracts between Seattle and PSCo.

292. Mr. Imbler argues that Mr. Hanser never discusses any connection between a particular seller's activity and specific contract negotiations in the Pacific Northwest spot market. Rather, Mr. Imbler asserts that Mr. Hanser only attempts to connect the market dysfunction in California to the prices paid by Seattle in the Pacific Northwest. Mr. Imbler argues that this cointegration analysis is flawed because (1) it does not include transaction-specific analysis; (2) it fails to address Seattle's own role in negotiating contracts; and (3) it uses forward contract prices rather than spot market prices.

293. Mr. Imbler avers that Seattle had the opportunity to negotiate lower prices in its spot market transactions and was not forced to enter into any transaction. Mr. Imbler

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[175] Mr. Imbler defines the spot market as transactions that are twenty-four hours or less and entered into the day of or the day prior to delivery.

[176] Mr. Imbler notes that Mr. Hanser relies on testimony in a separate proceeding that occurred almost ten years ago, which concerns sales into California rather than the Pacific Northwest market.

contends that Mr. Hanser's failure to address Seattle's role in the transactions is a fatal flaw to his analysis.

294. Mr. Imbler analyzes the transaction data and refund amounts claimed by Seattle. Mr. Imbler notes that the total amount of sales to Seattle from PSCo was $33,790,802 based on PSCo's data.[177] Mr. Imbler states that based on his definition of spot market, $15,589,274 were spot market transactions.

295. Mr. Imbler also asserts that "bookout" transactions[178] should be excluded from this proceeding. Mr. Imbler states that the Commission has only asserted jurisdiction over transactions that result in the physical delivery of energy, and therefore, "bookouts" do not qualify. Mr. Imbler states that based on Seattle's records, there were $542,588 worth of "bookouts" between PSCo and Seattle.

296. Next, Mr. Imbler makes general arguments opposing refunds in the Pacific Northwest. Mr. Imbler contends that PSCo took a number of system risks when making sales in the Pacific Northwest market during the relevant period and PSCo only undertook those risks because of the prevailing market prices. For example, Mr. Imbler states that PSCo took an aggressive approach in forecasting the amount of surplus energy that it would have available and operated its system accordingly, including running units at maximum capacity.

297. Mr. Imbler notes that notwithstanding the shortages of energy, the Pacific Northwest market was sufficiently competitive to enable purchasers to be selective about the products that they were buying. Therefore, purchasers often set terms and conditions, including requiring energy to be "financially firm."[179] Mr. Imbler contends that the transmission risk of these products was particularly relevant to PSCo because buyers only wanted energy at certain delivery points and PSCo held no firm transmission rights between Colorado and the Pacific Northwest market. Additionally, to get energy from Colorado to the Pacific Northwest market required multiple transmission paths, further

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[177] Seattle's data indicates a total of $33,235,712.

[178] "Bookout" transactions occur when there is no physical delivery of energy because the two parties have multiple buy and sell transactions at the same time. The parties offset the two transactions and only deliver the net amount of energy.

[179] Mr. Imbler describes "financially firm" energy as an energy product that required the seller to pay a financial penalty if the energy was not delivered. Thus, there was an increased risk to the seller if transmission could not be acquired or was cut. Mr. Imbler notes that PSCo had numerous transactions where PSCo had to pay penalties.

complicating the delivery of energy on non-firm transmission. Mr. Imbler states that the reasons PSCo assumed such risks are (1) the market price at the time and (2) PSCo's trading infrastructure, which enabled it to manage the risk.

298. Mr. Imbler contends that this transaction risk distinguishes the Pacific Northwest market from the California market. Because the Pacific Northwest market consisted of bilateral negotiations, parties could assess the risk for themselves and come to agreed-upon prices. In contrast, in California, the price was determined by an auction mechanism and was not known when a seller put in its initial bid.

299. Lastly, Mr. Imbler addresses PSCo's and Seattle's resource planning strategy leading up to and during the relevant period. Mr. Imbler notes that Seattle relied on purchases in the wholesale market to satisfy its load obligations. Mr. Imbler states that Seattle admitted that it plans to make up losses in years where its resources are limited with revenues from years where its resources are above average. However, Mr. Imbler notes that Seattle sold one of its production facilities in 2000, resulting in Seattle having fewer resources than were previously available. Moreover, Mr. Imbler states that in 2000 and 2001, a water shortage caused Seattle's hydroelectric facilities to produce fifty percent of the power it produced in 1999. Therefore, Seattle relied on the wholesale markets even more.[180]

300. Conversely, Mr. Imbler states that in 1999, PSCo began making short and long term[181] energy purchases from Independent Power Providers in order to meet PSCo's increased demand forecast. Mr. Imbler states that PSCo never considered avoiding long-term costs by relying on spot market power.

### L. Constellation Energy Commodities Group, Inc. Answering Testimony for the Section 206 Claims

301. Constellation's Answering Testimony responds to claims asserted by the City of Seattle. Constellation presented the testimony and exhibits of one expert witness, Mr. A. Joseph Cavicchi.[182]

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[180] Mr. Imbler notes that Seattle subsequently changed its resource plan by purchasing more energy for BPA.

[181] Mr. Imbler states that the only long-term solution was having independent producers build new generation, which because of the tight time frame, limited the number of competitors and increased the price.

[182] Ex. CCG-1.

302. Mr. Cavicchi asserts that Mr. Hanser made no specific allegations of wrongdoing by Constellation that affected the prices charged to Seattle. Mr. Cavicchi states that Mr. Hanser only makes general allegations of unlawful activity by sellers in California.[183] Mr. Cavicchi notes that Mr. Hanser does reference testimony in other cases regarding violations of certain reporting requirements, but states that these allegations are not within the scope of this proceeding.

303. Next, Mr. Cavicchi notes that Constellation and Seattle were selling energy at comparable prices. In 291 instances Seattle sold energy at a price higher than the price it bought energy from Constellation. Mr. Cavicchi argues that Seattle was acting in a similar fashion as other participants, buying and selling energy to maximize its profits and resources.

304. Lastly, Mr. Cavicchi states that Seattle's transactional data includes transactions with Constellation that were not on the spot market.[184] Specifically, there were two transactions in January 2001 for energy to be delivered in February. These two transactions account for nearly forty-five percent of the total revenue associated with sales to Seattle.

### M. Pacific Northwest Respondents Answering Testimony for the Section 206 Claims

305. The Pacific Northwest Respondents[185] submitted the answering testimony of Professor William W. Hogan.[186] Professor Hogan's testimony discusses the market fundamentals of the Pacific Northwest during the Western Energy Crisis.

306. Professor Hogan first addresses Dr. Fox-Penner's claim that economic efficiency calls for prices in competitive spot markets to be set at the short-run marginal cost of the

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[183] These general allegations include (1) physical and economic withholding of power; (2) Enron-type games; (3) anomalous bidding practices; and (4) failure to comply with reporting requirements.

[184] Mr. Cavicchi contends that spot market sales are either day-ahead or shorter.

[185] The Pacific Northwest Respondents are Avista Corporation d/b/a Avista Utilities; Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C.; Public Service Company of Colorado; PPL Montana LLC and PPL EnergyPlus LLC; TransCanada Energy Ltd.; and Constellation Energy Commodities Group, Inc.

[186] Ex. PNR-1.

seller. Professor Hogan states that this claim ignores the difference between individual sellers and marginal sellers. Professor Hogan notes that in a competitive market the price is the short-run costs plus the cost of scarcity to meet demand. Additionally, Professor Hogan notes that Dr. Fox-Penner is relying on a perfectly efficient market in his claims. Professor Hogan states that this is not an accurate description of electricity markets because there are a variety of physical, regulatory, and economic factors that make electricity markets in general, and the Pacific Northwest specifically, not perfectly efficient. For example, Professor Hogan notes that energy in the Pacific Northwest spot-market is not sold through a "clearing price" mechanism, but through bilateral contracts.

307. Professor Hogan also notes that scarcity and risk play significant factors in pricing. Professor Hogan states that prices, even in competitive markets, are driven higher in scarcity conditions. Additionally, if there is risk associated with particular sellers, the price can be affected. Professor Hogan notes that this is particularly true in bilateral negotiations with individual parties, where each party assesses the risk differently. Because of the lack of complete information by all parties, Professor Hogan states he would not expect the Pacific Northwest market to act as perfectly efficient.

308. Next, Professor Hogan responds to Dr. Fox-Penner's allegations of price discrimination. Professor Hogan first notes that certain aspects of CERS made the choices available to CERS limited, and therefore, affected pricing. For example, CERS owned no generation assets or transmission rights, limiting CERS to particular locations. Next, Professor Hogan notes that Dr. Fox-Penner uses his own subjective views regarding what premium size is "undue discrimination."

309. Professor Hogan also disagrees with Dr. Fox-Penner's use of the junk bond market to estimate the risk premium associated with CERS. Professor Hogan notes that the junk bond market is based on portfolio diversification, which limits risk. Professor Hogan contends that a more proper comparison would be the risk associated with a debt-ridden country, such as Argentina, which has a high probability of failure. Professor Hogan notes that the ISO, CalPX, and IOU's in California were effectively insolvent at the time and unwilling to pay their bills. Moreover, there was regulatory risk from both FERC and the California government.[187] Therefore, Professor Hogan concludes that it was reasonable for sellers to anticipate that there was significant risk in dealing with CERS and that the "premiums" calculated by Dr. Fox-Penner are consistent with this risk. Professor Hogan further notes that Dr. Fox-Penner only knows in hindsight that the

[187] Professor Hogan notes that this proceeding is an example of the regulatory risk associated with CERS because the California Parties are arguing that the contracts should be abrogated.

perceived risk from sellers was not accurate. However, Professor Hogan contends that the risk associated with CERS must be analyzed based on how market participants viewed CERS at the time. Lastly, Professor Hogan notes that the lack of information during the time also limited market participants' ability to accurately assess the risk associated with CERS.

310. Next, Professor Hogan discusses how opportunity costs affected the price CERS paid for electricity. Professor Hogan notes that sellers will make their pricing decisions based on what they could charge another buyer in other markets. Professor Hogan states that generators also considered maximizing their profits based on the time and market of a sale – selling at one particular time generally means forgoing a sale at some point in the future. Therefore, sellers would sell at certain times or in certain markets to maximize profits.[188] Professor Hogan states that the bilateral negotiations between buyers and sellers were influenced by the sellers' perception of what it could charge at some other time. Professor Hogan states that there is nothing unlawful about arbitraging the inter-temporal price differences and that this tactic is used in many commodity markets. Professor Hogan notes that generation sellers would also consider the price they could receive by providing ancillary services. Professor Hogan states that in tight supply conditions, ancillary services yield high prices. Therefore, this opportunity cost would be reflected in any sale to third parties.[189]

311. Therefore, Professor Hogan disagrees with the California Parties' claim that there is "no economic justification for the prices charged to CERS." Professor Hogan notes that this claim is made in the context that the prices were higher than short-term and long-term marginal costs. However, for the reasons discussed above, Professor Hogan states that even in competitive markets, the price may exceed short-run marginal costs. Additionally, Professor Hogan notes that it is inappropriate to analyze profits for just a 155 day period to determine if a generator's long-run costs are recouped. In order to assess long-run costs, Professor Hogan states a longer period of analysis is required.

312. Professor Hogan states that historically, the prices in energy markets have not been sufficiently high enough to spur investment in new generation. Professor Hogan notes that this problem also occurred in the years leading up to the Western Energy

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[188] Professor Hogan also notes that hydroelectric suppliers try to optimize their facilities in order to sell at the highest prices and buy when prices are lower. This is the opportunity costs associated with hydroelectric facilities.

[189] Appendix I of Professor Hogan's testimony provides a detailed analysis of the relationship between energy and ancillary service prices during shortage conditions.

Crisis. Professor Hogan notes that even the high prices during the energy crisis were not stable enough, high enough, and did not occur long enough to spur investment.

313. Next, Professor Hogan argues that the most important factor that caused the reduction in supply and increase in price during the Western Energy Crisis was the decreased output in hydroelectric generation. Professor Hogan notes that the reduction in generation between June 1999 and June 2000 averaged 6,700 MW, equivalent to six large nuclear power plants. Additionally, Professor Hogan notes that demand for electricity increased in the summer of 2000. Thus, the Western markets were forced to rely on inefficient, high-cost generation.[190] Professor Hogan states that a related factor to operating these inefficient units was the cost for NOx emission permits (and other environmental regulatory issues), which also skyrocketed at the time and led to further increases in electricity prices.[191]

314. Professor Hogan states that the tight balance between supply and demand in the Pacific Northwest market did not begin to ease until early 2001. Then, load-serving entities outside California, mainly BPA, pursued substantial load reduction efforts, reducing load by an estimated 4,000 MW during the summer of 2001. Additionally, California resumed payments to Qualifying Facilities so that they could produce energy again. Professor Hogan contends that these changes in supply and demand (among others), and not FERC's west-wide price cap, instituted on June 19, 2001, ended the energy crisis.

315. Professor Hogan next discusses BPA's load reduction efforts more specifically. Professor Hogan states that BPA instituted buybacks of power at relatively high prices ($280/MWh). Professor Hogan notes that these buyback prices set a floor at which utilities would sell power into California. Professor Hogan also states that the fact that BPA was offering buybacks to reduce load demonstrates the serious limitations facing hydroelectric generators.

316. Professor Hogan also contends that another way to estimate the cost of power is through the cost of blackouts. Professor Hogan asserts that the cost of a blackout estimates the cost consumers are willing to pay for additional energy. Thus, the market price for energy would equal the price paid by the last increment of demand.

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[190] Professor Hogan further notes that this resulted in higher natural gas prices, which magnified the price of electricity. Appendix III of Professor Hogan's testimony provides a detailed analysis of the natural gas markets and electricity prices.

[191] Appendix II of Professor Hogan's testimony provides more detailed information on the cost of NOx emissions.

Professor Hogan notes that Dr. Fox-Penner's own estimate for this cost is clearly above the marginal cost to generators.

317. Professor Hogan also states that Dr. Reynolds has previously estimated the cost of lower supply on purchasers of energy. Professor Hogan notes that Dr. Reynolds conducted his analysis in the context of examining the withholding of power by some sellers. However, Professor Hogan notes that the levels of withholding examined by Dr. Reynolds (1,000 MW or more) were far less than the reduction of hydroelectric resources during the relevant period. Professor Hogan contends that Dr. Reynolds' analysis demonstrates that costs are affected by lack of supply. Lastly, Professor Hogan notes that other organized markets account for the effect of shortages on pricing.

318. Next, Professor Hogan addresses Mr. Hanser's claim that the California markets were cointegrated with the Pacific Northwest markets. Professor Hogan first notes that the Commission cases cited by Mr. Hanser only show that the markets are interrelated, but not that the price impact in one market is translated to the other. Professor Hogan states that the market prices are determined by a mix of factors, some common and some local. Local factors include transmission constraints, credit risk, and scheduling constraints.

319. Professor Hogan argues that there is no evidence that the action of sellers in California affected the prices in the Pacific Northwest market, absent the fact that there are common market fundamentals. Therefore, Professor Hogan asserts it would not be proper to order refunds on the basis that the Commission previously found refunds were appropriate based on actions of California sellers. Here, Professor Hogan states that the market fundamentals account for any commonality between the two markets.

320. Next, Professor Hogan addresses Mr. Hanser's statistical cointegration analysis. First, Professor Hogan notes that the Commission established that a "general link" between prices in California and prices in the Pacific Northwest market would be insufficient in this proceeding. Professor Hogan contends that Mr. Hanser provided no analysis of specific actions by sellers linked to specific contracts.

321. With respect to the analysis itself, Professor Hogan notes that Mr. Hanser uses forward price data, rather than the spot prices at issue in this proceeding. Professor Hogan notes that while the two prices are related, there are variations, some significant, for many reasons, including weather. Therefore, Professor Hogan concludes that for Mr. Hanser's analysis to be meaningful, Mr. Hanser would need to show a connection between the spot market prices at issue in this proceeding and the data used in his analysis.

322. Additionally, Professor Hogan asserts that Mr. Hanser needed to control additional variables, such as the common market fundamentals, to show that the actions of sellers in California drove prices in the Pacific Northwest markets. Professor Hogan states that

without controlling for the common fundamentals, Mr. Hanser cannot show that the actions of sellers influenced price in the Pacific Northwest markets.[192]

323. Next, Professor Hogan states that Mr. Hanser failed to isolate the economic impact on Seattle (and its rate payers) of the water shortages in its hydroelectric resources. Professor Hogan notes that the water shortages caused Seattle to purchase more on-peak power than normal, and that Seattle failed to account for this submitting evidence on the cost to customers. Rather, Seattle attributed the entire cost to the market dysfunction. Moreover, Professor Hogan notes that Mr. Hanser failed to tie any specific action by particular sellers to the increased costs to Seattle.

324. Professor Hogan provides his overall view on the impact on consumers if the Commission were to retroactively abrogate the contracts. Professor Hogan first notes that consumers benefit from price stability when contracts are maintained and that consumers may be harmed if sellers of energy no longer have confidence in the contracts, limiting investment and creating instability. Professor Hogan notes that Seattle has not shown that this long-term negative impact on consumers is outweighed by the interest in abrogating the contracts. Professor Hogan asserts that certainty of contract is essential to a healthy economy. Professor Hogan states that the Commission has previously recognized the importance of contract stability, even in short-term contracts.

325. Next, Professor Hogan states that electricity demand is highly volatile, with large swings in demand during each day as the system moves from peak to off-peak loads. Too meet this demand, Professor Hogan notes that multiple generating plants with different characteristics produce electricity. Because each generator has different characteristics, the variable costs associated with the power vary greatly. Professor Hogan states that this difference in variable costs can be magnified by changes in fuel and emission costs. Thus, Professor Hogan states that markets are set up to minimize the variable cost associated with supplying a given load.

326. Professor Hogan states that in organized markets, an electric generation dispatch model is used to determine which plants are “dispatched” to produce electricity for a given load. Generators are “stacked” so that the plant with the lowest variable cost, typically coal and nuclear power, operates first. Generators with highest variable costs, also known as peaking plants, only operate when demand is highest.

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[192] Professor Hogan notes that it is not surprising the prices in California and the Pacific Northwest market are related to a certain extent because of they are physically interconnected.

327. Professor Hogan states that the principal complexities that affect the "cheapest first" dispatch are (1) the ability for a generator to change its output quickly based on changes in demand and (2) the availability of transmission. Professor Hogan notes that the more flexible the plant's output level, the more likely the opportunity costs of using it at any time is higher. Therefore, Professor Hogan states that hydroelectric generators are often treated as peaking plants because of their ability to change quickly based on demand.

328. Professor Hogan avers that transmission constraints affect the ability of generators in one area to supply demand in another area. Specifically, plants with low variable costs may not be able to supply power if the transmission capacity is unavailable to get supply to where demand is located. Professor Hogan further notes that environmental limitations, such as emissions or water temperature, also may prevent the cheapest available plants from operating. In total, Professor Hogan states that the price in the market will be at least as large as the variable cost of the most expensive generator running.

329. Professor Hogan next examines the prices in the West during the relevant period. Professor Hogan states that while prices in the WSCC tended to broadly move together, prices did vary by location. Professor Hogan states that these differences reflected the impact of transmission congestion.

330. Professor Hogan states that the following factors were the primary drivers for high prices in the West: (1) large reduction in hydroelectric resources; (2) higher demand for energy, in part due to weather; (3) high natural gas demand and prices; (4) increasing emission prices; (5) operating hour limits for some generators (as part of environmental permitting requirements); (6) nuclear generator outages; and (7) California policies which led to a reduction in Qualifying Facilities. Professor Hogan notes that California failed to make any changes that would have alleviated the supply and demand issues.

331. With respect to increasing demand, Professor Hogan notes that demand began to decline in 2001 because government entities and utilities began instituting conservation programs to address the supply shortage. Professor Hogan also states that consumption in California did not fall at the same time and to the same extent as other Western regions because the CPUC did not allow retail rates to rise in response to the high costs.

332. Professor Hogan also notes that the decline in hydro resources, the increase in gas price and demand, and the increase in emission prices are all interrelated. As less hydro was available, more gas was necessary, which increased gas prices and emissions from thermal plants. Therefore, the costs of emission credits rose. Professor Hogan states that these factors have a compound effect that dramatically increased prices.

333. Professor Hogan also discusses the changes in imports of hydroelectric power from Canada. Professor Hogan notes that the Canadian exports during the time increased

to California and decreased to the Pacific Northwest markets. Overall, Professor Hogan concludes that the amount of hydro resources decreased dramatically in 2000 and early 2001 compared to 1995-1999. Professor Hogan states that the supply of hydro generation in the West did not recover until late 2001.

334. Professor Hogan notes that the lower supply, and the fact that the drop in supply was unexpected, contributed to higher prices. Professor Hogan states that hydro suppliers were unable to properly plan for decreased supplies.

335. Next, Professor Hogan notes that the output from nuclear generators also decreased during the period, further exacerbating the supply and demand imbalance. Specifically, nuclear plant output was more than 1 million MWh lower in late 2000 than it was in 1994. The major cause of this reduction was routine refueling outages at San Onofre, Palo Verde, and Diablo Canyon. Professor Hogan notes that these outages required further reliance on natural gas, which increased the price of natural gas and natural gas fired generation. Similarly, Professor Hogan states that coal-fired generation was reduced during the Spring 2001 relative to the Summer. However, Professor Hogan notes that this is the normal operation of coal-fired generators.

336. Professor Hogan also states that changes in the outputs from Qualifying Facilities (QF) also increased the demand for natural gas fired-generation. Professor Hogan states that the change in QF output was the result of the following factors: (1) FERC rules allowing QFs to sell additional output (which tended to increase QF output); (2) high gas prices made it uneconomical to operate QFs; and (3) California IOUs failure to pay QFs. In total, Professor Hogan states that these factors lowered the output from QFs.

337. Professor Hogan concludes that as a consequence of these factors and the resulting tight supply and demand balance, there was increased reliance on natural gas fired generation. Professor Hogan notes that the amount of power produced from natural gas generation increased more than fifty percent in early 2001 compared to 1994 levels. Professor Hogan notes that this high utilization caused higher energy prices because (1) less efficient generators were operated; (2) gas prices spiked; and (3) environmental costs increased (particularly NOx emission costs, operating hour restrictions, and plant outages for environmental reasons). Professor Hogan notes that during the Western Energy Crisis, the price of spot market power and natural gas both rose together.[193]

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[193] Professor Hogan acknowledges that the prices did not move in lockstep and other factors affected the price of energy. One factor Professor Hogan discusses that affected the price of natural gas, and the subsequent price for power, was the explosion of the El Paso pipeline, which delivered natural gas to California.

338. Next, Professor Hogan discussed the impact of new generation on prices during the Western Energy Crisis. Professor Hogan first notes that unlike other markets, the CAISO did not provide a "capacity market" which was an additional revenue stream for generators. Professor Hogan states that although the CAISO market was premised on generation investment being driven by the sales of energy (long-term, short-term, and real-time), the CAISO instituted policies, such as a price cap, that did not allow for the efficient investment in generation. Moreover, Professor Hogan states that investment in new generation was further inhibited because of the western hydro cycle, which further limited the need for generation in years where water levels were normal. Thus, Professor Hogan concludes that the prices in the CAISO were not high enough to incentivize new generation investment. Professor Hogan contends that the CAISO did not take any steps to incentivize new generation until the Summer of 2000, and even this initiative was opposed by the CPUC President and the Chairman of the Electric Oversight Board. Professor Hogan states that significant new generation did not come online until after CERS began contracting for long-term power.

339. Professor Hogan notes that utilities outside California still had a traditional obligation to serve load. Therefore, these utilities were increasing generation, but without regard to spot market energy economics. However, Professor Hogan states that even these utilities were not investing in new generation at a fast enough pace.

340. Lastly, Professor Hogan concludes that the overall supply and demand imbalance was the primary factor driving the high prices in 2000 and 2001.

### N. Commission Trial Staff Answering Testimony for the Section 206 Claims

341. Trial Staff's Answering Testimony responds to testimony submitted by the California Parties, the City of Seattle, and the Respondents. Trial Staff presented the testimony and exhibits of five witnesses.

#### 1. Mr. Daniel Poffenberger[194]

342. Mr. Poffenberger's testimony responds to the California Parties' assertion that the CERS's spot market purchases were the result of fraud, duress, and bad faith. Mr. Poffenberger notes that Mr. Taylor primarily relies on the testimony of Ms. Lee and Mr. Hart to show that CERS was in a weak bargaining position and exploited by the Respondents. However, Mr. Poffenberger states that the Commission had previously determined, in the long-term contracts case, that CERS had options and that the

[194] Ex. S-1.

long-term contracts were not the product of unequal bargaining power. Mr. Poffenberger states that it would be surprising if CERS's expertise and bargaining power in negotiating long-term bilateral contracts were completely absent from its balance of month, day-ahead and day-of trading activities.

### 2. Mr. James Ballard[195]

343. Mr. Ballard's testimony concerns various engineering issues discussed by the parties in this proceeding. Mr. Ballard responds to the California Parties' assertions that Respondents engaged in False Exports.[196] Additionally, Mr. Ballard contends that Dr. Fox-Penner's long-run marginal cost analysis should have considered the lead-time for construction of new generation.

344. Mr. Ballard argues that Mr. Taylor misstates the Commission's description of the gaming activity employed by Enron. Mr. Ballard states that "False" represents deception to collect payment above price caps that were in effect at the time, not to describe the physics of how power flows in market transactions. Moreover, Mr. Ballard contends that absent the price cap, the Commission did not find similar transactions to be improper.

345. Lastly, Mr. Ballard states that Dr. Fox-Penner's long-run marginal cost analysis should have accounted for the minimum lead time for constructing new generation, which is typically two to four years based on EIA data.

### 3. Dr. David Savitski[197]

346. Dr. Savitski's testimony analyzes the California Parties' allegations regarding False Export, exchanges, price discrimination, and market power. Dr. Savitski first states that the analysis must take place on a transaction basis, noting that the California Parties often defined the unit of analysis as a portion of the transaction, a single hour of a larger block.

347. With respect to Mr. Taylor's False Export analysis, Dr. Savitski contends that the analysis is flawed because (1) it uses an export-import pair within a given hour rather

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[195] Ex. S-5.

[196] Mr. Ballard also discusses the California Parties' allegation that Respondents sold non-firm energy as firm. However, this allegation was subsequently withdrawn with respect to TransCanada and Coral, and the remaining Respondents have settled all claims with the California Parties.

[197] Ex. S-13.

linking to any particular contract; (2) the export-import link is based on coincidence rather than causation; and (3) parking, which Mr. Taylor notes is an essential part of the scheme, is not evaluated. Dr. Savitski notes that in some cases Mr. Taylor identifies transactions that were negotiated months or even years in advance as one "leg" of a False Export transaction.

348. Dr. Savitski also notes that unlike the Ricochet (or False Import) strategies discussed in the Commission's Gaming Order, the transactions identified by Mr. Taylor's False Export analysis were not done to avoid the price cap in the California organized markets. Instead, Dr. Savitski states that the transactions were used to arbitrage day-ahead and real-time prices. Dr. Savitski contends that this is a valid economic justification for any False Export (assuming it exists) because competitive firms had an incentive to by day-ahead energy and later sell it in real-time. Further, Dr. Savitski notes that because hydro resources allows for energy storage, optimal use of hydro resources involves extensive and flexible buying and selling of energy.

349. Additionally, Dr. Savitski argues that Mr. Taylor fails to consider the effect that the transactions had on each market. Dr. Savitski avers that the result of the alleged False Exports was to decrease the difference in prices between the day-ahead and real-time markets because the price is driven higher in the day-ahead market and driven lower in the real-time market due to supply shifting from day-ahead to real-time.

350. Dr. Savitski also criticizes the False Export analysis for three additional reasons: (1) because many Respondents purchased energy well in advance of the CERS Period, the Respondents would have had to refuse to sell to CERS or be subject to a False Export violation and (2) Mr. Taylor finds violations in some hours, but not others even though it is a single transaction.

351. Next, Dr. Savitski analyzes Dr. Fox-Penner's price discrimination analysis. Dr. Savitski contends that Dr. Fox-Penner's price discrimination analysis is flawed because: (1) Dr. Fox-Penner uses long-run costs in his analysis; (2) Dr. Fox-Penner ignores meaningful distinctions between CERS and other purchasers; and (3) Dr. Fox-Penner wrongly concludes that the volume and credit risk differences are trivial.

352. Dr. Savitski disagrees with Dr. Fox-Penner's use of long-run costs in his analysis because the CERS Period was too short to allow for the entry of new generation. Dr. Savitski argues that by focusing on long-run costs, Dr. Fox-Penner directs attention away from the factors that were actually impacting the short-run costs during the CERS Period.

353. Dr. Savitski next discusses scarcity pricing. Scarcity pricing occurs when the price of a product (in this case energy) reaches the point where all the production, or capacity, is sold.[198] Dr. Savitski states that once this point is reached, no price signal can create additional capacity. Dr. Savitski distinguishes this scenario with a party exercising market power because even if no party had market power, in high demand situations, the price would remain extremely high. Dr. Savitski argues that in considering the long-run costs, Dr. Fox-Penner does not consider scarcity pricing because it ignores the demand side and focuses only on the supply side.[199] Dr. Savitski states that a seller would be irrational and has no incentive to offer energy at marginal costs if the market price is higher. Dr. Savitski notes that only when demand is low will a seller reduce its pricing to the marginal costs.

354. Dr. Savitski avers that Dr. Fox-Penner also ignores, or does not properly evaluate, differences between CERS and non-CERS buyers. First, Dr. Savitski contends that Dr. Fox-Penner misevaluates the credit risk associated with sales to CERS. Dr. Savitski notes that several sellers refused to transact with CERS and that the actions of these suppliers should be given great weight because they were evaluating CERS's credit risk at the time. Dr. Savitski further states that the Commission allowed a ten percent risk premium in sales to the CAISO and CERS, many times greater than what Dr. Fox-Penner estimated.

355. Lastly, Dr. Savitski discusses the California Parties' market power analyses. Dr. Savitski first notes that the California Parties did not apply the then-applicable Hub and Spoke Test. Moreover, Dr. Savitski avers that the California Parties define the product and geographic markets too narrowly.

356. Dr. Savitski also disagrees with Dr. Reynolds' market power analysis. Dr. Savitski contends that Dr. Reynolds' product market[200] ignores other substitutes such as multi-day, balance-of-month, exchanges, and forward markets. Additionally, Dr. Savitski notes that Dr. Reynolds' geographic market also ignored locations other than

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[198] Dr. Savitski asserts that scarcity pricing was in effect during every hour of the CERS Period based on the blackouts and ISO-declared emergencies.

[199] In this regard, Dr. Savitski notes that Dr. Fox-Penner does not consider how price reduces demand and allocates energy among buyers.

[200] Dr. Reynolds' product market is the day-ahead and day-of energy markets. Dr. Reynolds also conducts an analysis using only real-time energy as the product market.

COB and NOB. Dr. Savitski states that these errors artificially increase the concentration in the market.

357. Dr. Savitski further argues that the various statistical analyses performed by Dr. Reynolds are flawed. First, Dr. Savitski notes that Dr. Reynolds' regression analysis contains dependent variables as explanatory variables. Dr. Savitski states that this leads to biased estimates regarding the impact of different variables on price. Dr. Savitski avers that using a simultaneous equations model corrects these flaws. Second, Dr. Savitski states that Dr. Reynolds' baseline regression results are not for any particular seller. Dr. Savitski states that this is contrary to the Commission's instructions to avoid a market-wide analysis and focus on specific seller behavior. Third, Dr. Savitski argues that if the sellers had market power, the CAISO's stage emergency conditions should have a stronger relationship to price than what Dr. Reynolds' analysis indicates. Fourth, Dr. Savitski asserts that Dr. Reynolds' analyses were conducted using hourly observations even though transactions were often for multiple hours.

358. Lastly, Dr. Savitski discusses Mr. Taylor's withholding claims. Dr. Savitski argues that Mr. Taylor wrongly claims that False Export transactions are withholding. Dr. Savitski states that a False Export is not withholding because the energy is being offered into the market and such transactions are consistent with price signals. Dr. Savitski states that the fact that CERS did not buy power in the day-ahead market indicates that CERS was exercising buyer-market power. Dr. Savitski states that arguments that CERS was unable to procure power in the day-ahead market ignore CERS's choice to not raise its purchase price in the day-ahead market to compete with other buyers.

### 4. Ms. Janice Radel[201]

359. Ms. Radel's testimony concerns the evidence relied upon by Mr. Taylor in his *Mobile-Sierra* analysis of the transactions between CERS and Respondents. Ms. Radel also responds to the California Parties' assertion that the price paid caused an excessive burden on California consumers.

360. Ms. Radel first notes that none of the exhibits cited by Mr. Taylor refer to a specific CERS transaction and many relate to activity outside the CERS Period. Ms. Radel also avers that Mr. Taylor relies on subjective, rather than objective, criteria in making his determinations. Ms. Radel further notes that Mr. Taylor does not consistently

[201] Ex. S-15.

apply his evaluations based on the alleged wrongdoing.[202] Thus, Ms. Radel concludes that Mr. Taylor's *Mobile-Sierra* determinations are unreliable.

361. Next, Ms. Radel discusses whether the contracts with CERS imposed an excessive burden on California consumers. Ms. Radel states that the California Parties focus only on the level of prices charged to CERS. Ms. Radel notes that the California Parties do not discuss specific contracts or separate the impact of market fundamentals. Ms. Radel also states that the rate impact was spread out over twenty years, which is often done by utilities when costs may have a large impact on rates. Ms. Radel asserts that the rate impact for the $1.05 billion in alleged overcharges by Respondents is less than seventy dollars per ratepayer. Ms. Radel concludes that this was not an excessive burden on consumers.

### 5. Ms. Chrystina Steffy[203]

362. Ms. Steffy responds to the direct testimony submitted by the City of Seattle. Ms. Steffy first argues that Seattle has not supported its claim that it is entitled to refunds. Ms. Steffy states that Mr. Hanser only makes general allegations of unlawful activity that may have affected prices. Ms. Steffy notes that there are no allegations against specific sellers for specific behavior that directly affected contract negotiations with Seattle, and that Seattle admitted that it has not reviewed individual contracts or transactions. Ms. Steffy states that Mr. Hanser's exhibits supporting his allegations of illegal behavior include testimony and documents from various proceedings from the last twelve years. Ms. Steffy argues that Mr. Hanser did not attempt to verify the factual accuracy of any documents that he did not prepare, but uses them to support his testimony.

363. With respect to Seattle's claim of withholding of energy, Ms. Steffy states that Seattle alleges that five sellers engaged in physical withholding. However, Ms. Steffy notes that Seattle has no claims against these sellers in this proceeding. Ms. Steffy also states that Seattle did not allege that any particular Respondent in this proceeding participated in the economic withholding of energy.

364. Similarly, Ms. Steffy asserts that Seattle only generally alleges that sellers engaged in manipulative activity. Ms. Steffy notes that Seattle does not make any allegations against specific Respondents in this proceeding. Rather, Mr. Hanser merely

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[202] Ms. Radel also notes that Mr. Taylor made significant changes between his originally filed testimony and his errata testimony.

[203] Ex. S-21.

notes that Avista Energy had a parking arrangement with Chelan County Public Utility District.

365. With respect to alleged violations of reporting requirements, Ms. Steffy states that Mr. Hanser does not make any allegations against specific sellers. Ms. Steffy further asserts that the Order on Remand specifically instructed the Presiding Judge to not consider these violations because they have already been resolved in a separate proceeding.

366. Next, Ms. Steffy discusses Mr. Hanser's allegation that prices paid by Seattle reflect the market dysfunction in California. Ms. Steffy argues that the Commission's orders cited by Mr. Hanser only establish that the California and Pacific Northwest markets are interconnected and interrelated, but do not establish that the prices in one market directly affected the prices in the other.

367. Lastly, Ms. Steffy discusses Mr. Hanser's claim that Seattle consumers suffered an undue burden by the high prices. Ms. Steffy contends that Mr. Hanser failed to consider evidence that indicates that other factors, such as Seattle's resource planning and market fundamentals, could have contributed to the fifty-eight percent rate increase.

### O. California Parties Rebuttal Testimony for the Section 206 Claims

368. The California Parties submitted rebuttal testimony in response to the Respondents' answering testimony. The California Parties submitted the testimony and exhibits of eleven witnesses.

#### 1. Commissioner Michael Peter Florio[204]

369. Commissioner Florio's rebuttal testimony responds to the testimony of Trial Staff witness Ms. Radel. Commissioner Florio disagrees with the assertion that because state bonds were used to spread the cost over many years, there was no excessive burden on consumers. Commissioner Florio notes that bonds are typically used when financing a tangible asset, but here, the excessive energy costs are still being paid off with no long-term asset. Commissioner Florio states that California consumers are still being asked to pay the entirety of the unjust and unreasonable rates charged in 2001. Moreover, Commissioner Florio notes that some consumers today are paying the surcharges even though they were not consumers in 2001.

370. Commissioner Florio also disagrees with Trial Staff's examination of the individual monthly rate impact of the bonds to determine if there is an excessive burden.

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[204] Ex. CAT-269.

Commissioner Florio argues that the most accurate measure of the burden on consumers is the total cost to consumers.

371. Next, Commissioner Florio contends that Ms. Radel wrongly claims that the California Parties do not link the excessive burden to a specific contract. Commissioner Florio states that it would be impossible to show that a single spot market contract imposed an excessive burden. Rather, Commissioner Florio contends that the contracts must be examined in the aggregate to assess the real burden on consumers.

372. Lastly, Commissioner Florio argues that the blackouts and potential blackouts in California imposed an additional burden on California consumers. Commissioner Florio notes that other witnesses previously testified about both the direct and indirect costs of the Western Energy Crisis on California.

### 2. Mr. Raymond Hart[205]

373. Mr. Hart's rebuttal testimony responds to claims regarding the credit risk of selling to CERS and claims that CERS had a competitive advantage when purchasing energy from Respondents.

374. Mr. Hart first states that CERS avoided posting letters of credit because the "most favored nations" clauses in the long-term contracts CERS was signing. Mr. Hart notes that these clauses would have required CERS to give letters of credit to long term suppliers for the entire amount of the long-term contract, which was not feasible because of the associated costs.

375. Mr. Hart also contends that arguments regarding "what CERS should have done" to relieve credit concerns are merely hindsight. Mr. Hart notes that from the outset CERS issued notices informing counterparties that CERS had revenues supported by appropriations. Mr. Hart states that these letters were regularly sent to sellers throughout the CERS Period. Additionally, CERS personally contacted executives of entities that refused to sell to CERS and urged them to change their policies.

376. Next, Mr. Hart responds to claims that CERS had access to non-public ISO information. Mr. Hart states that the only non-public information received by CERS traders was the gross amount of megawatts and costs of purchases the ISO was planning

[205] Ex. CAT-272.

to make from the BEEP Stack after the Commission's April 6, 2001 Order.[206] Mr. Hart states that clearly CERS paid above market prices, further indicating that it had no information that allowed it to take advantage of the market.

377. Mr. Hart states that CERS had to work with the ISO to ensure that the ISO acquired enough imbalance energy to keep the grid from collapsing. Mr. Hart notes that procedures and agreements were in place to ensure that CERS traders did not receive non-public information, but that CERS traders needed to be at the ISO to get the job done. Additionally, Mr. Hart states that he wanted CERS personnel at the ISO because CERS was responsible for paying for any ISO purchases and Mr. Hart wanted to ensure that the ISO was making purchases at prices CERS was willing to back. Mr. Hart asserts that even if CERS received non-public information, the chaotic minute-to-minute nature of the CERS Period ensured that CERS could not take advantage of this information.

378. Mr. Hart acknowledges that as the backer of the ISO Purchases, he requested that CERS be provided with certain limited non-public information to ensure that the BEEP Stack bids were made at the least possible costs. However, Mr. Hart states that CERS never received the information he requested during the CERS Period.

### 3. Ms. Susan Lee[207]

379. Ms. Lee's rebuttal testimony responds to claims regarding CERS's purchasing activities and CERS's role at the ISO

380. Ms. Lee states that Respondents mischaracterize CERS as a highly sophisticated market participant, particularly when CERS first came into existence in January 2001. Ms. Lee notes that CERS was created to respond to the energy crisis and when CERS first started, it had no supply portfolio and had to purchase all its power on the spot market. Ms. Lee states that it took time for CERS to develop a strategy for acquiring energy and that the strategy was largely not implemented by the time the Commission ended the crisis in June 2001. Ms. Lee asserts that during the CERS Period, CERS was required to purchase large amounts of spot market energy from a limited number of suppliers with little opportunity to "shop for price."

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[206] The April 6, 2001 Order required the ISO to have a creditworthy backer for all purchases made by the ISO. The April 6, 2001 Order also reinvigorated the BEEP Stack by eliminating the soft cap and "pay as bid" mechanisms.

[207] Ex. CAT-285.

381. Additionally, Ms. Lee states that CERS was limited by ISO directions (due to transmission congestion) that prevented CERS from buying energy at certain locations, further limiting the number of suppliers and the ability to buy lower priced energy. Ms. Lee acknowledges that more suppliers were available in the day-ahead market, but states that there were not many.[208]

382. Next, Ms. Lee contends that Respondents wrongly assert that CERS under-scheduled in the day-ahead market to drive down prices. Ms. Lee notes that CERS tried to fulfill its entire net short in the day-ahead market because it did not know if energy would be available in real-time. Ms. Lee asserts that sellers would often refuse to sell in the day-ahead market and waited until real-time. Ms. Lee notes that CERS only passed on day-ahead energy if the price was very high in comparison to what CERS expected to pay.[209] Ms. Lee notes that some counterparties even offered to aggregate energy for CERS because they could purchase energy at prices lower than what was offered to CERS. Ms. Lee states that even when the day-ahead prices were extremely high, CERS attempted to purchase as much of the net short as possible.

383. Ms. Lee also addresses TransCanada witness Dr. Morris's assertion that CERS engaged in buyer-side price discrimination. Ms. Lee states that CERS did not buy energy at the same price from all sellers in the bilateral markets. However, Ms. Lee notes that CERS could not dictate prices and was in fact forced to purchase at prices dictated by sellers. Ms. Lee contends that any difference in price was due to the seller's behavior, noting that Coral tended to demand the highest prices for their energy.

384. Ms. Lee also contends that acquisition of transmission capacity by CERS was not likely to broaden the number of suppliers available. Ms. Lee states that those sellers willing to transact with CERS had adequate transmission to provide energy at COB or NOB.

385. Next, Ms. Lee states that she was never aware that CERS used confidential ISO information in its purchasing decisions. Ms. Lee asserts that CERS traders were stationed at the ISO to make OOM purchases that the ISO needed to balance the market, and that close coordination between ISO schedulers and CERS traders was critical given the timing of when energy needed to be purchased. Ms. Lee notes that sellers refused to sell the needed OOM directly to the ISO because of credit risks. Therefore, the ISO

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[208] For example, Ms. Lee states that on March 8, 2001, CERS purchased over 4,100 MWh from only 15 suppliers in the day-ahead market.

[209] Ms. Lee knows of only two instances where CERS refused to buy day-ahead energy because the price was too high.

directed CERS to make certain purchases and CERS had no discretion to make these purchases on their own.

386. Ms. Lee notes that precautions were made to ensure that CERS traders did not have non-public information. Specifically, CERS traders were stationed on the periphery of the ISO floor and required to sign non-disclosure agreements.

387. Ms. Lee acknowledges that CERS asked the ISO for non-public information, but that the ISO refused to give the information during the CERS Period. Ms. Lee notes that CERS did receive aggregate cost and volume information after April 6, 2001 because CERS was required to back the ISO's purchases. Ms. Lee states that the non-public information received after the CERS Period was also aggregate information and did not give CERS a market advantage.

388. Ms. Lee states that she is not aware of any instance where CERS used confidential ISO information to affect negotiations with sellers. Additionally, Ms. Lee notes that CERS did not have information on the ISO's BEEP Stack during the CERS Period and that even if it did, no Respondent sold into the BEEP Stack.

#### 4. Mr. Gerald Taylor[210]

389. Mr. Taylor's rebuttal testimony responds to various assertions made by the Respondents in their answering testimony.

390. First, Mr. Taylor states that Respondents wrongly claim that market fundamentals and a "perfect storm" of circumstances explain the high prices paid by CERS during the Western Energy Crisis. Mr. Taylor contends that many of the arguments made by Respondents have previously been addressed by the Commission in earlier decisions dealing with the Western Energy Crisis. Mr. Taylor notes that the Commission allowed refunds for all purchases in both the CalPX and ISO OOM markets.[211] Additionally, Mr. Taylor states that the recent Initial Decision in Docket No. EL00-95-248 rejected arguments that the market fundamentals explain the high prices.

391. Mr. Taylor also notes that the March 2003 Commission Staff Report concluded that market fundamentals did not fully explain the prices in the Pacific Northwest. The

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[210] Ex. CAT-289.

[211] Mr. Taylor notes that ISO OOM purchases included transactions in the Pacific Northwest market, which are essentially the same as CERS's purchases at issue in this proceeding.

Staff Report also stated that the Pacific Northwest market was affected by the California spot market, which was driven up by market manipulation. With respect to the "cointegration" of prices in California and the Pacific Northwest, Mr. Taylor states that traders were aware that prices were being driven by California. Mr. Taylor further notes that the EL00-95-248 Initial Decision found the manipulative activity of Respondents in that proceeding, many who are also Respondents in this proceeding, affected the price at COB.

392. Next, Mr. Taylor contends that Respondents claim about market fundamentals is inconsistent with observed pricing patterns and ignores evidence. Mr. Taylor argues that the reduction in hydroelectric resources was the result of a strategic decisions, and that the increase in costs associated with gas-fired generation did not occur until after the electricity prices had already risen to unprecedented levels. Mr. Taylor states that Professor Hogan fails to explain why prices began to spike in May 2000, prior to the decrease in water levels and high natural gas prices.

393. Additionally, Mr. Taylor states Professor Hogan fails to discuss the fact that hydro generation can be discretionary. That is, hydro generation moves up or down based on the decisions of the operator. Mr. Taylor alleges that the decline in hydro generation during December 2000 "maps closely" with Powerex's plan to import large volumes of energy from the United States. Mr. Taylor notes that in prior years, Powerex imported approximately 600 MWh per hour into the United States. However, from December 2000 through March 2001, Powerex exported 1,100 MWh per hour. Mr. Taylor contends that Powerex's "swing in supply" was sufficient to have a tightening effect on overall energy supply and cause prices to rise.[212]

394. Mr. Taylor also responds to Respondents' assertions that they lacked market power. Mr. Taylor first notes that demonstrating that Respondents charged excessive prices based on fraud, duress or bad faith does not require a showing of market power. Mr. Taylor further notes that a showing of manipulation also does not require the seller to possess market power.

395. Regardless, Mr. Taylor avers that market power played a role in the prices paid by CERS. Mr. Taylor notes that the Respondent witnesses admit that high prices were partially the result of high margins over costs. Thus, Mr. Taylor argues that high costs cannot be used to justify the high prices. Additionally, Mr. Taylor contends that defenses based on credit risk are at odds with other explanations, such as high natural gas prices and emission permitting. Mr. Taylor further asserts that Respondents cannot claim that

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[212] Mr. Taylor states that this 1,700 MWh swing was generally larger than the entire net short of the California IOUs.

scarcity rents caused the increased prices because those scarcity rents would go to the generators, not the aggregators.[213] Mr. Taylor notes that the Commission Staff Report admitted that "it is difficult to separate scarcity from market power."

396. Next, Mr. Taylor discusses the claims made by Coral in its answering testimony. Mr. Taylor notes that Coral's witnesses discuss both credit risk and regulatory risk in seeking to justify the high mark ups charged to CERS. Mr. Taylor, relying on Dr. Fox-Penner's analysis, contends that credit concerns could not have justified Coral's $200 to $250/MWh premium over costs. Mr. Taylor notes that large suppliers, with more credit exposure to CERS, sold energy at lower margins. Moreover, Mr. Taylor contends that as CERS became less of a credit risk, based on Coral's own risk assessment, Coral raised its premiums rather than lowering them. Thus, Mr. Taylor concludes that the increase in price was simply to maximize profits. Mr. Taylor further notes that Coral's "premium" often increased if the price of energy increased, demonstrating that there was no link between credit risk and price.

397. Mr. Taylor states that Ms. Bowman's testimony, Coral trader tapes, and Coral emails demonstrate that Coral refused to sell to CERS until CERS became desperate enough to give in to Coral's price demands. Mr. Taylor notes that Ms. Bowman admits that Coral set prices at a level that would maximize profits without exceeding credit limits. Mr. Taylor characterizes this activity as withholding sales until CERS had no choice but to give in to the price demands. Mr. Taylor cites trader tapes where Coral would try to extract high mark ups ($75 to $200/MWh) on energy that it would buy and resell immediately to CERS. Mr. Taylor states that often Coral would refuse to sell or simply cancel Coral's planned purchase until CERS agreed to the high price.

398. Mr. Taylor further notes that Coral's strategy of engaging in B2B transactions demonstrates that Coral was not merely waiting until the market price went higher. Rather, the price that Coral paid for the energy was the market price and the immediate resale price to CERS was far above market pricing. Mr. Taylor contends that Coral was using CERS's position and Coral's market power to extract high prices.

399. Mr. Taylor also asserts that Coral's claim that regulatory risk justified high prices is inaccurate and circular. Mr. Taylor describes this claim as essentially saying that the risk of high prices being remediated by the Commission justifies charging high prices. Therefore, by increasing margins, Coral increased the risk that the Commission would remediate the contracts.

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[213] Mr. Taylor admits that scarcity played a factor in the pricing. However, Mr. Taylor notes that the scarcity allowed the exercise of market power.

400. Lastly, Mr. Taylor states that email correspondence and recorded conversations of Coral traders demonstrate that CERS traders only bought energy from Coral when under duress because it was absolutely necessary. Mr. Taylor notes that CERS traders often refused to buy from Coral because the prices were too high. In one instance, CERS refused to buy power from Coral even on a day with rolling blackouts.

401. Next, Mr. Taylor argues that TransCanada failed to justify the high prices of its sales to CERS. Mr. Taylor avers that the reason for TransCanada's high prices to CERS was high mark ups, not high acquisition costs. Mr. Taylor notes that TransCanada's mark ups often ranged from $115 to $165 per MWh with a sales price to CERS of $375 to $420 per MWh.

402. Mr. Taylor also asserts that TransCanada's trader records clearly reflect that TransCanada parked energy for sale in real-time. Mr. Taylor states that the fact that TransCanada engaged in this practice with other transactions only brings those transactions into question; it does not justify the transactions with CERS.

403. Mr. Taylor asserts that TransCanada's preference for real-time was not a legitimate response to CERS not revealing its true demand in day-ahead purchasing. Mr. Taylor states that this is a version of the underscheduling argument that was rejected by the EL00-95-248 Initial Decision. Moreover, Mr. Taylor notes that the prices in the day-ahead market at COB, where CERS purchased energy, were consistent with the prices at Mid-C, where CERS was not a participant. Therefore, there was no "driving down" of prices by CERS in the day-ahead market.

404. With respect to the trader tapes cited by TransCanada,[214] Mr. Taylor contends that TransCanada merely "cherry picked" certain trader conversations. Mr. Taylor notes that for six of the eight transactions cited by TransCanada, there was no finding of bad faith or duress. Therefore, it is unsurprising that the trader tapes reflected this. For the remaining two examples, Mr. Taylor states that in one, TransCanada realized that the market had fallen substantially and sold to CERS at a price far above market value. For the final example, Mr. Taylor acknowledges that he originally found duress where it did not exist and has subsequently changed his conclusion.

405. Next, Mr. Taylor responds to allegations made by several Respondents that CERS acted wrongly or caused the high spot market prices. Specifically, Respondents claim that CERS did not try to purchase all its power in the day-ahead market and that CERS had access to confidential ISO information.

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[214] TransCanada cites trader tapes to demonstrate that transactions with CERS were not the product of duress.

406. Mr. Taylor states that Respondents argue that CERS was a monopsonist and intentionally limited its day-ahead purchases in order to lower overall acquisition costs. Mr. Taylor first contends that CERS could not reduce the overall quantity of purchases because those were driven by consumption in California. Mr. Taylor asserts that if CERS were trying to exert buyer market power, CERS was "spectacularly unsuccessful." Mr. Taylor notes that Dr. Fox-Penner demonstrated that CERS paid higher prices than other participants, and that sellers to CERS made extremely large profits. Moreover, Mr. Taylor states that the day-ahead prices at COB, where CERS bought power, were essentially the same as the price at Mid-C, where CERS was not a participant. Conversely, in the day-of market, prices at COB were consistently higher than prices at Mid-C. Therefore, Mr. Taylor concludes that CERS's activity in the market resulted in higher prices in the day-of market.

407. Mr. Taylor also asserts that there is no credible evidence that CERS was or acted as a monopsonist. Mr. Taylor states that Respondents merely point out that CERS was the largest buyer in the market, but provided no analytical or evidentiary support. Further, Mr. Taylor states that the bilateral nature of the market and the relatively small role of CERS's day-ahead purchasing would make profitable withholding of day-ahead purchases very difficult.

408. Mr. Taylor states that during the CERS Period nearly an equal amount of energy was purchased in the day-ahead and day-of markets. Conversely, prior to the CERS Period, over eight-five percent of the IOUs purchases were in the day-ahead market. Mr. Taylor argues that because CERS had much less exposure to day-ahead prices, lowering of overall costs through reductions in day-ahead purchases was much less likely in the CERS Period than had been earlier.

409. Moreover, Mr. Taylor contends that there is affirmative evidence that CERS could not exercise buyer market power. Mr. Taylor states that trader tapes demonstrate that when CERS did try to "hold the line" on prices, it could not do so without threatening reliability. Mr. Taylor argues that the potential for blackouts gave Respondents market power with respect to CERS.

410. Mr. Taylor states that CERS sought to purchase as much day-ahead energy as it could at reasonable prices. Mr. Taylor notes that CERS faced several obstacles to supplying energy where it was needed, such as: (1) needing energy in Northern California even though much of the generation in California is in the south; (2) persistent south to north congestion; and (3) sellers in the north (at COB) refusing to sell to CERS and selling to "aggregators" instead. Mr. Taylor contends that CERS's only defense against these "aggregators" selling at excessive prices was to refuse to purchase in the day-ahead market. In support of his claims, Mr. Taylor cites a trader tape between a CERS trader and a broker in which the broker states that counterparties were offering high prices because CERS had very few options.

411. Next, Mr. Taylor addresses Respondents claims that CERS had access to confidential ISO information and used this information to reduce prices. Mr. Taylor notes that California Parties witnesses Mr. McIntosh and Mr. Alaywan, who oversaw the operations in the CAISO Control Room, confirm that it was essential for CERS traders to be located at the ISO and that CERS traders did not have access to confidential information.

412. With respect to allegations regarding Mr. Hart's effort to obtain BEEP Stack information, Mr. Taylor states that Mr. Hart and Mr. Alaywan both testify that the information was not provided to CERS until after the CERS Period. Moreover, the information that was provided was done so in a form that would not give CERS a competitive advantage.

413. Next, Mr. Taylor states that criticisms of Dr. Fox-Penner's price discrimination analysis have not altered his reliance on Dr. Fox-Penner's conclusions. Mr. Taylor notes that Dr. Fox-Penner responded to the criticisms in his rebuttal testimony and that Dr. Fox-Penner's updated findings were incorporated into Mr. Taylor's *Mobile-Sierra* database. Mr. Taylor asserts that the very fact that Respondent witnesses try to justify their higher prices to CERS demonstrates that their prices to CERS exceeded prices charged to others. Mr. Taylor also agrees with Dr. Fox-Penner that the Respondents failed to provide an adequate justification for the higher prices charged to CERS.

414. Mr. Taylor also states that Dr. Reynolds responds to criticisms of his market power analysis. Mr. Taylor avers that these criticisms did not cause Dr. Reynolds to change his conclusion that Respondents exercised market power. Moreover, Mr. Taylor notes Dr. Reynolds' rebuttal testimony regarding potential buyer market power is consistent with Mr. Taylor's finding that CERS did not exercise buyer market power.

415. Next, Mr. Taylor addresses various criticisms of his False Export analysis. Mr. Taylor first responds to Respondents' claim that the import and export transactions were independent of one another. Mr. Taylor states that just because two transactions were executed by different traders does not make them independent.

416. Mr. Taylor next addresses Coral's claim that it did not engage in False Exports because it did not supply CERS from a portfolio of resources that included purchases from within California, but rather from specific back-to-back purchases from suppliers outside the ISO. Mr. Taylor states that this does not change his False Export allegation because as a pure marketer, Coral required a third-party parking provider to buy in day-ahead and sell in real-time. Mr. Taylor states that the parking provider became the fictitious source of the laundered energy that the parking customer then sold to the ISO or later to CERS. Therefore, Mr. Taylor contends that what appears to be a back-to-back purchase from the parking provider and a resale to CERS is merely the completion of a False Export transaction. Mr. Taylor further notes that Coral previously stated that it

relied on a portfolio of energy products, but in this proceeding is denying that it used its portfolio for sales to CERS.

417. Mr. Taylor states that even if Coral's sales to CERS were sourced from outside California, the contracts should still be mitigated on the basis of fraud, duress, or bad faith. Mr. Taylor notes that Coral traders were instructed to wait for opportunities to extract excessive margins from CERS.

418. With respect to Coral's assertion that the "multi-party" False Exports were not sourced from within the CAISO, Mr. Taylor acknowledges that this is "technically correct." Mr. Taylor further notes that Coral's Answering Testimony demonstrates that these transactions did not involve withholding energy from the day-ahead market. Thus, Mr. Taylor states that he dropped these transactions from his False Export analysis.

419. Next, Mr. Taylor addresses Respondents issues with the methodology used in the False Export analysis. Mr. Taylor states that while some of these claims are without merit, some are valid and have motivated adjustments to the analysis. Mr. Taylor states that these adjustments reduce the volume of False Export transactions, but do not alter the conclusion that Coral engaged in False Export transactions during the CERS Period.

420. Specifically, Mr. Taylor states that he adjusted the analysis to correct claims regarding (1) double counting of hours in which False Exports occurred, (2) failing to eliminate all SP-NOB False Exports during hours of congestion, and (3) failing to fully account for wheel-through transactions.

421. Mr. Taylor also responds to criticisms from Trial Staff witness Mr. Ballard that he did not follow the Commission's definition of Enron's Ricochet strategy because the transactions were not done to avoid a price cap. Mr. Taylor notes that he is not relying on the Commission's precise definition. Rather, Mr. Taylor states that he explained in his analysis that these transactions harmed both the markets and the grid's reliability.

422. Next, Mr. Taylor contends that the California Parties have provided sufficient proof to link Respondents' behavior to specific contracts. Mr. Taylor first notes that his *Mobile-Sierra* database organizes information gathered from other sources and analyses relating to contracts. Thus, Mr. Taylor states that the *Mobile-Sierra* database is not itself the proof, but rather a way to organize the facts associated with each contract.[215]

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[215] For example, Mr. Taylor notes that there is evidence of Coral's practice of demanding excessive, unjustified margins and holding out until CERS was desperate enough to pay them. Mr. Taylor contends that this evidence could justify setting aside all Coral contracts as being negotiated under duress.

423. With respect to Respondents' criticism that his definition of contract is too broad, Mr. Taylor notes that confirmations were typically memorialized in recordings of trader conversations that established the terms of each deal. Mr. Taylor states that analyzing these confirmations is further complicated by the fact that the agreements were often adjusted several times during the course of a day. Mr. Taylor notes that parties expected that changes would occur throughout the operating day. Mr. Taylor provides an example in which a sale from BPA to CERS was adjusted eight times (price and volumes) over the course of the day and that by the end of the day the final outcome bore little resemblance to the terms discussed in the initial call.

424. In such circumstances, Mr. Taylor argues that it is not appropriate to rely upon the initial conversation as the contract and not reasonable to rely solely upon any of the subsequent adjustments. Thus, Mr. Taylor states that it is reasonable to consider each set of trades at the end of the day, when it is done because it is the only way the arrangements can be properly understood. Mr. Taylor states that this is the way transactions were memorialized in the CERS database.

425. Mr. Taylor contends that the evidence from Dr. Fox-Penner, Dr. Broehm, and Dr. Reynolds incorporated in the *Mobile-Sierra* database is reliable. Mr. Taylor states that the evidence received in discovery since the filing of the Direct Testimony, largely trader recordings, further confirms that CERS was the victim of price discrimination.

426. Mr. Taylor also disagrees with Respondents criticism that he used the market prices from *Power Markets Week* index for high load and low load transactions at COB and Mid-C during the CERS Period. Mr. Taylor states that he does not rely solely on high prices, but relies on a variety of evidence including both documentary evidence, pricing evidence, and expert analyses.

427. Next, Mr. Taylor responds to criticisms that his analyses are arbitrary and cannot reliably be replicated. Mr. Taylor argues that the process of determining if there is substantial evidence that contracts be set aside or prices be found contrary to the public interest does not lend itself to a formulaic determinations. Mr. Taylor notes that "duress" and "bad faith" are legal terms and there is no way to objectively quantify the weight to be given evidence that a party was in a weak bargaining position or that another sought to take advantage. Thus, although most cases were "clear cut," there were some instances that required judgment.

428. Mr. Taylor further contends that it was appropriate to consider evidence of general negotiating conditions, intent, and practice in evaluating individual contracts. For example, Mr. Taylor states that Coral traders were instructed to turn down profitable trades until CERS agreed to higher prices that met Coral's excessive margin targets.

429. Lastly, Mr. Taylor responds to Respondents' and Trial Staff's criticisms of his finding that the contracts are against the public interest. Mr. Taylor notes that Ms. Radel

argues that the bonds, which spread the cost of the CERS Period over twenty years, essentially eliminated any burden the contracts at issue could have imposed on California ratepayers. Mr. Taylor states that the fact that an unjust burden is spread out over time does not somehow transform it into something more just or less of a burden. Moreover, Mr. Taylor notes that the issuance of the bonds damaged California's credit rating and had wide-ranging impacts that California is only now recovering from.

### 5. Dr. Peter Fox-Penner[216]

430. Dr. Fox-Penner's rebuttal testimony responds to criticisms of his direct testimony by Respondents. Dr. Fox-Penner states that generally, Respondents argue: (1) that higher prices were not, in fact, charged to CERS for similar products; (2) that if higher prices were charged to CERS, it was due to greater supplier costs relating to CERS's credit or other risk factors, the greater volumes demanded by CERS, or that CERS bought a more flexible or shaped product that was more valuable or costly to provide; and (3) that an individual Respondent should not be considered to price discriminate if the prices it charged CERS were representative of all suppliers' prices charged to CERS.

431. Dr. Fox-Penner states that two conditions are necessary to support sustained, non-cost justified price discrimination: (1) market power over one particular customer or group of customers (in this case, CERS) and (2) an inability to easily resell the product.[217] Dr. Fox-Penner notes that Dr. Reynolds finds substantial empirical evidence that market power was present and exercised in transactions with CERS and Mr. Taylor explains how Respondents' conduct maintained and exploited that market power.

432. Dr. Fox-Penner next explains how the overall credit situation enhanced sellers' market power. Dr. Fox-Penner notes that it is standard practice for sellers in power markets to set credit limits for every counterparty in order to manage risk and limit exposure. Because of the high prices during the CERS Period, these credit limits were reached much more quickly. Dr. Fox-Penner contends that when prices are very high for sustained periods of time, credit limits can constrain market-wide supply at precisely the times when power is most needed, creating the potential for exercises of market power by those suppliers who have power to sell and who have sufficient headroom under their credit limits to still make sales.

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[216] Ex. CAT-413.

[217] Price discrimination is prevented when the low priced buyer can resell the product to the high priced buyer, undermining the seller's ability to discriminate.

433. Dr. Fox-Penner asserts that CERS was particularly affected by the credit constraints because CERS was a large buyer and it quickly hit the credit limits set by most sellers. Dr. Fox-Penner states that this greatly diminished its access to supply, allowing the remaining sellers to increase their prices. Dr. Fox-Penner notes that of the potential counterparties in the Pacific Northwest market, eight suppliers never sold to CERS because of credit concerns and most other suppliers only sold to CERS sporadically. Only twelve suppliers transacted in more than half of the weeks in the CERS Period and sold over 100,000 MWh. Dr. Fox-Penner states that this demonstrates that CERS was required to buy most of its volumes from only a few sources.

434. Dr. Fox-Penner also states that rapid, low-cost resale was not feasible in the markets in which CERS transacted. Dr. Fox-Penner states that the primary barrier to resale to CERS was often CERS's lack of credit.

435. Next, Dr. Fox-Penner contends that scarcity and market fundamentals do not explain the higher prices that Respondents charged CERS. Dr. Fox-Penner states that the tight supply conditions helped allow Respondents to exercise market power and engage in price discrimination. Dr. Fox-Penner notes that the FERC Staff Report concluded that "the underlying supply-demand imbalance and flawed market design greatly facilitated the ability of certain market participants to engage in manipulation." Further, Dr. Fox-Penner argues that market fundamentals are irrelevant to his price discrimination analysis because the fundamentals were relevant to all purchasers at the time, not just CERS.

436. Dr. Fox-Penner also asserts that Professor Hogan incorrectly compares PJM scarcity pricing with the prices charged to CERS because in PJM's organized market, a market-wide clearing price is set for all buyers. Dr. Fox-Penner states that if there is market-wide scarcity, the scarcity pricing should apply to all buyers. However, Dr. Fox-Penner alleges that CERS paid an additional premium that other buyers did not pay.

437. Dr. Fox-Penner also responds to Dr. Savitski's criticism of using long-run marginal costs for a price cap on spot market prices. Dr. Fox-Penner states that his testimony does not argue this and only points out that the spot market prices were many times higher than the long-run marginal costs. Similarly, Dr. Fox-Penner states that he did not conclude that any price above a seller's short-run marginal cost is *per se* improper.

438. Next, Dr. Fox-Penner addresses Respondents criticism that his analysis did not account for differences in the timing of transactions or the duration of delivery periods. Dr. Fox-Penner argues that the exact time of trade within a given day or hour would only affect the price of transactions if there were extreme and wholly unpredictable intra-day or intra-hour price volatility. Dr. Fox-Penner contends that his conservative thresholds for finding price discrimination accommodate any potential volatility.

439. With respect to the duration of the transactions, Dr. Fox-Penner contends that most of the day-of sales were transacted in very close timeframes and were of closely comparable durations. Dr. Fox-Penner concludes that the vast majority of matched CERS and non-CERS sales were either of perfectly matched identical hour durations or closely comparable durations.[218]

440. Dr. Fox-Penner also argues that it was reasonable to compare transactions at different locations because he adjusted the cost to reflect the cost of transmission and line losses. Dr. Fox-Penner asserts that Respondents' suggestion to use the price difference between the two locations is only useful if congestion exists on transmission paths between the two trading locations. Dr. Fox-Penner avers that without congestion, traders would take advantage of any arbitrage opportunity based on the price difference between the two locations. After examining the day-ahead price differential between COB and Mid-C, Dr. Fox-Penner concludes that transmission congestion was not common during the CERS Period. Dr. Fox-Penner further notes that the BPA transmission system experienced very little congestion for day-of transactions.

441. Next, Dr. Fox-Penner argues that finding perfectly identical matching transactions was unnecessary given the conservative price discrimination criteria used in the analysis. Dr. Fox-Penner asserts that Respondents' assumption that discrimination can be demonstrated only when there are contemporaneous, precisely-matching transactions that are identical in every respect but for the prices charged to a particular party is an impossibly stringent requirement to apply. Dr. Fox-Penner states that his approach was more stringent than the test that the Commission historically requires to be met and more conservative than the common treatment of economic discrimination in the United States courts. Dr. Fox-Penner notes that the Commission's test for price discrimination only requires that two customers be "similarly situated."

442. Dr. Fox-Penner further asserts that trader tapes demonstrate that sellers routinely offered prices to CERS at levels well above what they knew was the market price and well above the level at which Respondents themselves bought and sold with non-CERS counterparties. Dr. Fox-Penner avers that Respondents witnesses do not deny that different prices were charged to CERS as a matter of course. Thus, Dr. Fox-Penner concludes that the relatively few identically matched transactions do not imply a lack of widespread price discrimination; they simply limit the ability to prove discrimination by a simple inspection of identical transactions.

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[218] Dr. Fox-Penner defines closely comparable as transactions that are both (1) fully delivered within the same peak or off-peak period and (2) have no greater than two hours difference in durations.

443. With respect to the Commission's definition of "similarly situated," Dr. Fox-Penner states the essential aspect of being similarly situated is that the products and services obtained are similar (which is not the same as being identical) and that the differences in costs of supplying the two groups (if any) are insufficient to explain the differences in prices charged to the two groups. In applying this definition, Dr. Fox-Penner states that he first ensured that the products purchased by CERS and non-CERS buyers were substantially similar by comparing the same type of energy (day-ahead or day-of) delivered on the same day or hour in the same or nearby locations. Dr. Fox-Penner also examined for differences in the costs of serving CERS and non-CERS buyers and concluded that the average size of the transaction and differential credit risk could not explain the $50 to $200/MWh premiums that Respondents routinely charged to CERS.

444. Next, Dr. Fox-Penner states that in addition to specific transaction records of Respondents and CERS, he analyzed data on the average day-ahead and day-of prices and their dispersion using the Commission's data from Docket No. PA02-2. Dr. Fox-Penner states that this data allowed him to employ additional benchmarks for comparing transaction prices to detect additional instances of price discrimination.

445. Dr. Fox-Penner asserts that he use several benchmarks applied to every single hour or day during which CERS purchased power and applied his expert judgment to these combined benchmarks. Dr. Fox Penner contends that no single automatic formula is able to accurately assess the incidence of undue price discrimination in complex and dynamic power markets and such an approach would not provide the Commission with "scientific" or "objective" evidence that would assist in rendering a decision. Dr. Fox-Penner states that the Commission has never relied on a single arithmetic formula in determining price discrimination and typically uses its judgment after assessing the degree to which customers are similarly situated, the magnitude and nature of cost differences between the similarly situated customers, and the size of the price or rate differential. Further, Dr. Fox-Penner notes that the Respondents have failed to use a formula to determine whether undue price discrimination occurred.

446. Next, Dr. Fox-Penner uses alternative approaches to demonstrate that price discrimination by the Respondents was understated in his analysis. Dr. Fox-Penner states that economists typically conduct econometric regression analyses to determine if price discrimination occurred. Dr. Fox-Penner notes that these analyses don't require identical matching either because the purpose of the analysis is to avoid the need for exact matches. Rather, the econometric analyses isolate variables to determine the portion of cost increase due to each variable. Dr. Fox-Penner notes that United States adjudicatory bodies have given significant weight to these types of analyses.

447. Dr. Fox-Penner states that he conducted a regression analysis for each of the Respondents. The purpose of the test was to determine if a Respondent's sales to CERS were higher priced than sales to other purchasers during the CERS Period, when

controlling for the effects of higher sales quantities, natural gas prices, transmission congestion, ISO emergencies, peak conditions, and the particular changes occurring in the market each month. Dr. Fox-Penner asserts that the results of this analysis confirms that price discrimination occurred by all Respondents. The regression finds that Coral and TransCanada charged CERS $123 and $79 per/MWh more than they charged other non-CERS buyers, respectively. Dr. Fox-Penner notes that he varied the regression equation that he used, and in each case, price discrimination was found.

448. Dr. Fox-Penner also argues that the cost of credit risk does not account for the differences in price between CERS and non-CERS buyers. Dr. Fox-Penner first notes that only Coral explicitly discussed a credit risk premium in their Answering Testimony – other Respondents described the risk of selling to CERS, but focused on the use of credit limits to handle risk.

449. Dr. Fox-Penner states that the Commission previously addressed the credit risk for sales during the Western Energy Crisis. In the June 19, 2001 Order, the Commission established a ten percent premium for sales to the CAISO based on the risk of non-payment. Dr. Fox-Penner argues that the ten percent premium would be too high for sales to CERS because unlike the CAISO, CERS had no defaults and paid suppliers on a faster time frame.

450. With respect to Coral's sales to CERS, Dr. Fox-Penner states that the size of the premium charged by Coral was consistently higher than ten percent, averaging approximately twenty-five percent over the CERS Period. Dr. Fox-Penner asserts that Coral provided no justification for its mark-ups on it sales to CERS and did not justify why the CERS credit risk premium varied from as low as $50 to as high as $175.[219] Dr. Fox-Penner states that Coral, like other sellers, managed its risk exposure through credit limits and that the margins paid by CERS were unrelated to credit risk. Dr. Fox-Penner notes that Coral raised credit limits in order sell to CERS at higher margins, having an inverse relationship one would expect if high mark-ups reflected increased concerns about CERS's creditworthiness.

451. Next, Dr. Fox-Penner discusses Respondents' argument that the margins reflect the potential for Commission ordered refunds. Dr. Fox-Penner argues that there is no economic rationale for the Commission to include a regulatory risk premium as a legitimate element of seller cost. Dr. Fox-Penner states that the overcharge itself creates the risk of refunds and the probability of a refund order increases with the size of the

[219] Dr. Fox-Penner acknowledges that Coral provides some evidence that Coral was concerned about CERS's credit and that concern varied. However, Coral did not provide any evidence on how the premium was calculated.

"regulatory risk premium." Dr. Fox-Penner further notes that sellers in all Commission-regulated markets always bear the risk of Commission enforcement actions. Therefore, there is no reason to believe that the cost of bearing the risk of a Commission ordered refund was numerically significant.

452. Dr. Fox-Penner also avers that Respondents wrongly assert that large volume of each transaction justifies the higher prices charged to CERS. Dr. Fox-Penner notes that the Respondents provide no analysis to support their criticism other than to point out the volume differences between CERS and non-CERS transactions. Dr. Fox-Penner states that had the Pacific Northwest market been competitive, buyers with large demand, like CERS, would have had access to many competitive supply choices and could have aggregated the supply in a manner similar to what the Respondents did to extract large profits. Dr. Fox-Penner contends that the reason why the volumes sold to CERS were so high was because a few sellers aggregated the supply and resold to CERS.

453. Dr. Fox-Penner states that Dr. Reynolds' analysis establishes that prices charged to CERS increased significantly with quantity because the seller has a greater ability to exercise market power. Dr. Fox-Penner notes that trader tapes from Coral confirm that Coral was careful not to let other parties know it was in a "net-short" position because other sellers would be able to extract high prices from Coral when it needed to buy additional power. Additionally, Dr. Fox-Penner states that his regression analysis confirms that prices increased depending on the volume purchased by CERS.

454. Next, Dr. Fox-Penner responds directly to the arguments made by Coral in their answering testimony. Dr. Fox-Penner first notes that Coral engaged in back-to-back (B2B) transactions with CERS in the day-of market. Dr. Fox-Penner states that Coral pursued few day-of B2B transactions with other buyers. However, in the day-ahead market, Coral engaged in B2B transactions with buyers other than CERS.

455. Dr. Fox-Penner contends that Coral wrongly asserts that the premiums calculated in his analysis are overstated. Dr. Fox-Penner notes that Coral calculates the average mark up on B2B transactions while the price discrimination analysis determines the premium based on similar sales to other parties. Dr. Fox-Penner argues that these are entirely different calculations that are not comparable. However, Dr. Fox-Penner contends that Coral's calculations show price discrimination because Coral's back-to-back transactions show that some other seller was willing to sell otherwise identical power to Coral at a price much lower than the price that Coral obtained from CERS.

456. Dr. Fox-Penner states that when comparing Coral's markups on back-to-back sales to CERS with Coral's markups on back-to-back day-of sales to other counterparties, he finds that Coral consistently singled out CERS and applied markups that were significantly higher ($100/MWh more). Dr. Fox-Penner notes that the average mark-up

for day-ahead B2B transactions (CERS did not engaged in any day-ahead transactions with Coral) was only $0.40/MWh.

### 6. Dr. Carolyn Berry[220]

457. Dr. Berry first states that in her Direct Testimony, she found that CERS's real-time purchases from Respondents consisted of the exact same energy as CERS's real-time OOM sales to the CAISO. Dr. Berry notes that the Commission has already found that the prices of CERS's real-time OOM sales to the ISO were unjust and unreasonable and have been mitigated.

458. Dr. Berry asserts that Dr. Morris wrongly claims that her testimony "makes no economic sense because it is clearly using an apparent financial tracking mechanism to make presumptions about the appropriateness of refunds." Dr. Berry states that the "financial tracking mechanism" is really just tracing of the actual megawatt hours at issue in this proceeding from the Respondents to CERS, and then from CERS to the CAISO. Dr. Berry avers that if the CERS-to-CAISO portion of the transaction has already been mitigated, the Respondent-to-CERS portion involving the very same megawatt hours should also be mitigated. Dr. Berry asserts that if the CAISO had made the bilateral purchases of OOM energy directly from the Respondents, the transactions would already have been mitigated to the MMCP. Dr. Berry states that although the CAISO made some OOM purchases from sellers other than the Respondents, most of its OOM purchases were from CERS because Respondents and other sellers would not sell directly to the CAISO.

459. Next, Dr. Berry contends that Dr. Morris incorrectly asserts that the market was competitive. Dr. Berry states that the Commission determined that prices of sales in the CAISO and CalPX markets during the October 2, 2000 through June 20, 2001 period were unjust and unreasonable and mitigated the prices of those sales for all sellers regardless of their location, their costs, or their risk. Dr. Berry states that this was done because the Commission determined that the markets did not work, that sellers had the ability to exercise market power, and that the prices that buyers paid were excessive. Dr. Berry notes that CERS purchased in the same market that the Commission has already found to be dysfunctional. Moreover, Dr. Berry avers that since that time, new information about seller gaming and manipulation has been found.[221]

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[220] Ex. CAT-536.

[221] Dr. Berry cites, among other things, evidence of Enron's manipulation, El Paso Pipeline's exercise of market power, and other CFTC and FERC settlements with a variety of energy suppliers.

460. Lastly, Dr. Berry disagrees with Respondents' assertion that the electricity prices can be explained by market fundamentals. Dr. Berry states that there is documented evidence of seller withholding, gas price manipulation, Enron-style gaming, and tariff violations. Dr. Berry further notes that the Western Energy Crisis ended abruptly when the Commission implemented the West-Wide price cap in June 2001.

### 7. Dr. Romkaew Broehm[222]

461. Dr. Broehm's testimony concerned the allegation that Respondents sold non-firm energy as firm. Because the California Parties do not assert this claim against any of the remaining Respondents, Dr. Broehm's testimony is not summarized below.

### 8. Dr. Robert Reynolds[223]

462. Dr. Reynolds' Rebuttal Testimony responds to various criticisms and statements regarding his direct testimony that have been made by Respondents' experts. First, Dr. Reynolds addresses his econometric and statistical analyses of market power. Second, Dr. Reynolds responds to criticisms of the product and geographic markets that are relevant to the analysis of market power. Third, Dr. Reynolds addresses factual claims made by Respondents regarding how suppliers obtained and exercised market power.

463. Dr. Reynolds contends that the "fixes" proposed by Respondents are either (a) inappropriate because the fixes are themselves flawed and introduce, rather than remove, methodological flaws or (b) inconsequential or irrelevant and do not contradict or change the conclusions.

464. Dr. Reynolds states that Respondents and Trial Staff criticize his analysis because some of the explanatory variables are endogenous, variables that are jointly determined with the dependent variable. Dr. Reynolds contends that any bias resulting from endogeneity in the HHI variable will lead to his results to be understated, not overstated. With respect to the quantity variable, Dr. Reynolds states that even if price influences each firm's quantity, the effect would tend to depress the measured effect of firm quantity in his analysis. Dr. Reynolds avers that after considering the interrelationship between HHI, price, and quantity, the analysis' findings provides even stronger evidence that sellers exercised market power. Dr. Reynolds states that adopting Dr. Savitski's "fix" using Instrumental Variables results in virtually no change to his analysis.

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[222] Ex. CAT-585.

[223] Ex. CAT-631.

465. Dr. Reynolds also addresses criticisms made by Trial Staff witness Dr. Savitski. Dr. Reynolds contends that Dr. Savitski wrongly asserts that the coefficients on the emergency stage variables are not significant because the estimated effects on price of all twelve of the emergency stage coefficients have the expected positive correlation. With respect to the use of hourly data instead of transaction data, Dr. Reynolds states that Dr. Savitski provides no alternative analysis to support his criticism. Dr. Reynolds further avers that he used a common statistical technique, referred to as "clustered standard errors," to correct for any exaggeration in the precision of the results.

466. Next, Dr. Reynolds answers criticisms of his product and geographic market definition. Dr. Reynolds argues that if the product and geographic markets were as large as Dr. Savitski contends, then the empirically day-of price disparities and higher prices achieved by larger sellers would not be possible because competition from non-day-of products or from suppliers in more remote areas of the WECC would have constrained the prices. Similarly, Dr. Reynolds states that if Dr. Savitski's larger product and geographic markets were accurate, the estimated effects of the HHI variable on CERS price would be near zero, which was not the case.

467. Dr. Reynolds further argues that his statistical analyses are a more accurate way to determine market power effects than the use of market shares (based on a product and geographic market) because it is direct evidence that the firm is harming competition. Dr. Reynolds notes that federal courts agree that market share is not a threshold showing that must be made prior to determining market power. Rather, market share is only one way of estimating market power. Dr. Reynolds states that the Federal Trade Commission and Justice Department have stressed that direct evidence of competitive effects is important.

468. Dr. Reynolds also disagrees with Dr. Savitski's claim that his product market is too narrow. Dr. Reynolds states that Dr. Savitski misinterpreted his analysis and that his analysis splits the day-of and day-ahead into two separate markets. Dr. Reynolds states that this was appropriate because there were no good substitutes for day-of power given CERS's shortfalls in procuring energy in the day-ahead market and the unanticipated demand that occurs only in the day-of market.

469. Next, Dr. Reynolds responds to Respondents claims that they did not execute an agglomeration strategy when selling energy to CERS. With respect to Coral's assertion that its pricing is not reflective of market power, but of on-peak versus off peak sales, Dr. Reynolds states that he conducted statistical tests and found that even within each of the on-peak and off-peak groupings, Coral realized higher prices for larger quantities sold. Dr. Reynolds also states that limited availability of credit is simply one condition that allowed Respondents to exercise market power.

470. With respect to claims that Dr. Reynolds did not use the hub and spoke market power test that was employed by the Commission at the time, Dr. Reynolds states that

(1) an empirical examination (regression analysis) of pricing during the CERS Period demonstrates that sellers did exercise market power; (2) the hub and spoke test is a "predictive test" to examine future effects and Dr. Reynolds is examining past behavior; (3) the Commission stopped using the hub and spoke test in November 2001 because it "no longer adequately protects customers"; and (4) the hub and spoke test relies on generation capacity and has little relevance to marketers.

471. Lastly, Dr. Reynolds responds to claims that CERS exercised buyer market power. Dr. Reynolds notes that buyer market power occurs when an entity can reduce price by reducing the quantity it purchased. Here, CERS had an obligation to purchase a sufficient amount of power to meet consumer needs. Therefore, CERS did not have the option of reducing its overall purchases.

### 9. Dr. Peter Berck[224]

472. Dr. Berck's Rebuttal Testimony responds to Trial Staff witness Ms. Radel's testimony that the State of California's decision to finance the costs of alleged overcharges by Respondents and other sellers negated any burden imposed by the prices paid by CERS during the CERS Period. Dr. Berck states that the fact that the state found it necessary to issue the bonds to finance a non-capital item of past expense for wholesale electricity is, in itself, extraordinary and a strong signal that the burden of wholesale costs during the CERS Period was not reasonable.

473. Dr. Berck argues that Ms. Radel's approach incorrectly assumes that the burden of any principal amount, regardless of size, can be rendered reasonable or eliminated altogether if the payment plan is stretched out long enough to make the individual payments small. Dr. Berck states that the economic burden of payments made over time, no matter how small, is the present value. Dr. Berck notes that the Office of Management and Budget uses this "net present value" concept in evaluating costs and benefits.

474. Dr. Berck further notes that bonds are commonly used to spread out the costs of capital projects to better match the burden to the beneficiaries (because the benefit of a project occurs over time). Dr. Berck contends that Ms. Radel errs in not recognizing the difference between capital assets and one-time expenditures.

475. Lastly, Dr. Berck contends that Ms. Radel wrongly focuses on the individual customer impact of the $1.05 billion in alleged overcharges still at issue instead of the totality of the economic impact. Dr. Berck notes that the overall negative impact on the

[224] Ex. CAT-636.

California economy had the Respondents' overcharges been passed through in 2001 would have been substantial.

### 10. Mr. Jim McIntosh[225]

476. During the CERS Period, Mr. McIntosh worked for the CAISO as Director, Grid Operations and was in charge of the CAISO Control Room. Mr. McIntosh's rebuttal testimony responds to claims that CERS had access to non-public transmission and market information through CERS employees that were stationed on the CAISO Control Room floor.

477. First, Mr. McIntosh states that CERS employees were present at the ISO because CERS became responsible for acquiring the necessary energy to meet the CAISO's real-time balancing needs. However, Mr. McIntosh notes that CERS did not know how much energy the ISO needed from hour to hour, and in what locations. Therefore, ISO dispatchers had to work closely with CERS personnel who were purchasing imbalance energy each hour in order to make certain that the ISO acquired the amount of energy it needed. Mr. McIntosh states that having to make numerous phones calls to an offsite CERS trader would have created undue stress in achieving the WSCC scheduling deadlines.

478. Next, Mr. McIntosh describes a typical day at the CAISO during the CERS Period. The ISO performed a forecast each day of the likely "net short" of the IOUs for the following day and provided that forecast to CERS personnel at the ISO, who in turn communicated it to CERS day-ahead traders located at CERS headquarters in Sacramento. The CERS day-ahead traders would then attempt to acquire supplies to fill the net short on a day-ahead basis. The second activity involved purchasing the remaining net short during each operating hour. ISO personnel would determine what energy likely would be available from the BEEP Stack (virtually none in January 2001), and then quantify an amount for each hour that would need to be purchased out-of-market bilaterally. ISO personnel would provide CERS personnel, who were stationed at the ISO, a list of potential sellers, and the CERS personnel would proceed to call everyone on the list until the imbalance energy need for that hour was filled. Mr. McIntosh notes that there were usually only a handful of sellers willing to transact with CERS.

479. Mr. McIntosh states that there needed to be instantaneous communication between ISO dispatchers and CERS personnel as the hour of operation approached to make sure that the ISO was getting the energy that it needed at the locations that it needed it. Mr. McIntosh describes this process as an "hour to hour" fight to get the required

[225] Ex. CAT-641.

supplies, noting that for the first days of the CERS Period, the ISO announced rolling blackouts, and for the first month of the CERS Period, the ISO declared Stage 3 Emergencies every single day.

480. Next, Mr. McIntosh argues that CERS's access to the ISO floor did not give CERS an advantage in trading. Mr. McIntosh acknowledges that by necessity, CERS personnel had information about how much energy the ISO needed to buy in any given hour to balance the market. However, Mr. McIntosh notes that sellers got similar information to the extent they were contacted by the ISO or CERS to find out how much energy the seller was willing to sell and at what price. Mr. McIntosh states that CERS personnel were not provided and could not acquire information that other market participants did not have. Mr. McIntosh further notes that the ISO did not view CERS to be a separate "market participant" in any typical sense; rather, the CERS personnel were acting as an extension of the ISO because the sellers were refusing to sell to the ISO.

481. Mr. McIntosh avers that any information that was not provided to all market participants would be deemed confidential. This information included details about transmission outages and derates and generation outages. Additionally, market information in the form of BEEP Stack bid details and the output of the congestion management system was under the control of Mr. Alaywan, who addresses the highly restricted access to this information in his testimony.

482. Mr. McIntosh also describes the processes in place to prevent access to confidential information. Mr. McIntosh notes that in general, the CERS personnel located at the ISO were too busy to do anything other than make calls to purchase the energy. Even so, Mr. McIntosh states that he took steps to position CERS personnel in a way that they were not centrally located and could not easily observe the displays and monitors of information manned by ISO personnel. Mr. McIntosh states that CERS personnel were only allowed access within the Control Room at their desks and were not allowed to move about the control room or contact ISO employees, expect for the purpose of scheduling power. The ISO and CERS entered into a formal nondisclosure agreement so that in the unlikely event that CERS personnel acquired any information that was non-public, they were sworn to treat it as confidential and not use it for any purpose.

483. Mr. McIntosh states that he is not aware of any instance in which CERS personnel gained access to non-public information. Thus, assertions that CERS had a negotiating advantage based on proprietary information are inaccurate.

### 11. Mr. Ziad Alaywan[226]

484. Mr. Alaywan was the Managing Director of Engineering and Operations from 1999 until 2001, and Director, Market Operations from 2001 through 2005 at the CAISO. Mr. Alaywan's testimony responds to claims that CERS had access to confidential ISO information and that CERS could control and/or influence the ISO dispatch of its BEEP Stack.

485. Mr. Alaywan states that at the beginning of the CERS Period he and his staff had frequent interaction with CERS individuals to acclimate them to the ISO processes for acquiring OOM energy. Later in the period, and especially after the Commission's April 2001 order requiring ISO purchases be supported by a credit-worthy buyer, Mr. Alaywan's primary interactions were with CERS managers to ensure that the ISO's purchases had CERS's financial backing.

486. Mr. Alaywan notes that he and Mr. McIntosh were jointly responsible over the functions handled in the ISO Control Room. Mr. Alaywan and his staff were responsible for making sure the ISO acquired resources from the market in accordance with the ISO Tariff and calculating the cost associated with that procurement.

487. Mr. Alaywan states that the ISO did not provide confidential information to CERS during the CERS Period. Mr. Alaywan notes that the ISO considered the following types of information confidential – market bidding information for the Energy and Ancillary Services and congestion management information across the three markets (day/hour-ahead and real-time). Mr. Alaywan states that the access to the electronic bids was password protected and only a handful of ISO staff had access. Additionally, no grid management personnel had access to the information.

488. Mr. Alaywan notes that access to the prices the ISO paid for OOM energy was also considered confidential, but unlike the bids, OOM purchases were not done electronically. Rather, OOM purchases were a telephone discussion between the buyer and the seller. A manual recording of the transaction was entered into the ISO system to perform the settlements for accounting purposes. Typically, OOM information included (1) the amount and time of the energy to be delivered; (2) the name of the seller; and (3) the cost. Mr. Alaywan states that CERS typically had access to this information because CERS was making the purchase themselves. Further, Mr. Alaywan notes that because CERS had to back ISO transactions, CERS would typically know this information in order to pay the bill.

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[226] Ex. CAT-643.

489. Mr. Alaywan states that CERS did request non-public information from the ISO, but that with one minor exception, CERS was not given the information. Mr. Alaywan states that after the April 2001 Order, the ISO requested that CERS be the creditworthy backer for ISO purchases from the BEEP Stack and for ISO OOM purchases. CERS expressed a willingness to make that commitment as long as it had a clear understanding of the costs it was being asked to back and the price of BEEP Stack and OOM purchases that the ISO itself planned to make. CERS also requested ISO forecasts of net shortages of generation for the upcoming operating hour. After CERS made this requests, Mr. Alaywan states that the ISO informed the market and FERC and began an internal process on how to proceed. After negotiations with CERS, the ISO began providing limited information on June 25, 2001, after the close of the CERS Period in this proceeding.

490. Mr. Alaywan acknowledges that CERS did receive some BEEP Stack information in April, May, and June 2001 in order to ensure that CERS was willing to back the purchases. Mr. Alaywan notes that the ISO would provide CERS the total number of megawatts the ISO needed to purchase for a given hour and the total cost the ISO expected it to be.

491. Mr. Alaywan asserts that CERS did not gain a market advantage during the CERS Period because of information it received from the ISO was "highly aggregated" information, and only given after April 2001. Mr. Alaywan states that CERS paid extraordinarily high prices for power in its bilateral purchases and that fact demonstrates that CERS was not in a position to dictate price. Mr. Alaywan notes that the price of power paid by CERS increased each month from January through April. Additionally, the price-cost markup in the real-time energy market was highest in the Spring of 2001.

492. Moreover, Mr. Alaywan states that the non-public information received after the CERS Period was not the information that could easily be used to affect market outcomes. Rather, CERS was trying to reconcile its role as creditworthy backer of the ISO's purchases with its fiduciary obligation under the statute that created CERS to purchase energy on behalf of California ratepayers at a reasonable cost.

### P. <u>The City of Seattle, Washington Rebuttal Testimony for the Section 206 Claims</u>

493. The City of Seattle, Washington submitted rebuttal testimony in response to the Respondents' answering testimony. Seattle submitted the testimony and exhibits of two witnesses.

### 1. Mr. Phillip Hanser[227]

494. Mr. Hanser's rebuttal testimony addresses Respondents' Answering Testimony regarding three issues: (1) whether sellers in the Western market engaged in actions that violated the FPA, Commission regulations, seller tariffs, or the WSPP Agreement; (2) whether those violations affected the prices paid by Seattle; and (3) whether the prices had a burden on Seattle's consumers.

495. Mr. Hanser asserts that Respondents' answering testimony fails to rebut his conclusion that Respondents charged Seattle an unlawful market-based rate. Mr. Hanser states that these unlawful market-based rates directly affected the prices charged to Seattle for energy.

496. Mr. Hanser also contends that Respondents wrongly allege that he improperly relies on the expert testimony of other witnesses in other proceedings. Mr. Hanser states that he has adequate qualifications to perform the same analyses himself and in fact, participated in many of the other proceedings. Mr. Hanser asserts that the Commission does not require him to repeat these analyses. Mr. Hanser admits that he did not conduct an examination of individual transactions. However, Mr. Hanser argues that it is unnecessary because he is relying on analyses of other witnesses who examined the Respondents' market-based rates.

497. With respect to PSCo's assertion that the Commission has not exerted jurisdictions over "bookout" transactions, Mr. Hanser states that the Commission has not refused to assert jurisdiction. Mr. Hanser states that there is no economic reason why "bookouts" should be treated differently because Seattle paid the same unlawful price even if energy did not physically move.

498. Next, Mr. Hanser notes that he defined "spot sale" as (1) any sale that lasts one month or less and (2) any sale that is longer than one month, but less than one year and not part of the buyer's long-term planning process. Mr. Hanser states that this is the definition adopted by Trial Staff earlier in this proceeding. Mr. Hanser argues that the Respondents' definition is based on the definition from the California Refund Case, which ignores differences between the California and Pacific Northwest markets. However, Mr. Hanser admits that he did not attempt to determine which sales conform to this definition, but states that Seattle's Transaction Reporting Template identifies all spot purchases made by Seattle.

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[227] Ex. SCL-76.

499. Mr. Hanser also contends that Respondents' own Answering Testimony contains evidence of unlawful actions by sellers in the Western energy markets. Mr. Hanser states that Professor Hogan submitted the 10-year Coordinated Plan Summary prepared by the WECC, which included average on-peak prices for COB and Mid-C from April 1999 through December 2001. Mr. Hanser contends that this data confirm that wholesale prices rose dramatically and that prices were not the result of market fundamentals because the data show that the reserve margins were within the acceptable range needed to ensure reliability. Moreover, Mr. Hanser states that the data demonstrate that although there was a water shortage, there were still sufficient hydroelectric resources to serve all loads. Mr. Hanser further notes that Professor Hogan admitted at deposition that tight supply conditions need not exist for market power in the form of withholding to occur. Mr. Hanser argues that Professor Hogan's testimony demonstrates that in this type of dysfunctional market, load serving entities, like Seattle, were price takers and did not have the ability to bargain for lower prices.

500. Mr. Hanser also avers that Professor Hogan incorrectly asserts that the high prices were caused, in part, by a shift from hydroelectric to combustion resources. Mr. Hanser notes that Professor Hogan provided no evidence that shows the power purchased by Seattle was produced by combustion generators. Mr. Hanser further argues that Professor Hogan's conclusion is based on the fact that supplies were tight. However, Mr. Hanser states that many sellers were manipulating the natural gas market at the time. Mr. Hanser also asserts that the dysfunction in the California organized markets allowed sellers the opportunity to manipulate the market.

501. Next, Mr. Hanser contends that the testimony of Ms. Mattern further supports his allegations. Mr. Hanser notes that at deposition, Ms. Mattern admitted that the market price was too high, and on occasion, Avista lowered the price of energy to CERS. Mr. Hanser argues that because Avista knew that prices were inflated, Avista also knew that the market was dysfunctional.

502. Mr. Hanser also contends that there is no merit to Respondents' attempt to justify their unlawful rates based on Seattle's actions as a seller in the market. Mr. Hanser notes that Seattle's sales are not regulated by the Commission under the FPA and Seattle did not have a market-based rate tariff. Thus, Mr. Hanser contends that it is inappropriate to compare Respondents' regulated rates with Seattle's unregulated rates.

503. Next, Mr. Hanser asserts that Respondents failed to rebut his conclusion that unlawful actions by sellers in the Western energy markets directly affected the price Seattle paid for energy. Mr. Hanser notes that Professor Hogan admits that the Western markets are interconnected, further supporting his conclusion that the California market prices affected prices in the Pacific Northwest.

504. Mr. Hanser also states that Respondents incorrectly claim that the cointegration analysis does not show that the spot prices in California relate to the prices paid by

Seattle. With respect to Respondents' argument that the analysis did not control for market fundamentals, Mr. Hanser asserts that the purpose of the cointegration analysis was not to demonstrate a causal relationship between market dysfunction in California and wholesale prices in the Pacific Northwest. Rather, Mr. Hanser states that the cointegration analysis demonstrates that prices in the Pacific Northwest followed the same long-term pattern as prices in California. Therefore, controlling for market fundamentals would not be a meaningful exercise. Mr. Hanser states that the cointegration analysis merely confirms the Commission's previous statements concerning the relationship of prices in the Pacific Northwest and California.

505. Mr. Hanser also contends that Respondents wrongly claim that the cointegration analysis is not valid because of differences between the California organized markets and the Pacific Northwest bilateral market. Mr. Hanser argues that the analysis shows the statistical relationship of prices between the two markets, and therefore, the differences between the markets do not affect his conclusions. Mr. Hanser notes that no Respondent challenged the data or equations that he used in his analysis.

506. Lastly, Mr. Hanser states that Respondents' Answering Testimony fails to rebut his conclusion that Seattle's customers were unduly burden by the prices paid by Seattle. Mr. Hanser contends that Respondents wrongly claim that the high prices to consumers were the result of poor water conditions and Seattle's resource planning. Mr. Hanser notes that the reserve margins during the relevant period were within the acceptable range to insure reliability and therefore, there were adequate resources to serve load.

507. With respect to Seattle's resource planning, Mr. Hanser asserts that Seattle acted prudently based on the historical prices and load leading up to the 2000-2001 period. Specifically, Seattle attempted to take steps to mitigate price impacts on consumers. Mr. Hanser notes that once the prices in the Pacific Northwest began to skyrocket, there was nothing Seattle could do to further hedge against the price volatility. Mr. Hanser further notes that the prices in 2000 and 2001 were unique and the result of sellers' unlawful behavior.

508. Mr. Hanser also avers that Seattle was unable to negotiate lower prices in bilateral contracts because Seattle was a price taker during the period and had an obligation to serve load regardless of cost. Mr. Hanser notes that Respondents also paid similar prices for power.

### 2. Mr. Wayne Morter[228]

509. Mr. Morter is currently the Director of Power Management for Seattle City Light. Mr. Morter's testimony rebuts Respondents' claims regarding (1) the definition of "spot" sales; (2) Seattle's identification of specific sales between Respondents and Seattle; and (3) the exclusion of "bookout" transactions.

510. First, Mr. Morter states that "spot" sales should include (1) all sales of one month or less and (2) sales longer than one month, but less than one year, if the sale was not part of the buyer's long-term planning process. Mr. Morter notes that Respondents use the same definition used by the Commission in the California Refund Case, but ignore differences between those two proceedings. Mr. Morter states that Seattle's definition is supported by previous testimony and briefs submitted in this proceeding by Commission Trial Staff. Mr. Morter states that this definition is also based on his experience in the Pacific Northwest spot market.

511. Second, Mr. Morter describes the bilateral transactions between Seattle and Respondents. Mr. Morter submitted a transaction template that contains the sales information. Mr. Morter notes that this information was first submitted by Seattle in 2001 and then resubmitted as part of Seattle's "Statement of Claims" in August 2012.

512. Third, Mr. Morter responds to PSCo's claim that "bookouts" should be excluded from this proceeding. Mr. Morter states that there are no economic reasons why "bookouts" should be treated differently in this proceeding.

## Q. PPL Montana, LLC and PPL EnergyPlus, LLC Surrebuttal Testimony for the Section 206 Claims

513. On June 20, 2013, PPL filed the surrebuttal testimony and exhibits of Ms. Rosemarie Spear.[229] Ms. Spear's surrebuttal testimony responds to the transaction reporting template filed by Seattle witness Mr. Morter in his rebuttal testimony.

514. Mr. Spear states that Seattle's transaction template contains several errors. First, the data indicate that nearly every PPL-Seattle transaction had a delivery location of "BPA." Mr. Spear states that for almost all of PPL's sales to Seattle the actual delivery point was not within BPA's system, but at an intertie to the BPA system from an adjacent system or within another transmission system. Ms. Spear states that ninety-eight percent

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[228] Ex. SCL-81.

[229] Ex. PPL-7.

of the deliveries identified by Seattle occurred at locations that are hundreds of miles from Mid-C and COB and that only one transaction is correctly identified as having a delivery point of "BPA."[230]

515. Second, Ms. Spear states that the transaction template does not identify individual contracts, but rather is just a listing of hourly deliveries. Nor does the template include information on when the contract was entered into. Ms. Spear notes that Seattle and PPL entered into three forward contracts, and deliveries pursuant to those contracts are listed in the Seattle template.

516. Lastly, Ms. Spear notes that the average prices PPL charged Seattle were comparable to the average prices at which Seattle sold energy to PPL, including instances where Seattle charged higher prices.

### R. Constellation Energy Commodities Group, Inc. Surrebuttal Testimony for the Section 206 Claims

517. On July 30, 2013, Constellation filed the surrebuttal testimony and exhibits of Mr. Thomas Q. Marlatt.[231] Mr. Marlatt's surrebuttal testimony responds to the transaction reporting template filed by Seattle witness Mr. Morter in his rebuttal testimony.

518. Mr. Marlatt states that Seattle's transaction template contains several errors. Mr. Marlatt asserts that the data state that nearly every Constellation-Seattle transaction had a delivery location of "BPA." Mr. Marlatt notes that for several transactions, Constellation's data show that delivery did not even occur in the Pacific Northwest market. Mr. Marlatt states that his understanding of these discrepancies is that power may have been sourced elsewhere and delivered to Seattle in the Pacific Northwest. The transactions may also reflect one-half of power trading transactions that were sourced at different points.

519. Next, Mr. Marlatt states that the transaction template does not identify individual contracts, but rather is just a listing of hourly deliveries. The template does not include information on when the contract was entered into. Mr. Marlatt asserts that he modified the transaction template based on Constellation's data and provided the underlying

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[230] However, Ms. Spear notes that the volume of the transaction is misstated by Seattle's template because it was part of an aggregated delivery at two different points (35 MWh at Mid-C and 30 MWh at Hot Springs).

[231] Ex. CCG-14.

transaction data and delivery point. Based on this review, Mr. Marlatt identifies certain transactions that are not even spot-market transactions because a number of hourly deliveries were done pursuant to month-long forward contracts.

520. Additionally, Mr. Marlatt notes that the average prices Constellation charged Seattle were comparable to the average prices at which Seattle sold energy to Constellation. Mr. Marlatt notes that the comparison does not take into account a variety of factors that may affect price.

521. Lastly, Mr. Marlatt notes that Seattle's transaction template includes "bookout" transactions where no power actually flowed. Mr. Marlatt contends that these "bookouts" must be taken into consideration as offsets because Seattle received offsetting revenue for these sales.

### S. The City of Seattle, Washington Direct Testimony for the Section 309 Claims

522. On March 12, 2013, the City of Seattle, Washington (Seattle) submitted its direct testimony. Seattle submitted the testimony and exhibits of two witnesses.

#### 1. Mr. Wayne Morter[232]

523. Mr. Morter's testimony (1) provides Seattle's definition of "spot" sales; (2) identifies specific purchases made by Seattle from the Respondents; and (3) describes "bookout" transactions and explains why Seattle is entitled to refunds for these transactions.

524. Mr. Morter states that "spot" sales should include (1) all sales of one month or less and (2) sales longer than one month, but less than one year, if the sale was not part of the buyer's long-term planning process. Mr. Morter states that this definition is based on his experience in the Pacific Northwest market.

525. Mr. Morter notes that his definition is broader than the one used by the Commission in the California Refund Case, but differences between the two markets justify different definitions. Mr. Morter asserts that unlike California, the sales in the Pacific Northwest market are arranged through bilateral negotiations. Additionally, Mr. Morter states that load serving entities in the Pacific Northwest rely more heavily on hydropower, which is subject to variations that are felt for longer periods of time. Because these variations last longer, the need for wholesale power extends beyond the single hour or single day. Moreover, Mr. Morter notes that LSEs that rely on hydropower

[232] Ex. SCL-95.

attempt to avoid exposure to the spot market, but still make longer term resource planning decisions based on water forecasts. Therefore, Mr. Morter concludes that these longer term transactions serve the same balancing function as the day-ahead and hour-ahead transactions in California. Lastly, Mr. Morter states that his definition is the same definition used by Trial Staff earlier in this proceeding and is consistent with (although not the exact same) the definition used by BPA and the Department of Interior.

526. Next, Mr. Morter states that he has provided nine exhibits (one for each Respondent) which contain the relevant information about Seattle's spot purchases during the Section 309 Period. Mr. Morter states that the accuracy of the spreadsheets was confirmed using invoices provided by Respondents. With respect to the delivery point designation of "BPA," Mr. Morter states that it means that power was delivered to Seattle at a point on BPA's transmission network. Mr. Morter notes that Seattle did not have transmission rights on other networks that would have allowed it to receive power at other locations.

527. Lastly, Mr. Morter asserts that Seattle properly included "bookout transactions." Mr. Morter first notes that the Commission has distinguished "bookouts" from purely financial transactions. Mr. Morter contends that if Seattle's counterparty sold energy to Seattle as part of a "bookout" at an unlawful rate, Seattle would be harmed.

### 2. Mr. Phillip Hanser[233]

528. Mr. Hanser's direct testimony addresses the following issues: (1) the relationship between prices in California and prices in the Pacific Northwest market; (2) whether sellers charged Seattle prices that violated section 205 of the FPA; (3) whether unlawful acts by sellers adversely impacted the prices that Seattle paid; and (4) whether Seattle and the public interest were harmed by the sellers' unlawful prices.

529. Mr. Hanser first describes the Pacific Northwest market. Mr. Hanser notes that during the relevant period, a variety of wholesale power products were bought and sold using bilateral contracts. Mr. Hanser notes that many of these bilateral contracts were made pursuant to the WSPP Agreement. Conversely, in California, most energy was sold in the organized markets. Mr. Hanser notes that only if there was insufficient energy in the organized markets did the CAISO make bilateral purchases (OOM Purchases).

530. Mr. Hanser states that because of the strong transmission interties throughout the Western Interconnect, the Pacific Northwest and California markets have historically taken advantage of a trading relationship where energy is sent north in the winter and

[233] Ex. SCL-110.

south in the summer. Mr. Hanser asserts that the interties also result in a strong relationship between wholesale power prices in California and the Pacific Northwest.

531. Mr. Hanser states that he compared wholesale peak prices in California with prices in the Pacific Northwest and found that it was visually evident that the prices moved together. Based on this visual inspection, Mr. Hanser concludes that Pacific Northwest prices are "strongly linked" to prices in California and driven by the same underlying "price drivers." Mr. Hanser states that this conclusion is supported by the Commission's Staff Report from November 2000.

532. Mr. Hanser also discusses the relationship between day-ahead and month-ahead prices. Mr. Hanser notes that the overall shape of the price curves are the same, indicating that the day-ahead and month-ahead prices "moved" together and were driven by the same factors. Therefore, Mr. Hanser concludes that if the day-ahead prices were the result of market dysfunction, the month-ahead prices were also influenced by the dysfunction.

533. Next, Mr. Hanser alleges that during the Section 309 Period, Respondents charged Seattle rates that are unlawful under section 205 of the FPA. Mr. Hanser states that the Commission requires prices charged pursuant to market-based rate authority to be within the "zone of reasonableness" based on the seller's marginal costs. Mr. Hanser notes that the Commission's view is that competitive forces in a functioning market will put downward pressure on prices and prevent a seller without market power from charging excessive prices. Mr. Hanser asserts that the Commission has made clear that prices that exceed the "zone of reasonableness" indicate that the seller has acquired market power and, as a result, the seller's prices are unjust and unreasonable under the FPA.

534. To determine if a Respondents' price was within the "zone of reasonableness," Mr. Hanser compared the average monthly price of power to Seattle with two competitive benchmarks: (1) the Mitigated Market Clearing Price (MMCP) used by the Commission in the California Refund Case and (2) a "surrogate" marginal cost of the pivotal unit (Pivotal Unit Benchmark) based on natural gas prices and data provided by Energy Velocity. With respect to the MMCP, Mr. Hanser notes that because he calculated monthly averages, he could not use the granular MMCP data. Therefore, Mr. Hanser calculated a monthly average MMCP.

535. Based on a comparison to the MMCP, Mr. Hanser finds that from May 2000 through December 2000 nine Respondents sold power to Seattle at average prices that were above the MMCP. Mr. Hanser further contends that the fact that a seller's average price was below the MMCP during one particular month does not mean that Seattle was not harmed that month because individual transactions may have been higher. Additionally, Mr. Hanser notes that the monthly average used may understate prices paid by Seattle because it includes long-term contract deliveries. Mr. Hanser concludes that

each of the Respondents sold power to Seattle at anticompetitive prices above the MMCP.

536. Mr. Hanser also compares the Respondents' prices to the Pivotal Unit Benchmark. Mr. Hanser notes that the Pivotal Unit Benchmark is generally much higher than the MMCP, suggesting that it is a conservative estimate. Using this benchmark, Mr. Hanser finds that from May 2000 through December 2000, eight Respondents sold at prices below this benchmark. However, Mr. Hanser argues that this result underestimates the premiums charged by Respondents because the Pivotal Unit Benchmark is influenced by sellers' manipulative behavior. For example, Mr. Hanser notes that the Commission has already found that sellers parked power in the Pacific Northwest to drive up California prices, which influenced this benchmark to be higher than it would have been absent the manipulation.[234] Mr. Hanser states that the fact that the prices are close to the Pivotal Unit Benchmark under these circumstances indicates that sellers exercised market power when transacting with Seattle.

537. Next, Mr. Hanser argues that unlawful acts by sellers drove prices above just and reasonable levels. Mr. Hanser first states that his prior testimony discusses unlawful acts by sellers. Mr. Hanser further notes that the price spikes during the summer of 2000 were caused by withholding acts by large generators and exchange transactions that exacerbated the problem. Mr. Hanser cites his own prior testimony in the "100 Days of Discovery" in the California Refund Case as evidence of seller withholding. Mr. Hanser avers that these findings were corroborated by other witnesses in this and other proceedings.

538. Mr. Hanser further notes that some sellers, including some Respondents, took advantage of capped CAISO prices to purchase energy and then resold the energy in OOM transactions without a price cap. Mr. Hanser contends that this activity helped lead to the insolvency of the CalPX markets and California's IOUs. Specifically, Mr. Hanser alleges that TransAlta bought thousands of megawatts in the CalPX and then resold the energy back to California at high prices. Mr. Hanser states that by being an indirect seller, firms avoided reporting sales above the price cap. Therefore, Mr. Hanser concludes that sellers, such as TransAlta, contributed directly to the collapse of the California power markets.

539. Mr. Hanser states that he also conducted a statistical cointegration analysis to demonstrate that prices in the Pacific Northwest and California were linked and driven by the same fundamentals. Mr. Hanser's analysis finds that prices at Mid-C were

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[234] Although this behavior occurred in California, Mr. Hanser states that because the prices are cointegrated, the behavior affected the Pacific Northwest prices.

cointegrated with prices at COB and prices at both COB and Mid-C were cointegrated with prices at NP-15. Therefore, Mr. Hanser concludes that the prices paid by Seattle were driven by the same fundamentals, including market dysfunction and unlawful behavior, as the prices in California.

540. Lastly, Mr. Hanser alleges that the prices paid by Seattle seriously harmed Seattle and the public interest. First, Mr. Hanser repeats his prior testimony concerning the large costs that Seattle incurred in the wholesale markets. Mr. Hanser notes that as a result of the high prices, Seattle City Light passed five separate rate increases in 2001 for an average rate increase of forty-two percent. Additionally, the Seattle City Council passed another 10.3 percent increase based on BPA's transmission rates. Mr. Hanser notes that these increases were significantly higher than the last time Seattle was forced to increase rates.

541. Second, Mr. Hanser asserts that the high prices impacted Seattle's retained earnings because Seattle had to draw down its retained earnings and eventually issue revenue bonds to pay for power. Mr. Hanser states that the revenue bonds also resulted in significant underwriting and related costs. Moreover, Mr. Hanser notes that the Seattle's credit rating declined, causing the cost of credit to increase. Mr. Hanser further states that the high prices also impacted the regional economy, estimated to be in the billions of dollars.

### T. Avista Energy, Inc. (Avista Energy) Answering Testimony for the Section 309 Claims

542. Avista Energy's Answering Testimony responds to claims asserted by the City of Seattle. Avista Energy presented the testimony and exhibits of one witnesses, Mr. Lloyd C. Reed.[235] Mr. Reed's testimony responds to Seattle witnesses with regard to Avista Energy's bilateral sales to Seattle during the Section 309 Period. Generally, Mr. Reed notes that Seattle made no specific, or even general, allegations of Federal Power Act section 309 violations against Avista Energy with regard to any of its bilateral sales to Seattle.

543. Mr. Reed first notes that Avista Energy was a marketing and trading company and did not own any generating assets in 2000. Avista Energy bought and sold energy and assisted customers in the WECC to optimize the value of their generating assets while reducing their risk exposure in markets for electricity.

[235] Ex. AVE-12.

544. Next, Mr. Reed asserts that the transaction data filed by Seattle contains a list of all of Avista Energy's sales, including many transactions that are not spot sales, but rather hourly deliveries made by Avista Energy to Seattle under monthly term and quarterly term transactions.[236] Based on Avista Energy's transactional database, Mr. Reed states that Avista Energy made 32,382 MWh of spot sales to Seattle in the Pacific Northwest markets during the Section 309 Period, with an associated gross revenue of $2,317,641.50. Mr. Reed states that these sales occurred on 586 separate hours and had an overall weighted average price of $71.57/MWh.

545. Mr. Reed argues that Mr. Morter wrongly relies on Commission Trial Staff's prior definition of spot sale in this proceeding. Mr. Reed states that the Commission has subsequently defined spot sale in other cases, including one involving the Pacific Northwest market. Moreover, Mr. Reed states that the process by which Seattle made purchases in the wholesale market is not relevant to the power products that are traded. Mr. Reed asserts that Mr. Hanser implicitly recognizes this in his cointegration analysis because he uses two distinct power products. Additionally, Mr. Reed notes that Mr. Morter failed to define all the terms in his definition, such as "long-term planning process." Lastly, Mr. Reed contends that Mr. Morter's definition of "spot sale" leads to illogical results because the same transactions can be both a "spot" and "non-spot" transaction based solely on the buyer's motives.

546. Mr. Reed also avers that Mr. Morter wrongly claims that LSEs manage their water resources by purchasing power several days and months in advance. Rather, Mr. Reed argues that LSEs' wholesale purchase decisions are driven by continuous risk managing strategy. Therefore, Mr. Reed avers that it is incorrect to analyze particular transactions individually to determine if they are part of a "long-term planning process."

547. Further, Mr. Reed states that Mr. Morter wrongly claims that monthly purchases are the most economical and lowest risk means for meeting load demands. Mr. Reed notes that in some cases day-ahead or hour-ahead prices may be lower (or higher) than the month-ahead prices. Moreover, Mr. Reed avers that Mr. Morter ignores that fact that some LSEs, including Seattle, also sell wholesale power.

548. Mr. Reed states that in general, the prices Seattle paid are comparable to the prices Avista Energy paid because both parties sold energy at the prevailing market price. Mr. Reed notes that there were periods of time (including the exact same hours) when

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[236] Mr. Reed defines a spot sale as a sale for a period of twenty-four hours or less, and entered into on the day of or the day prior to delivery. Mr. Reed states that his definition is consistent with the Commission's prior definition and is the commonly accepted definition in the Pacific Northwest power industry.

Seattle's prices to Avista Energy were significantly higher than Avista Energy's prices to Seattle. Mr. Reed further notes that Seattle does not address the issue of whether its sales in the Pacific Northwest market should be subject to refund.

549. Specifically, Mr. Reed notes that Avista Energy had 78,710 MWh of spot purchases from Seattle during the Section 309 Period, with an associated gross cost of $2,950,306.50. These purchases occurred on 1,430 separate hours and had an overall weighted average price of $37.48/MWh. Thus, Mr. Reed argues that Seattle's implication that it was only a purchaser of wholesale power is inaccurate. Mr. Reed further notes that for on-peak hours, the average price charged by Seattle was $345.58/MWh whereas the average price charged by Avista Energy was only $132.84/MWh.

550. Next, Mr. Reed asserts that Mr. Hanser makes no specific section 309 allegations against Avista Energy. Rather, Mr. Hanser makes general allegations against "sellers" for manipulative activity in the California markets. Additionally, Mr. Reed notes that Mr. Hanser's testimony implies that Seattle is seeking refunds for all sales, including those with prices as low as $13/MWh.

551. Mr. Reed further contends that the figures comparing prices at COB, NP-15, and Mid-C do not support Mr. Hanser's claim that the prices behaved "almost identically." Mr. Reed argues that by including data outside the Section 309 Period, Mr. Hanser visually compresses the relevant data and makes it more difficult to accurately compare prices during the Section 309 Period.

552. Next, Mr. Reed addresses Mr. Hanser's claim that prices at Mid-C are a "good proxy for prices Seattle paid." Mr. Reed notes that Mr. Hanser fails to provide any support for this statement even though the prices Seattle actually paid for energy were available to him.

553. Mr. Reed also disagrees with Mr. Hanser's conclusion, based on the cointegration analysis, that prices in the Pacific Northwest were affected by the events in California. Mr. Reed first notes that Mr. Hanser failed to demonstrate a link between a specific violation by a specific seller and a particular transaction. Second, Mr. Reed states that Mr. Hanser did not incorporate any actual Seattle purchase data in his analysis. Third, Mr. Reed contends that Mr. Hanser wrongly based his analysis on "broker-supplied" quotes for monthly term sales at Mid-C because Mr. Hanser fails to demonstrate how these quotes relate to Avista Energy's actual sales to Seattle. Mr. Reed notes that Mr. Hanser did not attempt to establish that Seattle actually purchased power at the quote price or the *Power Markets Week* price that he used in his analysis. Fourth, Mr. Reed states that Mr. Hanser only used "on-peak" quotes even though only sixty-six percent of Avista Energy's sales to Seattle were during "on-peak" hours.

554. Despite these flaws, Mr. Reed states that he is not surprised that Mr. Hanser found that prices in California and the Pacific Northwest are generally related. Mr. Reed notes that the Commission has recognized this fact. However, Mr. Reed contends that the cointegration analysis does not demonstrate causation effects between the two markets.

555. Lastly, Mr. Reed addresses Mr. Hanser's MMCP Benchmark and Pivotal Unit Benchmark analyses. Mr. Reed first notes that these types of analyses are outside the scope of this proceeding because they do not link a seller's particular violation with particular contracts. Rather, Mr. Hanser's analyses merely try to show that the prices were too high generally. Mr. Reed contends that selling power at a "high" price is not itself a section 309 violation. Mr. Reed notes that the WSPP Agreement contains no price restriction (or margin restriction) for entities with market-based rate authority. Nor did the WSPP Agreement require sellers to set their price at their marginal costs.

556. With respect to Mr. Hanser's MMCP Benchmark, Mr. Reed states that it is flawed because it is based on pricing data outside the Section 309 Period. Moreover, Mr. Reed argues that using monthly averages has the potential to significantly bias the outcome because (1) Avista Energy's sales occurred in varying volumes and at varying prices and (2) using a simple average (instead of a weighted average) wrongly emphasizes low volume sales. Mr. Reed further contends that Mr. Hanser uses price data that includes non-spot sales from Avista Energy.

557. With respect to the Pivotal Unit Benchmark, Mr. Reed states this analysis contains the same flaws as the MMCP analysis. Additionally, Mr. Reed contends that Mr. Hanser included only six of the fifteen balancing authority areas in the Pacific Northwest and does not explain why some balancing authority areas were included and others were excluded. Additionally, Mr. Reed notes that the data used by Mr. Hanser does not include any units placed into service before 1990. Moreover, Mr. Reed states that the Pivotal Unit Benchmark analysis actually supports Respondents. Mr. Reed notes that Avista Energy's sales to Seattle were $44.70/MWh below the benchmark.

### U. Avista Corporation d/b/a Avista Utilities Answering Testimony for the Section 309 Claims

558. Avista Utilities' Answering Testimony responds to claims asserted by the City of Seattle. Avista Utilities presented the testimony and exhibits of one witnesses, Ms. Kimberly Mattern.[237] Generally, Ms. Mattern states that Seattle's direct testimony does not contain any allegations against Avista Utilities and no allegations of wrongdoing with respect to any particular Avista Utilities spot sale to Seattle.

[237] Ex. AVI-67.

559. First, Ms. Mattern provides general background information on Avista Utilities. Avista Utilities is a state-regulated load-serving utility based in Spokane, Washington, serving parts of eastern Washington, northern Idaho, and southern and eastern Oregon. As a state-regulated load-serving utility, Avista Utilities' primary function is to supply power to the retail customers in its service territory, managing its costs through a portfolio of resources.

560. Next, Ms. Mattern responds to the testimony submitted by Mr. Hanser. Ms. Mattern first notes that Mr. Hanser provides analyses and testimony concerning events outside the Section 309 Period. Ms. Mattern also states that Mr. Hanser does not make any allegation of a violation of the FPA or an applicable tariff by Avista Utilities. Ms. Mattern contends that Mr. Hanser simply claims that all Respondents sold power at prices outside the "zone of reasonableness." Ms. Mattern characterizes this claim as merely asserting that prices were too high.

561. Ms. Mattern next describes Avista Utilities' relationship with Seattle. Ms. Mattern notes that Seattle and Avista Utilities were regular counterparties who bought and sold energy with each other. Avista Utilities and Seattle also engaged in non-spot transactions like monthly and quarterly term sales. Ms. Mattern states that Avista Utilities sold Seattle 36,688 MWh of spot power at a total cost of $3,509,440.00, and at an average price of $95.66/MWh. Ms. Mattern states that the prices reflected prevailing market conditions and were generally on par with the prices of other Respondents. Ms. Mattern states that during the Section 309 Period, Seattle sold Avista Utilities 21,078 MWh of spot power at a total cost of $1,746,802.25, and at an average price of $82.87/MWh. Ms. Mattern contends that the fact that Seattle bought more power than Avista Utilities demonstrates that Seattle knowingly accepted certain risks by relying on the spot market for power.

562. Ms. Mattern notes that during the Section 309 Period, Avista Utilities recognized the market volatility and tried to balance its portfolio and minimize risk. Therefore, Avista Utilities minimized its activity on the spot market. Ms. Mattern states that when Seattle requested power, Avista Utilities would try to find resources to help the neighboring control area.

563. Next, Ms. Mattern addresses Mr. Hanser's MMCP Benchmark analysis. Ms. Mattern contends that Mr. Hanser improperly uses monthly averages even though the MMCP is based on hourly increments. Ms. Mattern further argues that Mr. Hanser improperly includes Respondents' non-spot sales. Ms. Mattern notes that the MMCP was specifically calculated for use in the California organized markets and was derived eight years after the fact. Therefore, Ms. Mattern avers that traders would not have considered the MMCP (or the Pivotal Unit Benchmark) when making trading decisions.

564. With respect to the Pivotal Unit Benchmark, Ms. Mattern states that Mr. Hanser improperly included monthly and quarterly term sales. Therefore, because Avista

Utilities sales to Seattle between May and December 2000 were the only "true" spot sales, Ms. Mattern states that it is not surprising that Avista Utilities' prices were higher than the benchmark. Ms. Mattern further notes that many of Avista Utilities' sales to Seattle occurred when supplies were extremely limited and Seattle was badly in need of power.

565. Ms. Mattern also contends that Mr. Hanser's Pivotal Unit Benchmark analysis is flawed because (1) it does not include January to April of 2000; (2) Mr. Hanser uses a simple average instead of a volumetric average; and (3) the benchmark is based on all hours even though some sellers may have only sold during peak periods. Ms. Mattern argues that these flaws skew the results toward a finding that Avista Utilities charged more that the benchmark. Ms. Mattern corrected for these errors and found that Avista Utilities' price was below the benchmark.

566. Ms. Mattern also responds to Mr. Hanser's claim that the prices harmed the public interest. Ms. Mattern notes that Avista Utilities and other LSEs were also affected by the scarcity and price spikes. Ms. Mattern states that had it sold power to Seattle at lower prices, those costs would have been passed on to its customers. Ms. Mattern further notes that Avista Utilities had an obligation to sell power at the highest price it could get.

567. Next, Ms. Mattern responds to the Direct Testimony of Mr. Morter. First, Ms. Mattern states that Mr. Morter wrongly defines "spot sale." Ms. Mattern states that Mr. Morter's definition is at odds with the understanding of market participants, noting that real-time and day-ahead sales are arranged by real-time and day-ahead schedulers, respectively. Ms. Mattern further argues that Mr. Morter's definition is vague and turns entirely on the intentions of the purchasing party because it is based on the buyer's "long-term planning process." Mr. Mattern notes that market participants like Seattle and Avista Utilities routinely analyze and adjust their portfolios due to evolving market conditions. Ms. Mattern states that the effect of including Avista Utilities' non-spot sales to Seattle during the Section 309 Period is to increase the value of sales from $3,509,440 to $4,643,838.50.

568. Additionally, Ms. Mattern contends that the bilateral nature of the Pacific Northwest market does not justify Mr. Morter's definition. Ms. Mattern notes that Mr. Morter does not explain how the differences in the market support a different definition. Rather, Mr. Morter simply notes the differences and concludes that a different definition is appropriate. Similarly, Ms. Mattern states that the reliance on hydroelectric power does not support changing the definition of spot sale.

569. Lastly, Ms. Mattern notes that Mr. Morter did not include any allegation of a violation by Avista Utilities of the FPA or of an applicable tariff.

## V. Cargill Power Markets, LLC Answering Testimony for the Section 309 Claims

570. Cargill's Answering Testimony responds to claims asserted by the City of Seattle. Cargill presented the testimony and exhibits of one witnesses, Mr. David Toole.[238] Mr. Toole's testimony responds to allegations made by Seattle in their Section 309 direct testimony.

571. Mr. Toole states that Cargill is a power marketer that did not own any generation or transmission facilities during the Section 309 Period. Mr. Toole states that the Pacific Northwest spot market generally operated through bilateral sales under the terms and conditions of the WSPP Agreement. Mr. Toole notes that this is different from the California spot market, which had a centralized power exchange and utilized a market clearing price.

572. Mr. Toole states that a "spot market" transaction is a transaction for twenty-four hours or less and that is entered into the day of or the day prior to delivery. Mr. Toole notes that this definition is consistent with the Commission's definition used in the West-Wide price mitigation order. Mr. Toole states that his definition is also consistent with the trading practices that are widely established in the industry.

573. Next, Mr. Toole asserts that Mr. Hanser makes no allegation that Cargill violated either a filed tariff or a specific statutory requirement under the Federal Power Act. Mr. Toole avers that Seattle also failed to make any specific allegation with respect to a particular sale during the Section 309 Period. Mr. Toole notes that Mr. Hanser identified unlawful activity in a different market – California – and did not allege that Cargill engaged in any of the unlawful activity. Moreover, Mr. Toole notes that Seattle failed to discuss any particular contracts or negotiations of those contracts.

574. Mr. Toole states that Mr. Hanser only makes a generalized allegation that all Respondents sold energy at unlawful prices based on his MMCP and Pivotal Unit Benchmarks. With respect to the MMCP analysis, Mr. Toole states that there is no reason to believe that the benchmark established for the California markets is applicable to the Pacific Northwest market. Rather, Mr. Toole notes that Mr. Morter, another Seattle witness, admitted that there were fundamental differences between California and the Pacific Northwest markets. Thus, Mr. Toole concludes that there is no reason to conclude that Cargill's prices were unjust and unreasonable based on the MMCP Benchmark.

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[238] Ex. CPM-2.

575. With respect to the Pivotal Unit Benchmark, Mr. Toole states that Mr. Hanser concluded that Cargill sold power at prices above the benchmark in only one month and the average price from May 2000 to December 2000 was $22.91/MWh less than the benchmark.

576. Next, Mr. Toole states that Mr. Hanser should have considered Seattle's role in negotiating the bilateral spot market purchases. Mr. Toole notes that Seattle had the opportunity to negotiate the price down and was not forced into entering into contracts. Mr. Toole states that Cargill was often a "price taker" in dealings with Seattle, meaning that Cargill would accept the price asked for by the Seattle trader.

577. Further, Mr. Toole states that Seattle willingly accepted the risks associated with its resource management strategy. By relying on average generation, Seattle was required to make significantly more spot market purchases in low water years, particularly 2000.

578. Lastly, Mr. Toole states that Seattle's claim that Cargill's prices were unlawfully high is based on a determination that Cargill's market-based rate authority should not have been in effect. However, Mr. Toole notes that Seattle makes no claim that Cargill exercised market power during the Section 309 Period.

### W. Constellation Energy Commodities Group, Inc. Answering Testimony for the Section 309 Claims

579. Constellation's Answering Testimony responds to claims asserted by the City of Seattle. Constellation presented the testimony and exhibits of one witnesses, Mr. Thomas Q. Marlatt.[239] Mr. Marlatt's answering testimony responds to allegations made in the direct testimonies of Mr. Wayne L. Morter and Mr. Philip Q. Hanser on behalf of the City of Seattle. Mr. Marlatt also provides a transaction template that details the relevant terms of transactions between Constellation and Seattle during the Section 309 Period.

580. First, Mr. Marlatt summarizes the transactions between Seattle and Constellation during the Section 309 Period. Mr. Marlatt states that his data include sales by Seattle to Constellation, as well as Constellation's sales to Seattle. Mr. Marlatt avers that the prices charged by Seattle were similar, and in some cases exceeded, the prices charged by Constellation. Mr. Marlatt further notes that during the Section 309 Period, Seattle sold more energy to Constellation than it purchased from Constellation.

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[239] Ex. CCG-12.

581. Mr. Marlatt states that the data provided by Mr. Morter is inaccurate and misleading. Mr. Marlatt asserts that Mr. Morter's data contain only hourly deliveries and not individual contracts or transactions. Moreover, the data do not include a specific delivery point, only indicating that energy was delivered at some point on the BPA system. Mr. Marlatt states that Constellation's data confirm that the overwhelming majority of transactions between Seattle and Constellation occurred at the Mid-C and COB delivery points. Mr. Marlatt notes that there were five transactions that show delivery at Palo Verde. However, Mr. Marlatt states that this likely means that energy was sourced at Palo Verde and delivered in the Pacific Northwest market.

582. Mr. Marlatt states that the precise delivery location is important because transaction costs can vary substantially depending upon the location where the power was sourced for delivery to Seattle and where on BPA's extensive system it was delivered. Mr. Marlatt states that the delivered pricing used by Mr. Morter would reflect transmission related costs. Mr. Marlatt further contends that Constellation's data are more accurate because the price of power often depends on the particular product that was purchased. Mr. Marlatt notes that because Mr. Morter only included hourly deliveries, there is no way to derive what product was actually purchased.

583. Lastly, Mr. Marlatt discusses the benchmark analyses conducted by Mr. Hanser. Mr. Marlatt asserts that Mr. Hanser wrongly used a monthly average MMCP benchmark rather than comparing the hourly prices. Additionally, Mr. Marlatt states that the prices charged by Seattle on its sales to Constellation significantly exceed the MMCP benchmark in each month.

## X. El Paso Power Marketing Company, LLC Answering Testimony for the Section 309 Claims

584. El Paso's answering testimony responds to claims asserted by the City of Seattle. El Paso presented the testimony and exhibits of one witnesses, Mr. Dennis Price.[240] Mr. Price responds to the direct testimony filed by Seattle concerning the Section 309 Period.

585. Mr. Price first describes El Paso's role in the Pacific Northwest market. Mr. Price states that El Paso held modest interests in generation facilities throughout the United States, but none in the Pacific Northwest.[241] Rather, El Paso was primarily a marketer of

[240] Ex. EP-2.

[241] Mr. Price notes that during the Section 309 Period El Paso made no sales in the Pacific Northwest market for generation it had an interest in.

purchased power, buying energy for the sole purpose of reselling it. El Paso did not purchase power for its own use or for service of any native load. Mr. Price also notes that El Paso did not own any interest in any electric transmission facilities.

586. Mr. Price states that El Paso's transactions in the Pacific Northwest market were done pursuant to its market-based rate authority. Mr. Price further notes that between the time El Paso was granting market-based rate authority and the relevant period, no changes occurred that would have altered the Commission's conclusion that El Paso could not exercise market power in the Pacific Northwest market. Mr. Price also asserts that El Paso did not engage in any activity in violation of its market-based rate tariff and the conditions imposed on El Paso by the Commission.

587. Next, Mr. Price states that the proper definition of spot market is transactions for twenty-four hours or less prescheduled no more than twenty-four hours in advance. Mr. Price states that Mr. Morter's definition conflicts with his first-hand experience in the Pacific Northwest market and with the Commission's definition. Mr. Price notes that spot market is not defined with respect to a particular buyer's long-term planning process. Mr. Price states that the distinction between a spot market contract and a forward contract is the amount of time a buyer has to transact in order to balance or match its resources and obligations. Spot market transactions are the result of an event which requires action "immediately" to balance or match available resources to actual obligations and should not be relied upon to address predictable events.

588. Mr. Price states that the entities to which El Paso sold power had numerous competitive alternatives, noting that El Paso regularly won and lost sales with other marketers. Mr. Price states that the fact that Seattle is alleging claims against numerous Respondents demonstrates that Seattle had alternatives to El Paso. Thus, Mr. Price concludes that El Paso could not set the price for power.

589. Mr. Price also notes that Seattle sold power to multiple counterparties at similar and sometimes higher prices during the Section 309 Period. Specifically, Seattle sold 20,000 MWh to El Paso during January 2000 at $29.60/MWh, which is higher than the $24.00/MWh price that El Paso charged for energy deliveries to Seattle in January 2000.

590. Next, Mr. Price asserts that the spreadsheet submitted by Mr. Morter does not identify specific bilateral contracts. Rather, the spreadsheet contains a list of hourly deliveries pursuant to a variety of transactions. Moreover, Mr. Price asserts that the spreadsheet includes deliveries that were not made pursuant to a spot market transaction. Rather, nearly all the deliveries were done pursuant to monthly contracts.

591. Mr. Price further avers that at the time, there were no allegations that spot market contract prices in the Pacific Northwest were affected by illegal or manipulative actions taken by sellers. Moreover, Mr. Price notes that Seattle has not made any specific

allegation that El Paso engaged in unlawful conduct that affected particular contracts or that El Paso engaged in any unlawful actions in the Western markets generally.

592. Lastly, Mr. Price states that there is no basis for ordering refunds in this proceeding. Mr. Price contends that parties freely engaged in bilateral contracts in a competitive environment. Mr. Price argues that ordering refunds will introduce regulatory risk and disincentivize market participation, leading to higher prices.

### Y. PPL Montana, LLC and PPL EnergyPlus, LLC Answering Testimony for the Section 309 Claims

593. PPL's Answering Testimony responds to claims asserted by the City of Seattle. PPL presented the testimony and exhibits of one witnesses, Ms. Rosemarie Spear.[242] Ms. Spear's answering testimony responds to allegations made by Mr. Morter and Mr. Hanser in their direct testimony.

594. First, Ms. Spear states that Seattle's transaction template is inaccurate. Ms. Spear notes that the template is a list of hourly deliveries to Seattle from various sellers, but does not include the underlying transaction information. Additionally, Ms. Spear asserts that the template wrongly identifies "BPA" as the delivery point. Ms. Spear states that most of PPL's sales to Seattle occurred at boundary of the Montana Power Company Control Area.[243] Ms. Spear notes that the data submitted in Docket No. PA02-2 confirms that only 3,397 MWh were delivered at Mid-C (in the BPA). Ms. Spear states that many of these deliveries were resales at Mid-C. Moreover, contrary to Mr. Morter's statement, Ms. Spear asserts that it would have been possible for Seattle to either purchase transmission from locations outside BPA or accept delivery of energy at the intertie of the BPA transmission system and another transmission system.

595. Next, Ms. Spear argues that Mr. Morter's definition of "spot sale" is incorrect. Based on her experience, Ms. Spear states that spot market transactions are uniformly understood to include only day-ahead or real-time transactions, consistent with the WECC pre-scheduling calendar and hourly scheduling practices and timelines. Ms. Spear notes that Mr. Morter's definition is dependent on the intention of the party purchasing power and that individual market participant's long-term planning processes are not transparent to the rest of the market. Therefore, there is no way for a seller to know if it is engaged in a spot market transaction.

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[242] Ex. PPL-10.

[243] PPL's generation is interconnected to the Montana Power Company Control Area.

596. Ms. Spear avers that because Mr. Morter did not include the contract information in his database, the database includes sales that are not spot market transactions. Ms. Spear notes that PPL entered into a term forward contract with Seattle during the Section 309 Period.

597. Ms. Spear also states that PPL did not and could not have engaged in unlawful market activity. Ms. Spear notes that Seattle has not alleged nor presented any evidence that PPL engaged in conduct that violated their market-based rate authority or any tariff or otherwise manipulated the Pacific Northwest bilateral spot market. Moreover, Ms. Spear states that "Enron manipulation strategies" involved bidding in California's organized markets and are not relevant to the bilateral contracts in the Pacific Northwest. Ms. Spear further notes that PPL never bought energy from the CAISO or from sellers within the CAISO control area, never received any congestion revenues, never sold non-firm energy as firm, and never submitted false schedules. Lastly, Ms. Spear asserts that PPL could not have exercised market power because it had only a limited amount of excess energy available to sell into competitive wholesale energy markets because of its full requirements contracts with the Montana Power Company.

### Z. Public Service Company of Colorado Answering Testimony for the Section 309 Claims

598. PSCo's Answering Testimony responds to claims asserted by the City of Seattle. PSCo presented the testimony and exhibits of one witnesses, Mr. Thomas Imbler.[244] Mr. Imbler's testimony responds to allegations made by City of Seattle.

599. Mr. Imbler first states that much of Mr. Hanser's Section 309 Direct Testimony relies on the same analyses as his Section 206 Direct Testimony. Therefore, Mr. Imbler incorporates the criticisms found in his Section 206 Answering Testimony.

600. Next, Mr. Imbler contends that the proper definition of "spot market" includes sales for twenty-four hours or less that are entered into the day of or the day prior to delivery. Mr. Imbler notes that this definition is consistent with the Commission's definition in the June 19, 2001 Order (West-Wide price mitigation order). Mr. Imbler further states that this definition reflects trading practices that are widely established in the industry. Conversely, Mr. Imbler contends that Seattle's proposed definition is inherently flawed. Mr. Imbler asserts that Seattle's reliance on transactions that are "critical" to load balancing is flawed because Mr. Morter could not identify any transaction that was not critical for load balancing. Moreover, Mr. Morter acknowledged that transactions of six months or even one year would be critical to balancing load.

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[244] Ex. PSC-4.

601. Mr. Imbler also argues that Seattle failed to demonstrate that PSCo violated a filed tariff or a specific provision of the FPA. Mr. Imbler states that Mr. Hanser failed to make any specific allegation against PSCo and admitted at deposition that he is not alleging that PSCo engaged in unlawful market activities. Rather, Mr. Hanser acknowledged that he makes only a generalized allegation that all Respondents sold energy at unlawful prices based on his Benchmark Analyses.

602. Mr. Imbler states that PSCo had authority to charge market-based rates during the period and that authority was not conditioned on PSCo charging prices at or near either the MMCP or Pivotal Unit Benchmark. Mr. Imbler argues that Mr. Hanser essentially converts market-based rate authority into a capped-rate tariff. Mr. Imbler further notes that PSCo exceeded the MMCP Benchmark in only six months during the Section 309 Period by an average of only $38.06/MWh.

603. Moreover, Mr. Imbler contends that the MMCP is not an appropriate benchmark for the Pacific Northwest market because it was developed for California markets. Mr. Imbler notes that Mr. Morter admitted at deposition that there are fundamental differences between the California and Pacific Northwest markets because of the market structure and the Pacific Northwest's reliance on hydroelectric resources. Mr. Imbler notes that these differences caused Mr. Morter to adopt a different definition for "spot sale" in this proceeding.

604. With respect to the Pivotal Unit Benchmark, Mr. Imbler notes that PSCo's prices exceeded this benchmark in only four months during the Section 309 Period, and from May 2000 through December 2000, PSCo's average monthly premium was negative $33.67/MWh. Mr. Imbler further contends that Mr. Hanser's Pivotal Unit Benchmark is flawed because it only includes the marginal costs and does not include an additional fixed costs component. Additionally, Mr. Imbler states that Mr. Hanser failed to consider the risk associated with transactions. Mr. Imbler notes that PSCo often agreed to pay damages if it failed to deliver energy for any reason, including transmission availability.

605. Next, Mr. Imbler argues that Mr. Hanser is essentially claiming that PSCo's market-based rate authority should not have been in effect during the Section 309 Period, and therefore, the sales were unlawful. However, Mr. Imbler notes that at deposition Mr. Hanser admitted that he does not allege that PSCo had or could exercise market power over Seattle or any other purchaser. Mr. Imbler states that in October 2000, PSCo filed a revised market power study and the Commission determined that PSCo lacked market power.

606. Mr. Imbler further avers that Mr. Hanser failed to consider Seattle's own role in negotiating prices during the Section 309 Period. Mr. Imbler notes that Seattle often dictated the price and terms of service in their transactions. Mr. Imbler states that purchasers, including Seattle, had a significant number of options when buying energy, and thus, were able to dictate that the terms of transactions. Additionally, Mr. Imbler

states that the bilateral nature of the transactions means that each party undertook individual risk assessments. Because of these individual assessments, Mr. Imbler contends that the Commission should not go back in time and reset the transaction prices.

607. Mr. Imbler also notes that Seattle failed to consider its sales to PSCo at the same or higher prices. Therefore, Mr. Imbler concludes that it would be inequitable to award refunds to Seattle while allowing Seattle to retain the entirety of their revenue from similarly priced sales.

608. Lastly, Mr. Imbler states that Seattle's resource planning relied on purchases from wholesale markets, particularly when water conditions were "low." Mr. Imbler notes that 2000 and 2001 were historically low water years that required Seattle to purchase more in the wholesale markets than normal. Thus, higher demand in the spot market also contributed to higher prices.

### AA. TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. Answering Testimony for the Section 309 Claims

609. TransAlta's answering testimony responds to claims asserted by the City of Seattle. TransAlta presented the testimony and exhibits of one witnesses, Mr. Wes Harrigan.[245] Mr. Harrigan's answering testimony discusses (1) the state of the market during the Section 309 Period; (2) how market conditions affected TransAlta's trading activity; and (3) how TransAlta's overall trading strategy was influenced by its responsibilities associated with the Centralia Generation Plant.

610. Mr. Harrigan states that the market prior to May 2000 was normal, but as demand began to increase, there were price spikes in California and neighboring regions. Mr. Harrigan notes that after May 2000, the California IOUs did not buy an adequate amount of day-ahead energy and forced the CAISO to purchase OOM energy. Mr. Harrigan states that in the fall and winter, the off-peak prices at Mid-C were high enough to support wheeling power out of the Desert Southwest and SP15 to the Pacific Northwest. Mr. Harrigan notes that this pricing dynamic was consistent with the onset of a drought in an area heavily dependent on hydro power, the Pacific Northwest. Mr. Harrigan asserts that the problem was exacerbated by the fact that California was dependent on imports from the Pacific Northwest markets and that the Pacific Northwest was experience winter peaking.

[245] Ex. TAE-23.

611. Mr. Harrigan next states that as the supply and demand conditions tightened, prices moved higher and higher beyond historical norms and exhibited extreme volatility. Mr. Harrigan speculates that risk managers curbed speculative activities and longer-term products were less available. Rather, sellers focused on trades in the day-ahead and real-time markets.

612. With respect to TransAlta specifically, Mr. Harrigan notes that TransAlta's participation in the market was affected by the acquisition of the Centralia generating plant on May 4, 2000. Mr. Harrigan notes that TransAlta had presold a portion of the output of the Centralia plant through a variety of long-term firm and non-firm contracts. However, if one unit went down, TransAlta lost half its generation and still had obligations to deliver power. TransAlta would be forced to purchase replacement power at much higher prices. Therefore, TransAlta would attempt to hedge against its price risk by making purchases in lower priced markets and reselling the energy if it was not needed.

613. In addition to hedging the Centralia Plant, Mr. Harrigan states that TransAlta would make trades (1) to trade power in conjunction with its transmission rights and (2) for purely speculative purposes. Mr. Harrigan notes that by the end of the Section 309 Period, speculative trades were minimal due to risk limits.

614. Mr. Harrigan also states that the majority of power purchased by TransAlta during this period was pursuant to forward transactions that happened to coincide with the Section 309 Period. Mr. Harrigan asserts that these transactions were entered into with the intent of selling to a higher-priced market in conjunction with transmission rights or to cover Centralia commitments due to a known outage or derate or to mitigate the risk of an unplanned outage. Mr. Harrigan states that TransAlta never had any strategy of buying power in California with the intent of reselling the power as higher priced OOM to the CAISO. Mr. Harrigan states that buying energy from the CalPX, sinking it with Snohomish, and then selling it to the CAISO was efficient for the CAISO because the CAISO regularly had excess generation in the south, but was short in the north. Mr. Harrigan notes that the CAISO would pay Pacific Northwest counterparties who took northbound power at NOB and returned southbound power at COB.

615. Next, Mr. Harrigan states that Mr. Hanser wrongly claims that TransAlta's activities had a large bearing on the financial decline of the IOUs. Mr. Harrigan first notes that TransAlta's activities were very limited and had relatively few exports from California in hours in which it sold OOM energy to California. Mr. Harrigan further notes that Mr. Hanser did not analyze any transaction data. Moreover, Mr. Harrigan contends that TransAlta did not engage in a strategy of buying out of the CalPX at the price caps in order to resell to the CAISO. Mr. Harrigan concludes that the small volumes did not have any impact on the financial welfare of the IOUs.

616. Lastly, Mr. Harrigan discusses TransAlta's transactions with Seattle. Mr. Harrigan states that he reviewed the Seattle transaction data and notes that TransAlta bought power from and sold power to Seattle at similar price levels during the Section 309 Period. Moreover, although much of the data aligns with TransAlta's records, Mr. Harrigan notes that there are some discrepancies. For example, Seattle's data includes all transactions with TransAlta regardless of the delivery point.

### AB. Joint Defense Group Answering Testimony of the Section 309 Claims

617. The Joint Defense Group's[246] answering testimony responds to claims asserted by the City of Seattle. The Joint Defense Group presented the testimony and exhibits of one witnesses, Mr. A. Joseph Cavicchi.[247] Mr. Cavicchi's testimony addresses the following: (1) the definition of spot market transaction; (2) Mr. Hanser's testimony as it relates to the Commission framework for market-based ratemaking; and (3) Mr. Hanser's benchmark pricing comparisons.

618. Mr. Cavicchi defines spot market sales as those for immediate delivery – sales made a day ahead of delivery or on the day of delivery. Mr. Cavicchi states that this definition is consistent with all organized and bilateral electricity markets. Mr. Cavicchi further asserts that the fact that the Pacific Northwest market was a bilateral marketplace does not justify Mr. Morter's definition. Mr. Cavicchi states that every bilateral market that he is aware of defines spot market as sales for immediate delivery. Mr. Cavicchi notes that the Mid-C hub is considered one of the most liquid bilateral trading points in the West. Thus, the Pacific Northwest market has a robust bilateral market that supports spot market sales and is similar to many spot markets both organized and bilateral all over the country.

619. Moreover, Mr. Cavicchi avers that the underlying generation mixture and resource planning process does not define "spot market." Rather, wholesale markets are defined based on the product being traded. Thus, "spot market" refers to the electricity product

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[246] The Joint Defense Group is Avista Energy, Inc. (Avista Energy); Avista Corporation d/b/a Avista Utilities (Avista Utilities); El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.) (El Paso); Exelon Generation Company, LLC, Successor-In-Interest to Constellation Energy Commodities Group, Inc. and Constellation Power Source, Inc. (Constellation); PPL Montana, LLC and PPL EnergyPlus, LLC (PPL); Public Service Company of Colorado (PSCo); and TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. (TransAlta).

[247] Ex. JDG-1.

that has immediate delivery. Mr. Cavicchi contends that Mr. Morter's proposed definition is inherently subjective because it depends on the purchaser's generation asset mixture and long-term planning process. Under Mr. Morter's spot sale definition, if Seattle bought power for delivery in six months as part of its long-term planning process, the purchase would not be a spot market transaction, but if it made the same purchase after learning that one of its generation resources would be shutting down for unplanned maintenance, it would be a spot market transaction. Further, Mr. Cavicchi notes that the seller would have no knowledge of the purpose of the transaction.

620. Mr. Cavicchi also states that advanced purchasing decisions that are not part of long-term planning by load serving entities are not necessarily a consequence of the Pacific Northwest's reliance on hydropower. Rather, these decisions are the result of a variety of factors including unplanned plant outages or required maintenance, weather conditions, load forecasts, and risk management. Mr. Cavicchi notes that these factors are common to all LSEs regardless of their reliance on hydropower.

621. Mr. Cavicchi states that additional facts differentiate spot market transactions from long-term forward transactions. Mr. Cavicchi contends that supply/demand conditions in spot markets cannot be expected to be the same as supply/demand conditions in forward markets. Mr. Cavicchi states that even throughout the course of a day, demand will vary. Therefore, spot market prices may vary from forward market prices depending on specific conditions, such as the weather. Similarly, the supply of energy may vary from the forward markets to the spot markets due to system outages and other operational restrictions.

622. Next, Mr. Cavicchi addresses Mr. Hanser's allegations regarding sellers exercising market power and charging unjust and unreasonable prices. Mr. Cavicchi first notes that the Commission defines market power as the ability of a seller to "significantly influence price in the market by withholding service and excluding competitors for a significant period of time." Mr. Cavicchi states that the applicable standard for determining whether Respondents engaged in unlawful activities, such as the exercise of market power, should be based on the laws, regulations, orders, and tariffs in effect at that time.

623. Mr. Cavicchi states that the market power test used by the Commission in 2000 was the hub and spoke screen. Under this screen, a seller could be found to have market power only if its installed and uncommitted generation capacity in relevant geographic markets is greater than twenty percent. Mr. Cavicchi notes that all members of the Joint Defense Group were found not to possess market power during the year 2000 under the Commission's hub and spoke screening analysis.

624. Mr. Cavicchi notes that Mr. Hanser did not review or analyze the specific contracts for which Seattle is seeking refunds. Rather, Mr. Hanser compared the prices charged to Seattle with two benchmarks: the MMCP Benchmark and the Pivotal Unit Benchmark.

625. With respect to the MMCP benchmark, Mr. Cavicchi states that it is based on the generating units that were operating in California during 2000-2001 and are applicable only to the California organized wholesale markets for the purposes of the Commission's California Refund Proceeding. The Pivotal Unit Benchmark is defined as the highest marginal cost unit located in the Pacific Northwest producing a non-trivial amount of power during each hour of the relevant period. Mr. Cavicchi contends that Mr. Hanser's Pivotal Unit Benchmark analysis assumes (1) that he is able to find an electric generating resource that he asserts was the most expensive resource running in the Pacific Northwest during particular hours and (2) that he can use this resource's supposed operational cost as a benchmark against which he can compare Respondent prices. Additionally, Mr. Cavicchi notes that Mr. Hanser ignores all of the Pacific Northwest bilateral market transaction data when defining his benchmarks even though the Pacific Northwest market prices were an important factor informing buyer and seller decision making at the time.

626. Mr. Cavicchi notes that neither benchmark comparison is a market power analysis. Mr. Cavicchi contends that the Commission has never endorsed such an analysis when analyzing market competiveness. Mr. Cavicchi asserts that the proper market power analysis would have considered the circumstances surrounding the execution of buyers' and sellers' transactions with Seattle and whether the transaction prices were affected by physical or economic withholding of supply. Additionally, Mr. Hanser failed to consider such factors as market share, market concentration, transmission constraints, and other factors that the Commission has assessed under the hub and spoke test and continues to assess under the market power tests in place thereafter.

627. Next, Mr. Cavicchi states that Mr. Hanser's analysis is flawed because Mr. Hanser calculates his supposed marginal cost benchmarks by taking the simple average of the hourly values for each month and compares the price to the weighted average price for Seattle. Mr. Cavicchi notes that Seattle did not purchase power from Respondents every hour, or even most hours, of the year 2000, and that using these averages overstates the difference between average contract prices and the benchmarks (particularly if Seattle tended to buy more power during peak hours).

628. Lastly, Mr. Cavicchi notes that Seattle was also charging comparable, and sometimes higher, spot market prices in its sales to Respondents.

### AC. Section 309 Respondents Answering Testimony for the Section 309 Claims

629. The Section 309 Respondents'[248] answering testimony responds to claims asserted by the City of Seattle. The Section 309 Respondents presented the testimony and exhibits of one witnesses, Professor William Hogan.[249] Professor Hogan responds to allegations advanced by Seattle that the retail rates charged to its customers were increased by the misconduct of sellers and by electricity market dysfunction in the California spot markets during the relevant period. Professor Hogan further notes Mr. Hanser merely repeats allegations of unlawful activity that have appeared elsewhere and conducts no independent analysis. Lastly, Professor Hogan responds to Mr. Hanser's assertion that the prices Seattle paid for electricity during the relevant period imposed an undue burden on Seattle.

630. First, Professor Hogan states that Mr. Hanser did not show that unlawful activity by sellers affected the prices paid by Seattle. Professor Hogan notes that in his experience he has not seen any persuasive evidence or demonstration that widespread misconduct of the type that might have materially affected market prices occurred. Further, Professor Hogan notes that Mr. Hanser conducted no independent analysis of these allegations and only repeats allegations previously filed in this and other proceedings. Moreover, Professor Hogan contends that Mr. Hanser's analysis fails to demonstrate the relationship between alleged unlawful activity and prices paid by Seattle.

631. With respect to Mr. Hanser's cointegration analysis, Professor Hogan notes that this is the same analysis previously conducted by Mr. Hanser and already addressed in Professor Hogan's previously filed testimony. Professor Hogan further notes that Mr. Hanser failed to isolate other factors affecting Seattle's prices, such as low water conditions in the Pacific Northwest. Moreover, Professor Hogan contends that Mr. Hanser's analysis fails to consider that conditions in the Pacific Northwest may have affected prices in California. Lastly, Professor Hogan notes that while cointegration can show the similarity of price behavior in the long run, a cointegrated series may still exhibit temporary departures from their long-term relationship, making cointegration a

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[248] The Section 309 Respondents are Avista Energy, Inc. (Avista Energy); Avista Corporation d/b/a Avista Utilities (Avista Utilities); Exelon Generation Company, LLC, Successor-In-Interest to Constellation Energy Commodities Group, Inc. and Constellation Power Source, Inc. (Constellation); PPL Montana, LLC and PPL EnergyPlus, LLC (PPL); and Public Service Company of Colorado (PSCo).

[249] Ex. NW3-1.

poor choice to assess whether specific incidents of market misconduct in California did or did not affect Pacific Northwest prices.

632. With respect to Mr. Hanser's visual inspection of prices, Professor Hogan states that the graphical data do not support the conclusion that California misconduct affected Pacific Northwest prices. Rather, Professor Hogan asserts that the graphs only demonstrate that prices across the Western Interconnection move together because price is affected by the same market fundamentals.

633. Lastly, Professor Hogan addresses Mr. Hanser's claims of excessive harm. Professor Hogan argues that the difficult economic conditions Seattle faced in the relevant period were the result of many factors, including its own power purchase decisions. In particular, sellers did not cause the low water conditions that required Seattle to rely more heavily on power purchases during peak hours than it had in the past. Additionally, Professor Hogan notes that Mr. Hanser failed to consider the long-term negative impact of abrogating contracts. Professor Hogan asserts that capping electricity prices, especially after-the-fact, can harm consumers in both the short-run and the long-run because providers may be less likely to build new generation.

634. Professor Hogan further states that Mr. Hanser failed to present evidence that price levels during the relevant period led to an excessive burden to consumers "down the line." Professor Hogan notes that Seattle's rates have stabilized since 2002 because of policy decisions made by Seattle. Moreover, Professor Hogan states that consumers benefit from price stability when contracts are maintained and face long-term harm if contracts can be abrogated after the fact.

### AD. Commission Trial Staff Answering Testimony for the Section 309 Claims

635. Trial Staff's answering testimony responds to testimony submitted by the City of Seattle and the Respondents. Trial Staff presented the testimony and exhibits of two witnesses.

#### 1. Ms. Chrystina Steffy[250]

636. First, Ms. Steffy states that Seattle only made general allegations of unlawful market activity and failed to demonstrate any specific violation of the FPA or a tariff, as required by the Commission's Rehearing Order. With respect to Seattle's claims of undue harm, Ms. Steffy contends that other factors, such as Seattle's Resource Planning

[250] Ex. S-23.

and general market conditions, could have led to Seattle's rate hikes and that Seattle failed to analyze which portions of the rate hike are attributed to seller actions.

637. Next, Ms. Steffy states that Commission Trial Staff does not support Mr. Morter's definition of spot market. Rather, Trial Staff is taking no position on the proper definition of sport market. Ms. Steffy states that because Seattle did not support their claims for refunds under any definition, the issue is irrelevant.

638. With respect to the transaction data provided by Mr. Morter, Ms. Steffy asserts that the data only include hourly deliveries and fail to provide necessary information to analyze each transaction or contract. Ms. Steffy notes that the transaction data does not even identify the type of transactions – day-ahead, hour-ahead, balance of month, etc. – or the delivery location. Ms. Steffy further states that Seattle failed to tie any violation by the seller to a specific contract.

639. Ms. Steffy also disagrees with Seattle's inclusion of "bookouts." Ms. Steffy notes that it is unclear how an identical rate offered by two different entities would be unlawful for one entity and not the other when, such as here, the rates being charged are market-based.

640. Next, Ms. Steffy disagrees with Mr. Hanser's assertion that prices in California affected prices in the Pacific Northwest. Ms. Steffy notes that this is the same claim made by Mr. Hanser in his previous testimony and that Ms. Steffy has already responded to these arguments and analyses. Ms. Steffy notes that Mr. Hanser did not demonstrate a specific unlawful activity impacted the bilateral transactions with Seattle and Respondents.

641. Lastly, Ms. Steffy argues that Mr. Hanser failed to demonstrate that a specific seller violated section 205 of the FPA by charging prices outside the "zone of reasonableness." Ms. Steffy notes that there are no Commission or tariff requirements that mandate prices be at marginal costs. Nor has the Commission ever set a specific "zone of reasonableness." With respect to Mr. Hanser's Benchmark Analyses, Ms. Steffy states that she did not analyze these benchmarks because there is no Commission requirement that price be within a specific "zone of reasonableness" based on marginal costs.

### 2. Dr. David Savitski[251]

642. Dr. Savitski responds to allegations made by Mr. Hanser concerning False Exports, withholding, and exchanges. Dr. Savitski notes that Mr. Hanser relies on the testimony of the California Parties witnesses Mr. Taylor and Dr. Berry.

643. First, Dr. Savitski contends that Mr. Hanser wrongly claims that False Exports involved withholding. Rather, Dr. Savitski states that to the extent that False Export even existed, energy was arbitraged across markets. Dr. Savitski avers that energy involved in a False Export is clearly not withheld because it is sold.

644. Moreover, Dr. Savitski contends that Mr. Hanser incorrectly alleges that False Exports increased price. Dr. Savitski states that arbitrage has offsetting effects on price in general, increasing the day-ahead price and decreasing the real-time price. Dr. Savitski contends that Mr. Hanser misleadingly focuses on the export transaction, ignoring the import transaction. Dr. Savitski also notes that Mr. Hanser confuses False Export with false import, which would tend to increase both day-ahead prices and real-time prices because the energy is sold above the price cap.

645. Furthermore, Dr. Savitski states that Mr. Taylor's False Export analysis is largely based on coincidental observations.[252] Dr. Savitski notes that Mr. Hanser presented no independent analysis, and therefore, failed to identify actual specific transactions that involved False Exports.

646. Second, Dr. Savitski states that Mr. Hanser wrongly claims that exchanges exacerbated prices spikes. Dr. Savitski asserts that exchanges, like False Export, moved energy from lower-price locations and times to higher-priced locations and times, and thus ameliorated price spikes. Dr. Savitski further notes that exchanges were entered into by choice and the parties entering into exchanges benefited by the flexibility of the agreements.

647. Lastly, Dr. Savitski notes that exchanges were priced as a barter ratio, which Dr. Savitski states was reasonable. Therefore, there could only be an indirect effect on prices.

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[251] Ex. S-24.

[252] Dr. Savitski discussed flaws in Mr. Taylor's analysis in his February 5, 2013 Answering Testimony and repeats the same criticisms in this portion of his testimony.

### AE. The City of Seattle, Washington Rebuttal Testimony for the Section 309 Claims

648. The City of Seattle, Washington submitted rebuttal testimony in response to the Respondents' answering testimony. Seattle submitted the testimony and exhibits of two witnesses.

#### 1. Mr. Phillip Hanser[253]

649. First, Mr. Hanser addresses claims that his benchmark analyses failed to identify specific spot sales at prices outside the "zone of reasonableness." Mr. Hanser states that he updated his analysis to respond to Respondents' criticisms by using the hourly data for the relevant period and comparing this data to the monthly invoice data used in his direct testimony. Mr. Hanser avers that any discrepancies between the monthly invoice and hourly data were minor.

650. Mr. Hanser also states that he made changes to the calculations of the Pivotal Unit Benchmark regarding the heat rates and gas prices. Mr. Hanser states that these changes were made in direct response to criticisms from Respondent witnesses. Additionally, Mr. Hanser states that he changed the process of calculating both the MMCP and Pivotal Unit Benchmarks in order to account for the hourly data. Therefore, Mr. Hanser asserts that he was able to calculate a premium above the benchmark for each hour of a Seattle transaction.

651. Following these adjustments, Mr. Hanser finds that Respondents charged premiums over the MMCP Benchmark in 11,221 of 15,523 hourly observations and premiums over the Pivotal Unit Benchmark in 5,999 of 15,523 hourly observations. Mr. Hanser states that the percentages are similar to the monthly percentages calculated in his direct testimony.

652. Next, Mr. Hanser responds criticisms that his Benchmark Analyses do not relate to proof of market power. Mr. Hanser states that Respondents wrongly claim that proof of market power obtained through high market shares is necessary. Mr. Hanser notes that the Commission's analyses of Enron and other CAISO market participants demonstrate that other strategic behavior can work to benefit a market participant even in the absence of market power, as defined by the "hub and spoke" test. Mr. Hanser notes that in 2004, the Commission changed its market power analysis to focus on pivotal suppliers. Therefore, Respondents' focus on traditional antitrust principles is not relevant to the behavior in this proceeding. Mr. Hanser states that his Benchmark Analyses demonstrate

[253] Ex. SCL-115.

that Respondents consistently raised their prices above the benchmark and thus, Respondents were "pivotal" in their dealings with Seattle.

653. Mr. Hanser further argues that Respondents' market-based rate authority does not shield them from liability. Mr. Hanser states that he provided proof of systematically high prices charged by Respondents that were outside the zone of reasonableness. Mr. Hanser also notes that because he used only monthly invoices in his direct testimony, the results understate the degree of premiums because they include longer term trades and other transactions with lower premiums.

654. Next, Mr. Hanser responds to claims that he did not properly consider the cost of transmitting energy to Seattle and other the market fundamentals. With respect to transmission costs, Mr. Hanser states that any differential would have been included in Respondents' price and that by not adjusting for the transmission cost, the Benchmark Analyses actually understates the premium.

655. Mr. Hanser also responds to Avista's claim that he should have included all fifteen Balancing Authority Areas (BAA) in his Pivotal Unit Analysis. Mr. Hanser notes that most of these BAAs have hydroelectric resources with little or no fossil-fuel generation, which the Pivotal Unit Benchmark is based on. Thus, excluding these BAAs have little or no effect. Nevertheless, Mr. Hanser revised his analysis to include these BAAs in his Pivotal Unit Benchmark Analysis.

656. Mr. Hanser next responds to claims that his analysis fails to consider market fundamentals, such as lack of hydroelectric resources, high gas prices, and wide pricing variances. Mr. Hanser contends that his benchmark analyses tie in the hourly prices, which were the result of these market fundamentals. Thus, the MMCP and Pivotal Unit Benchmarks are higher as a result of the market fundamentals. With respect to the credit issues during the relevant period, Mr. Hanser notes that credit was a concern for the California Parties, but was not an issue with Seattle. Lastly, Mr. Hanser notes that had he considered non-thermal generation, the Pivotal Unit Benchmark would have decreased due to hydroelectric's low marginal costs.

657. Mr. Hanser also responds to criticisms of the methodology and calculations in his benchmark analyses. With respect to claims that the MMCP is not appropriate for the Pacific Northwest markets, Mr. Hanser states that his cointegration analysis shows that

California and the Pacific Northwest were linked and therefore, the MMCP for California is an appropriate benchmark for the Pacific Northwest.[254]

658. Mr. Hanser states that he made additional changes to his Benchmark Analyses to respond to Respondents criticisms. First, Mr. Hanser increased the threshold of his analysis to twenty megawatt units, which he states is still conservative. Second, Mr. Hanser removed the "simple average" monthly pricing when calculating the multi-month premium. Third, Mr. Hanser removed data from his analyses that was outside the relevant period.

659. With respect to the differences in the Pivotal Unit Benchmark and the lower MMCP Benchmark, Mr. Hanser states that prices above the MMCP Benchmark are the primary indication that the price was outside the zone of reasonableness. Those prices that are higher than the Pivotal Unit Benchmark are particularly high and thus, the Pivotal Unit Benchmark provides further support for his conclusions.

660. Mr. Hanser also argues that the "spot" power transactions should be measured against the marginal costs of fossil fuel units. Mr. Hanser asserts that any other benchmark would ignore the concept of pivotality.

661. Next, Mr. Hanser responds to more general claims raised by Respondents. First, Mr. Hanser contends that Respondents argument that there was a legitimate business purpose in charging the highest prices that they could is not surprising and cannot justify the extremely high prices. Mr. Hanser notes that the extremely high prices can only be justified by extremely high costs. Mr. Hanser contends that the Respondents failed to show that the actual costs, or opportunity costs, justified the high prices.

662. With respect to arguments that Seattle assumed the risk of high prices, Mr. Hanser contends that this argument should be rejected. Mr. Hanser states that the sales from the Centralia Plant should not have exceeded the marginal costs and that his benchmark analyses go to the very question of what price Seattle should have been responsible for. Moreover, Mr. Hanser notes that a "lack of prudence" is not a defense to Seattle's claims. In any event, citing Ms. Green's prior testimony on behalf of the City of Seattle, Mr. Hanser argues that Seattle's resource planning was in fact prudent.

663. Next, Mr. Hanser addresses Respondents' assertion that Seattle charged similar prices in their sales to Respondents. Mr. Hanser contends that Respondents had an

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[254] Mr. Hanser states that criticism of his cointegration analysis primarily goes to individual seller activity and fails to rebut the overall conclusion that the prices in the two markets were linked. Mr. Hanser notes that many Respondent witnesses admit this fact.

opportunity to claim that those prices were outside the zone of reasonableness, but did not do so.

664. Next, Mr. Hanser responds to arguments that Seattle did not properly define "spot sale." Mr. Hanser repeats prior testimony that its definition is consistent with the Trial Staff's definition from earlier in this proceeding. Additionally, Mr. Hanser repeats prior arguments that Respondents' definition does not consider differences between the California markets and the Pacific Northwest, including the resource planning of LSEs. Nevertheless, Mr. Hanser updated his analyses to only include sales as defined by the Respondents.

665. Mr. Hanser also responds to claims that his analyses did not show harm to Seattle. Mr. Hanser asserts that his direct testimony demonstrates that the prices charged by Respondents directly led to increases in retail rates to consumers. Additionally, the unlawful activity and market dysfunction in California increased the costs that Seattle paid for power. Specifically, the following effects were seen: (1) rate increases, (2) loss of retained earnings; (3) the cost of issuing revenue bonds; (4) the increased cost of credit; and (5) general economic loss for the region.

666. Lastly, Mr. Hanser provides a summary of his updated analysis. The MMCP Benchmark Analysis yields a cumulative premium of $25,008,193 across all hour-ahead and day-ahead spot transactions and $2,880,763 for all other spot transactions during the relevant period. The Pivotal Unit Benchmark analysis yields a cumulative premium of $16,915,181 across all hour-ahead and day-ahead spot transactions and $1,205,573 for all other spot transactions during the relevant period.

### 2. Mr. Wayne Morter[255]

667. Mr. Morter responds to criticisms of his definition of "spot sale" and the transaction data provided. Mr. Morter also responds to claims regarding Seattle's ability to negotiate lower prices.

668. First, Mr. Morter states that Respondents wrongly claim that his definition of "spot sale" would result in inconsistent outcomes based on the purchasers' long-term planning process. Mr. Morter notes that many inconsistencies would be alleviated because his definition includes all monthly power transactions as "spot sales." Next, Mr. Morter states that criticisms that he failed to define "long-term planning process" are unwarranted. Mr. Morter notes that LSEs engage in planning processes to meet long-term demand needs and that all LSEs engage in this type of activity. Mr. Morter

[255] Ex. SCL-117.

states that he is surprised that Respondents' expert witnesses seem not to understand this aspect of LSE planning.

669. Mr. Morter also states that Respondents wrongly claim that his definition is subjective because the Commission Trial Staff proposed the exact same definition earlier in this proceeding. Mr. Morter repeats his prior testimony that his definition accounts for the unique characteristics of the Pacific Northwest market. Additionally, Mr. Morter notes that the Commission has never defined spot sale for the purposes of this proceeding. Lastly, Mr. Morter notes that his definition is not intended to comport with the understanding of Respondent traders. Rather, the definition is based on the realities and practices in the Pacific Northwest market.

670. Second, Mr. Morter responds to criticisms of his transaction data. Mr. Morter first notes that no Respondent witness provided contradicting data. Mr. Morter further states that the data he provides is consistent with his definition of "spot sale." With respect to the fact that the data do not include sales made by Seattle to Respondents, Mr. Morter contends that the Commission lacks jurisdiction to order refunds from Seattle. Lastly, Mr. Morter states that because Seattle lacked transmission capacity, no sale in the transaction data would have occurred outside the United States.

671. Third, Mr. Morter states that contrary to Respondents' assertions, Seattle did not have the ability to negotiate with sellers. Mr. Morter notes that Seattle pursued a strategy of purchasing the lowest cost power available and that purchases were generally made at the prevailing market price. Any alternatives would have been at the same or higher prices.

### AF. Joint Defense Group Surrebuttal Testimony for the Section 309 Claims

672. On August 27, 2013, the Joint Defense Group filed surrebuttal testimony and exhibits of Mr. A. Joseph Cavicchi.[256] Mr. Cavicchi's surrebuttal testimony responds to the updated hourly analyses filed by Seattle witness Mr. Hanser in his rebuttal testimony.

673. Mr. Cavicchi first notes that Mr. Hanser updated his benchmark analyses by using hourly data and changing the methodology for calculating premiums. Mr. Cavicchi states that he recalculated Mr. Hanser's "premiums" using (1) actual reported gas market prices instead of "calculated" gas prices and (2) including hourly prices that were both above and below the benchmarks. Mr. Cavicchi states that for the Pivotal Unit Benchmark analysis, making these two changes resulted in the "premium" charged to Seattle to be negative for the entire Section 309 Period.

[256] Ex. JDG-7.

## IV. Burden of Proof and Standard of Review[257]

674. Seattle and the California Parties bear the burden of proof because they are the proponent of an order to abrogate the subject contracts and to require refunds.[258] Further, for the reasons discussed below, the more rigorous application of the statutory "just and reasonable" standard of review, often characterized as the *Mobile-Sierra* "public interest" standard, is applicable to the adjudication of the contracts in dispute between the parties in this proceeding absent a showing that a particular Respondent engaged in "unfair dealing at the contract formation stage,"[259] which "alter[ed] the playing field for contract negotiations,"[260] and had "a causal connection … [to] the contract rate."[261]

675. In *Morgan Stanley*, the Supreme Court clarified that the *Mobile-Sierra* doctrine did not recognize a "public interest" standard separate and apart from the "just and reasonable" requirement of sections 205 and 206 of the Federal Power Act; rather, the doctrine recognized a "differing *application* of the just-and-reasonable standard" in which rates set at arm's-length in bilateral contracts are presumed to be "just and reasonable."[262] Bilateral contracts, such as those at issue in this case, and the rates set in those contracts, are presumed to be "just and reasonable" pursuant to the *Mobile-Sierra* doctrine, as precedent of the Supreme Court and other courts applying the doctrine over its nearly sixty year history confirms.[263]

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[257] The positions of the parties concerning this issue are summarized in the relevant sections *supra*.

[258] 5 U.S.C. § 556(d) (2012) ("[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof" and any sanction imposed must be "supported by and in accordance with reliable, probative and substantial evidence").

[259] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008).

[260] *Id*. at 554; Order on Remand at P 20.

[261] *Morgan Stanley*, 554 U.S. at 555.

[262] *Id*. at 535.

[263] *See, e.g., United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956); *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008). *See also California ex rel. Brown*, 135 FER ¶ 61,178, at P 77 (2011).

676. The *Mobile-Sierra* presumption may be avoided only "where there is unfair dealing at the contract formation stage," for instance in the form of fraud or duress,[264] or where there is a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract.[265] Thus, even where claims are raised that illegal actions of one of the parties to a contract led to the dysfunctional market under which the contract was formed, the Commission must find "a causal connection between unlawful activity and the contract rate" before there will be any forfeiture of the presumption that a contract rate is just and reasonable.[266] Additionally, the presumption may be overcome in "extraordinary circumstances" involving "unequivocal public necessity" where the contract "seriously harms" the public interest or imposes "an excessive burden on consumers."[267]

677. The Supreme Court's recent application of the *Mobile-Sierra* doctrine, in its *Morgan Stanley* decision, came in the context of market-based rates and claims of excessive charges by public utilities. The *Morgan Stanley* decision is directly applicable to Seattle and the California Parties' similar claims here, as the Commission recognized in its Order on Remand.[268] *Morgan Stanley* reviewed the Commission's decision to apply the *Mobile-Sierra* presumption to contract rates entered into between buyers and sellers of wholesale electricity under long-term contracts during the California Energy Crisis.[269] According to the Court, "[a]fter the crisis had passed, buyer's remorse set in and [the buyers] asked FERC to modify the contracts."[270] The buyers contended that the presumption that the contracts were just and reasonable should not apply because the

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[264] *Morgan Stanley*, 554 U.S at 547.

[265] Order on Remand at P 21 (citing *Nev. Power Co. v. Enron Power Mktg., Inc.*, 125 FERC ¶ 61,312, at P 24 (2008)).

[266] *Morgan Stanley*, 554 U.S at 554-55.

[267] *Id.* at 530, 534, 547, 549 n.4, 550; *see also* Order Granting Interlocutory Appeal at P 12.

[268] *See* Order on Remand at P 21.

[269] *Morgan Stanley*, 554 U.S. at 541.

[270] *Id.*

contracts were entered into at a time when rates were substantially higher than historic rates due to circumstances in the California market.[271]

678. Rejecting the buyers' contention and determining that the *Mobile-Sierra* presumption applied to those contracts, the Court instructed: "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law. The presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*."[272] The Court also referred to its holding in *Sierra*, which provided that "only when the mutually agreed-upon contract rate seriously harms the consuming public may the Commission declare it not to be just and reasonable."[273] The Court emphasized that the public interest "is the 'sole concern' in a contract case" when determining whether that contract should be modified.[274]

679. In *Morgan Stanley*, the Court also evaluated and *rejected* the Ninth Circuit's use of a "zone of reasonableness" test based on marginal cost to determine whether a rate was so high as to impose an excessive burden on consumers and thus avoid the *Mobile-Sierra* presumption.[275] Under its test, the Ninth Circuit had equated rates above marginal costs as imposing an excessive burden on consumers.[276] The Court rejected categorically that use of marginal cost as a test of reasonableness because it "fails to accord an adequate level of protection to contracts."[277] The Court further held that:

> [a] presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract based-regulation. We have said that, under the *Mobile-Sierra* presumption, setting aside a contract rate requires a finding of '*unequivocal public necessity*' or '*extraordinary circumstances*'. *In no*

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[271] *Id.*

[272] *Id.* at 530 (emphasis added).

[273] *Id.* at 545-46 (citing *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956)).

[274] *Id.* at 546 n.3.

[275] *Id.* at 548-50.

[276] *Id.* at 550.

[277] *Id.* at 548.

> *way can these descriptions be thought to refer to the mere exceeding of marginal cost.*[278]

680. The Court thus made clear "that the FPA intended to reserve the Commission's contract-abrogation power for those *extraordinary circumstances* where the public will be *severely harmed*,"[279] and that the *Mobile-Sierra* presumption cannot be overcome based upon a theory of "zone of reasonableness," or by reliance upon marginal costs.[280]

681. It is clear that the *Mobile-Sierra* presumption applies to the subject contracts absent a showing that a particular Respondent engaged in "unfair dealing at the contract formation stage,"[281] which "alter[ed] the playing field for contract negotiations,"[282] and had "a causal connection … [to] the contract rate."[283] Seattle and the California Parties acknowledge that all of the transactions for which they are seeking refunds were conducted under the Western Systems Power Pool (WSPP) Agreement. Each of these transactions made under the WSPP Agreement umbrella was bilateral and individually negotiated. Numerous buyers and sellers transacted under the WSPP Agreement, as demonstrated by the list of approximately 200 signatories included with the WSPP Agreement.[284] Further, the Commission has specifically held that the WSPP Agreement demonstrates the "intent that neither seller nor buyer be able to seek changes under section 205 or 206 of the FPA other than under the 'public interest' standard of review."[285] Accordingly, as previously explained, "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and

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[278] *Id.* at 550-51 (emphasis added) (citations omitted).

[279] *Id.* (emphasis added).

[280] *Id.*

[281] *Id.* at 547.

[282] *Id*. at 554; Order on Remand at P 20.

[283] *Morgan Stanley*, 554 U.S. at 555.

[284] Ex. CAT-124 at 108-10 (attachment to WSPP Agreement listing members). *See also* Tr. 3173:2 (Morter) (agreeing that there were "a lot" of WSPP members).

[285] *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at P 36 (2003). *See also* Order on Remand at P 20; Order on Rehearing at P 13.

reasonable' requirement imposed by law."[286] The presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*."[287]

## V. The City of Seattle's Claims

682. The City of Seattle, Washington (Seattle) asserted claims pursuant to section 206 of the Federal Power Act and section 309 of the Federal Power Act. Seattle asserted claims against Avista Corporation d/b/a Avista Utilities (Avista Utilities); Avista Energy, Inc. (Avista Energy); Cargill Power Markets, Inc. (Cargill); El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.) (collectively, El Paso); Exelon Generation Company, LLC (Successor-In-Interest to Constellation Energy Commodities Group, Inc.) (Constellation); PPL Montana, LLC and PPL EnergyPlus, LLC (collectively, PPL); Public Service Company of Colorado (PSCo); Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral); and TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. (collectively, TransAlta). Initial briefs were filed by the parties on December 16, 2013,[288] and reply briefs were filed on January 28, 2014.[289]

### A. Summary of the Position of the Parties

#### 1. City of Seattle, Washington Initial Brief

##### (a) Allegations of Unlawful Activity by Respondents

683. Seattle states that the Commission concluded that the *Mobile-Sierra* presumption "generally applies" to short-term bilateral power contracts like those at issue in this case,[290] and therefore, prices are presumed to be "just and reasonable" within the

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[286] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[287] *Id.*

[288] Seattle and TransAlta filed errata to their initial briefs.

[289] In their post-hearing briefs, Respondents provide substantially similar arguments on numerous issues. Those arguments are not repeated in each summary.

[290] *Puget Sound Energy, Inc.*, 137 FERC ¶ 61,001, at P 20 (2011) (Order on Remand).

meaning of the FPA.[291] Thus, in order to obtain refunds, Seattle must demonstrate that (1) the *Mobile-Sierra* presumption does not apply to the contracts where Seattle is seeking refunds or (2) Seattle has rebutted the presumption with respect those contracts where it does apply.

684. Seattle contends that the *Mobile-Sierra* presumption does not apply to the contracts at issue because Respondents engaged in unlawful activity that directly affected the prices of those contracts.[292] Seattle states that Mr. Hanser conducted econometric and statistical analyses of the wholesale energy markets in the Pacific Northwest and California during the refund period,[293] and concluded: (1) the wholesale energy markets in California and the Pacific Northwest were interconnected with each other and with the other wholesale energy markets in the Western Interconnection;[294] (2) due to these interconnections, in the absence of congestion, wholesale power could be easily transmitted throughout the Western Interconnection at relatively little cost compared to the price of the energy itself;[295] and (3) the difference between the price for wholesale energy at a delivery point in California and the price for that same energy at a delivery point in the Pacific Northwest was generally equal to the cost of transporting the energy between those two delivery points.

685. Seattle states that Mr. Hanser also determined that that during the refund period, the markets for wholesale energy in California and the Pacific Northwest had the same price drivers. Seattle notes that this conclusion is based on the visual inspection of prices at NP-15, COB, and Mid-C,[296] as well as a cointegration analysis.[297]

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[291] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[292] Order on Remand at P 21.

[293] The refund period for this proceeding is January 1, 2000 through June 20, 2001. *See* Order on Rehearing at P 32.

[294] Ex. SCL-110 at 11:4-18.

[295] Tr. 1975:3-19, 2249:10-21 (Hanser).

[296] Ex. SCL-110 at 11-31. *See also* Ex. SCL-79.

[297] Ex. SCL-1 at 25:23-25; Ex. SCL-110 at 68:11-13.

686. Next, Seattle asserts that during the Refund Period, prices for wholesale energy in both the Pacific Northwest and California markets skyrocketed to record highs that far exceeded historical levels. For example, on December 11, 2000, the prices for wholesale power at COB and Mid-C soared to record highs of $3,200 per megawatt-hour and $3,683 per MWh, respectively.[298] Seattle notes that the extremely high prices were not isolated incidents, but the tip of an enormous price spike that began in May 2000 and did not end until June 2001.[299]

687. Seattle avers that the California energy markets were not competitive and were subject to manipulation on an unprecedented scale. Seattle notes that the Ninth Circuit concluded that "the California energy market was subjected to artificial manipulation on a massive scale …."[300] Seattle further states that the Commission has found unlawful acts of manipulation by sellers in the California markets helped drive price for wholesale energy in those markets to unjust and unreasonable levels during the period of October 2, 2000 through June 20, 2001.[301] Seattle notes that the Commission required sellers to refund the difference between the prices they actually charged under their market-based tariffs and the Mitigated Market Clearing Price (MMCP).[302]

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[298] Ex. SCL-76 at 13:9-12. *See also* Tr. 3504:1-18 (Harrigan); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,522 (2001) (Commissioner Massey dissenting).

[299] Ex. SCL-76 at 12:20-23; Ex. PNR-1 at 224, Table 60.

[300] *See California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1014 (9th Cir. 2004).

[301] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275 (2001). Seattle states that the Commission has not yet reached a final decision on whether the prices for wholesale energy in California were also unjust and unreasonable during the period May 1 through October 1, 2000. However, an Initial Decision issued February 15, 2013 found tariff and other violations by sellers that affected prices in California. *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 142 FERC ¶ 63,011 (2013).

[302] The MMCP is calculated for each hour using the marginal costs of the last unit dispatched to meet load in the ISO's real-time market, as adjusted to reflect various inputs. *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120 (2001). Seattle states that the MMCP represents prices that would have been charged for wholesale energy had the market been competitive and not subject to manipulation.

688. Seattle contends that beginning on May 1, 2000 and continuing throughout the refund period, Respondents repeatedly charged Seattle market-based rates for wholesale energy in the Pacific Northwest that exceeded the MMCP.[303] Specifically, during the Section 309 Period, Respondents charged excess prices in over seventy two percent of the observations,[304] exceeding the MMCP by $27,888,956 in total.[305] Seattle argues that the ability to charge prices in excess of the MMCP is clear evidence that Respondents acquired, possessed, and exercised market power.

689. Seattle asserts that by acquiring market power and charging such prices, each Respondent violated its market-based tariff because that tariff was conditioned on Respondent's lack of market power. Seattle notes that in order to obtain a market-based rate tariff, each Respondent had to represent to the Commission that it and its affiliates lacked market power, or had mitigated their market power, so that the prices they charged under a market-based tariff would be limited by the normal workings of a competitive marketplace.[306] In addition, the Commission required each Respondent to make periodic reports to the agency to ensure that the seller did not acquire market power after it had received market-based rate authority.[307]

690. Seattle argues that in acquiring and exercising market power, Respondents also violated Section 205 of the FPA.[308] Seattle states that both the Commission and courts have long held that a market-based tariff is lawful under the FPA only if it produces prices for wholesale power that are "just and reasonable."[309] Seattle contends that when a seller with a market-based tariff acquires market power, the prices produced by its market-based rate are not "just and reasonable."

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[303] Ex. SCL-115 at 46.

[304] *Id.* at 8:18-19.

[305] *Id.* at 45:7-9.

[306] *See, e.g.*, Ex. PSC-6.

[307] *Id.*

[308] 16 U.S.C. § 824d(a) (2012).

[309] *California ex rel. Lockyer v. FERC*, 383 F.3d 1006 (9th Cir. 2004); *California ex rel. Lockyer*, 99 FERC ¶ 61,247 (2002).

691. Next, Seattle addresses numerous assertions made by the Respondents. First, Seattle argues that Respondents wrongly claim that they may charge any price under their market-based rate tariff, even if the market was not competitive and subject to manipulation.[310] Seattle asserts that the FPA mandates that all rates charged for wholesale power by sellers covered by that act must be "just and reasonable" or they are "unlawful."[311] Seattle further notes that the Ninth Circuit explained that the Commission cannot fulfill its duty of ensuring rates are "just and reasonable" by relying on market forces alone.[312] Furthermore, Seattle avers that at oral argument in the *Montana Consumer Counsel* proceeding, Commission staff specifically stated that it was not relying on market forces to insure that market-based rate tariffs produced prices for wholesale energy that were "just and reasonable."[313]

692. Second, Seattle asserts that the Respondents wrongly claim that the MMCP is flawed because of differences between the California and the Pacific Northwest markets. Seattle states that the Commission has already held that all Out of Market (OOM) purchases by the California ISO should be mitigated.[314] Seattle notes that the OOM purchases included contracts with delivery points in the Pacific Northwest.[315] Thus,

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[310] Seattle asserts that Respondents' position cannot be reconciled with the principle that the Commission will not grant a market-based rate tariff to a seller who possesses market power. *California ex rel. Lockyer*, 99 FERC ¶ 61,247 (2002). Seattle states that it is axiomatic that if a seller of wholesale energy can extract from a customer any price that the seller desires, that seller possesses market power.

[311] *Lockyer*, 383 F.3d at 1011.

[312] *Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011) ("FERC may not substitute prevailing market prices for its own judgment").

[313] The Commission staff further stated that it was also relying on its *ex ante* test to make sure a seller did not have market power before it granted the seller's request for market-based rate authority and its constant monitoring of the seller's prices thereafter to make sure the seller did not acquire market power once it had received such authority. *See Mont. Consumer Counsel*, 659 F.3d at 919-20; *see also Lockyer*, 383 F.3d at 1013.

[314] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515-16 (2001); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,178 (2001).

[315] *See* California Parties, Motion Requesting Consolidation and Severance of Specified Proceedings, Docket Nos. EL00-95-000, EL00-98-000, EL01-10-000, *et al.*, at

(continued…)

Seattle contends that the Commission concluded that the MMCP does represent the price that would have been charged in a bilateral contract in the Pacific Northwest if that market had been competitive and not subject to manipulation.[316]

693. Moreover, Seattle contends that the differences cited by Respondents, such as differences in market structure, are not relevant to the issue of whether or not Respondents exercised market power to charge prices that exceeded the prices that could have been charged in a competitive market. Seattle also argues that the MMCP is conservative in favor of Respondents because the MMCP included a ten percent adjustment for credit risk associated with the California markets. Seattle notes that no Respondent claimed that similar credit issues plagued the Pacific Northwest market.

694. Third, Seattle avers that Respondents' argument that Mr. Hanser should have considered prices below the MMCP is contrary to the Commission's criteria for determining the appropriate rate in a competitive market. Seattle states that in the California Refund Case, the Commission rejected various sellers request to reduce their overcharges by their alleged undercharges, noting that the FPA requires all prices for wholesale power must be just and reasonable, not just average prices.[317]

695. Additionally, Seattle states that to the extent Respondents are arguing that they are entitled to refunds from Seattle, Respondents argument is premature because this phase of the case is limited to liability issues. Seattle notes that although the Commission has determined that entities such as Seattle are not subject to refund,[318] Seattle has agreed to voluntarily reduce any refund claims it makes against a Respondent by the amount of refunds Seattle would owe that Respondent if Seattle were subject to the Commission's jurisdiction.

696. Fourth, Seattle argues that Respondents' objections to Mr. Hanser's cointegration analysis are meritless. Seattle notes that no Respondent took issue with the actual

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55 (filed May 22, 2009); *Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1053 (9th Cir. 2006) ("[t]he OOM transactions at issue here were bilaterally negotiated sales of power at different prices than the market clearing price established in the auction market").

[316] *See Pub. Utils. Comm'n of Cal.*, 462 F.3d at 1052-53.

[317] 16 U.S.C. § 824d(a) (2012).

[318] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 121 FERC ¶ 61,607, at P 59 (2007).

calculations performed by Mr. Hanser[319] or provided an alternative model that demonstrated that the prices in California and the Pacific Northwest did not have the same price drivers.[320] Seattle asserts that Respondents' objection based on differences between the wholesale markets in the Pacific Northwest and California reveals a fundamental misunderstanding of the purpose of the cointegration analysis. Seattle states that the cointegration analysis is used determine whether or not two series of numbers have a long-term relationship,[321] and does not depend on the similarities or dissimilarities of the markets involved. Additionally, Seattle avers that the cointegration analysis eliminates any possible bias that could be inherent in other forms of analysis, such as visual inspections, anecdotal evidence, or "gut" feelings. With respect to Professor Hogan's claim that the cointegration analysis is nothing more than a "fancier" correlation analysis,[322] Seattle argues Professor Hogan fundamentally misunderstands this important statistical technique.

697. Fifth, Seattle addresses claims that the MMCP is unfairly based on the same estimated costs for all Respondents, rather than actual costs for each Respondent. Seattle notes that in the California Refund Case, the Commission rejected an almost identical argument, stating that the determination of whether a market is competitive and free from manipulation must be made by looking at the market as a whole.[323] The Commission further noted that the purpose at the liability stage of the proceeding is to determine whether or not the market as a whole is behaving as expected.[324] Seattle asserts that because this stage of the proceeding involves only the question of liability, Seattle does

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[319] Ex. SCL-76 at 26-27.

[320] *Id.*

[321] Ex. SCL-1 at 23-26.

[322] Tr. 4138:2-4 (Hogan).

[323] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275 (2001).

[324] *Id.* at 62,218 ("[w]hile high prices, in and of themselves do not make a rate unjust and unreasonable (because, for instance, underlying production prices may be high), if over time rates do not behave as expected in a competitive market, the Commission must step in to correct the situation").

not need to calculate a competitive, unmanipulated price for wholesale power for each Respondent.[325]

698. Sixth, Seattle argues that Respondents wrongly assert that the MMCP will cause them to incur losses.[326] Seattle first states that the MMCP was only used to address liability, and not to compute refunds.[327] Additionally, Seattle asserts that Respondents will have the opportunity to assert "ripple" claims against their suppliers.[328] Lastly, Seattle notes that Respondents always have the opportunity to demonstrate that a refund obligation imposed by the Commission would cause it to operate at a loss in a given market.[329]

699. Seventh, Seattle argues that the Commission has already determined that Respondents cannot recover opportunity costs, scarcity rents, and transmission costs. Seattle states that the in the California Refund Case, the Commission fully considered and rejected identical arguments concerning the MMCP.[330]

#### (b) Allegations that Contracts Imposed an Undue Burden on Consumers or Harmed the Public Interest and Are Unduly Discriminatory

700. Seattle states that the Commission held that the *Mobile-Sierra* presumption could be rebutted in any way permitted by the Supreme Court's decision in *Morgan Stanley*.[331]

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[325] Seattle notes that the MMCP was used for the sole purpose of addressing the liability issue. Tr. 2237:15-2238:1, 2261:3-14 (Hanser). Seattle states that Respondents can be given the opportunity to "true up" estimated data with actual data in the same way they were permitted to do in the California Refund Case. Tr. 2243:23-2244:2 (Hanser).

[326] This claim is based on the fact that for some transactions, the wholesale power sold to Seattle may have been purchased at a price that exceeds the MMCP.

[327] Tr. 2253:23-25 (Hanser).

[328] *Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 13, 2012) (Order Confirming Rulings from the September 6, 2012 Prehearing Conference).

[329] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,214-15 (2001).

[330] *Id*. at 62,211-16.

[331] Order Granting Interlocutory Appeal at P 15.

Seattle argues that it demonstrated that the contracts at issue imposed undue burdens on Seattle and Seattle City Light's (SCL) customers that are contrary to the public interest.

701. Seattle states that SCL set its retail rates for the three-year period ending February 28, 2003 based on an anticipated wholesale market price of power in peak hours of $23 per MWh for 2000, $25 per MWh for 2001, and $27 per MWh for 2002. Seattle asserts that these estimates were consistent with historical prices.[332] Seattle states that the actual average cost of wholesale purchases was $83 per MWh for 2000, $215 per MWh for 2001, and $26 per MWh for 2002.[333] As a result of the high prices, Seattle asserts that in 2000 and 2001, SCL exceeded the utility's budget estimates by nearly $600 million.

702. Seattle states that in order to recover costs associated with power that was purchased, SCL implemented several rate increases in 2001, resulting in a total increase of over forty percent for the average customer.[334] Seattle contends that the increased rates also resulted in decreased economic activity, which lowered the City's tax revenues.[335] Additionally, Seattle notes that SCL spent all $248 million of retained earnings and had to issue revenue bonds in order to pay for the increased cost of power to serve its load.[336] In addition to the substantial underwriting and legal fees, Seattle states that the bonds adversely impacted Seattle's credit rating.[337]

703. Seattle also argues that the public interest is not served by permitting a seller to charge prices for wholesale energy that violate its tariff and are not "just and reasonable," particularly when Respondents' unlawful market activity caused those unjust and unreasonable prices. Furthermore, Seattle contends that the exercise of market power by sellers is contrary to the public interest because such unlawful actions had the potential to

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[332] Ex. SCL-1 at 33; Ex. SCL-40.

[333] Ex. SCL-1 at 32-33; Ex SCL-38; Ex. SCL-39.

[334] Tr. 1982:25-1983:18 (Hanser).

[335] Ex. SCL-110 at 80:19-81:4. *See also San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,522 (2001) (Commissioner Massey dissenting) ("[b]uyers in the Northwest paid outrageous prices for power that caused much economic dislocation").

[336] Ex. SCL-110 at 79:9-80:5; Ex. SCL-10.

[337] Ex. SCL-10 at 23.

cause brownouts and blackouts in the Pacific Northwest.[338] Seattle avers that Respondents' exercise of market power in the Pacific Northwest threatened the stability of the grid in the entire Western Interconnect.[339]

704. Next, Seattle contends that the contracts at issue are unduly discriminatory because Respondents charged Seattle rates that frequently exceeded the MMCP that was adopted for the California Refund Case. Seattle notes that the Commission determined that the MMCP was the just and reasonable price for OOM sales at various delivery points in the Pacific Northwest. Therefore, Respondents sales above the MMCP discriminate against Seattle and in favor of the California ISO. Seattle states that it is similarly situated to the California ISO because both are not-for-profit entities that serve load and do not trade energy in order to make a profit, both were price takers that were forced to pay high prices in order to serve their load, and both were victimized by non-competitive markets that were manipulated on a massive scale.

### (c) Claims Pursuant to Section 309 of the FPA

705. Seattle states that in order to receive refunds under section 309 of the FPA, Seattle must demonstrate that Respondents violated either a substantive provision of the FPA or a filed tariff or rate schedule.[340] Seattle asserts that each Respondent acquired market power and then used that market power to charge Seattle rates that greatly exceeded the rates the Respondent could have charged if the market had been competitive. Seattle argues that by doing so, each Respondent violated its market-based tariff and section 205 of the FPA, which requires all prices for wholesale power to be "just and reasonable."[341]

706. Seattle also contends that the Order on Rehearing permits Seattle to submit claims for refunds under section 309 for the entire refund period – January 1, 2000 through June 20, 2001.[342] Seattle states that the Commission did not limit Seattle's section 309 refund claims to the period January 1 through December 24, 2000, as Respondents assert.

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[338] Ex. SCL-76 at 32:10.

[339] *Id.*

[340] Order on Rehearing at P 32.

[341] 16 U.S.C. § 824d(a) (2012).

[342] *Id.*

### (d) Proper Definition of Spot Market

707. Next, Seattle argues that the Commission should adopt the following definition of spot sale for this proceeding: (1) a sale that lasts one month or less, and (2) a sale that lasts longer than one month but less than one year if the sale was not part of the purchaser's long-term planning process.[343] Seattle notes that in its July 25, 2001 Order establishing a preliminary evidentiary hearing in this case, the Commission expressly acknowledged that "[w]hat is a 'spot market' sale for bilateral transactions in the Pacific Northwest may differ from what is a 'spot market' sale in the California ISO and CalPX organized spot markets."[344] Thus, Seattle asserts that the Commission has not adopted a definition of "spot sale" for this case or given any further guidance on this issue.

708. Seattle argues that fundamental differences between the wholesale market in the Pacific Northwest and the California organized markets justify different definitions of "spot sale." These fundamental differences include (1) different market structures; (2) the Pacific Northwest's reliance on hydroelectric generation;[345] and (3) the behavior of LSEs in the Pacific Northwest. Seattle states that LSEs generally engage in a process of buying and selling power in transactions up to one month in duration in order to triangulate toward a precise balance of loads and resources when the hour of actual delivery occurs.[346] Seattle notes that the effects of changed water conditions can last up to one year, and therefore, the need for energy to balance load is not limited to a single hour or a single day. Thus, compared to market participants in California, participants in the Pacific Northwest "trade energy across much longer timeframes, with the standard products specifying delivery for multiple hours in each day, and products traded for a day, a month, a quarter, or a year (or longer) at a time."[347]

709. Seattle further asserts that its definition of "spot sale" is identical to the definition previously proposed by Commission Trial Staff[348] and several other objective sources.

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[343] Ex. SCL-81 at 4-6; Ex. SCL-15 at 3-9. However, the longest transaction for which Seattle is seeking refunds is three months long.

[344] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,520 n.74 (2001).

[345] Ex. SCL-37 at 9:11-13.

[346] Ex. SCL-95 at 6:16-19; Ex. SCL-83. *See also* Ex. SCL-96.

[347] Ex. SCL-117 at 13:3-6.

[348] Ex. SCL-81 at 5:6-14; Ex. SCL-82; Ex. SCL-95 at 9:20.

For example, Seattle states that the BPA website provides a definition of spot market that contemplates sales and purchases of power normally for less than one year.[349] Seattle notes that BPA has a dominant presence in the region's power market,[350] and its definition provides an objective basis for understanding how market participants in the Pacific Northwest define the spot market. Additionally, Seattle avers that the testimony of Stan Watters, who was Vice President of Trading and Origination for PacifiCorp, states that spot transactions should "include all transactions up to and including one month in duration."[351]

710. Seattle also cites to Department of Interior regulations that defined the "spot market price" for coal as "the price received under any sales transaction when planned or actual deliveries span a short period of time, usually not exceeding one year."[352] Seattle contends that the analogy between coal and water as fuels for generation facilities supports a similar definition of "spot sale" in the Pacific Northwest, where water is the predominant source of power generation.[353]

711. Seattle argues that Respondents wrongly rely on a definition of spot sale as transactions with a term of twenty-four hours or less that are entered into the day of or day prior to delivery.[354] Seattle describes this definition as "self-serving" because it would effectively reduce refund liability to the maximum extent possible. Seattle also notes that Commission Trial Staff previously concluded that Respondents' proposed definition of "spot sale" is not consistent with the business realities in the Pacific Northwest that require a definition of "spot sale" that is different from the one the

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[349] Ex. SCL-95 at 7:18-8:11.

[350] During the relevant time period, BPA owned and operated approximately eighty percent of the Pacific Northwest's high-voltage transmission systems and marketed forty percent of the electricity consumed in the region. Ex. SCL-95 at 8:13-15.

[351] Ex. SCL-83 at 3.

[352] 30 C.F.R. §§ 206.251, 206.451 (2000).

[353] Additionally, Seattle states that Mr. Hanser made his own independent review of the proposed definition and concluded it was the definition most nearly reflected by the market realities in the Pacific Northwest. *See* Ex. SCL-76 at 11:10-13; Ex. SCL-115 at 34:1-35:4.

[354] *See, e.g.*, Ex. EP-2 at 6:4-7.

Commission adopted in the California Refund Case.[355] Seattle asserts that Respondents improperly rely on Commission orders issued in other dockets and their purported experience with or knowledge of trading practices in the industry.[356] Thus, Seattle concludes that Respondents' definition of "spot sale" has no relationship to the Commission's regulatory goals in this case, is inappropriate for the Pacific Northwest, and lacks a rational basis.

### (e) Claims Pursuant to Section 206 of the FPA

712. Seattle states that in order to receive refunds under section 206 of the FPA, Seattle must demonstrate that the prices for wholesale energy in the Pacific Northwest were unjust and unreasonable during the Section 206 Period. As discussed above, Seattle argues that it has demonstrated that each Respondent charged Seattle unjust and unreasonable rates, and therefore, Seattle is entitled to refunds under section 206 of the FPA.

### (f) Response to Respondents' Defenses

713. First, Seattle contends that Respondents' defense based on the prices charged by Seattle has been rejected by the Commission and is moot. Seattle states that the Commission has ruled that it is not subject to Sections 205 and 206 of the FPA.[357] Seattle further states that it has never had a market-based rate tariff or any other Commission regulated tariff for wholesale energy. Accordingly, Seattle concludes that the prices it charged Respondents were lawful in all respects, even when those prices were higher than the prices Respondents were charging.

714. Seattle also contends that Respondents' equity argument is premature and deals with the remedy phase of the proceeding rather than the current liability phase. Moreover, Seattle states that the Commission has held that it is not inequitable to permit a governmental entity like Seattle to receive refunds even though the Commission lacks jurisdiction under the FPA to order Seattle to pay refunds in the same proceeding.[358]

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[355] *See* Ex. SCL-82 at 24-25.

[356] *See, e.g.*, Ex. EP-2 at 6:16-7:10.

[357] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 125 FERC ¶ 61,297 (2008).

[358] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 121 FERC ¶ 61,607, at P 59 (2007).

Furthermore, Seattle contends that Respondents' argument is moot because, as discussed above, Seattle has agreed to voluntary reduce its refund claims by the amount of "refunds" that would be due if Seattle were subject to the Commission's jurisdiction.

715. Second, Seattle avers that Respondents wrongly claim that Seattle lacked prudence in its resource planning. Seattle states that in determining whether wholesale rates are just and reasonable, the Commission has consistently refused to consider whether or not a purchaser has acted prudently.[359]

716. Furthermore, Seattle asserts that Respondents' criticisms of Seattle's resource planning are meritless. For example, Seattle notes that in 1996, when it reduced its purchase entitlement under a contract with BPA, Seattle was in a surplus generation position of over 250 MW. Additionally, the price BPA was entitled to charge for that power exceeded the market price.[360] With respect to Respondents' criticisms of Seattle's decision to sell its eight percent share of the Centralia Generation Plant in 2000, Seattle states that it was still in a surplus position with respect to resources at the time,[361] and the sale relieved Seattle of its long-term liability for mine reclamation.[362] Seattle further notes that following the sale of its minority interest in Centralia, Seattle executed numerous contracts to hedge against a deficit position up to the limits of SCL's financial authority.[363] Seattle concludes that there is no valid reason for permitting Respondents to avoid liability for their unlawful actions and retain their ill-gotten gains merely because,

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[359] *See, e.g., Ky. W. Va. Gas Co. v. Pa. Pub. Util. Comm'n*, 837 F.2d 600, 609 (3d Cir. 1988); *Pa. Power & Light Co.*, 23 FERC ¶ 61,325 (1983). *See also Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, at P 415, *clarified*, 124 FERC ¶ 61,055, *order on reh'g*, Order 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), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012).

[360] Ex. SCL-80 at 3.

[361] *Id*.

[362] *Id*. at 9.

[363] *Id*. at 2. Seattle notes that SCL was in a net projected surplus position of 22 MW in 2001. *Id*. at 3.

in Respondents' view, Seattle caused its own problems by not planning more carefully for Respondents' unlawful market activity.

717. Third, Seattle avers that Respondents' assertion that market fundamentals explain the high prices is irrelevant and has been rejected by the Commission. Seattle argues that regardless of fundamentals, Respondents are not permitted to charge any price for wholesale energy that the market will bear. Rather, under their market-based rates, Respondents are limited to charging Seattle prices for wholesale energy that are "just and reasonable." Additionally, Seattle notes that in the California Refund Case, Commission rejected an argument that the MMCP should include scarcity rents because the MMCP was designed to replicate prices in a competitive market.[364]

718. Lastly, Seattle notes that Professor Hogan's testimony demonstrates that there were adequate resources in the Western energy markets to serve all load and guarantee system reliability.[365] Seattle states that for the period May 2000 through June 2001, the reserve margin after forced outages for the entire WECC region was over fifteen percent in every month, with the exception of August 2000 and May 2001, when the reserve margins were 13.5 percent and 13.7 percent, respectively.[366] Seattle contends that these reserve margins are well within the acceptable range needed to insure system reliability, and therefore there was no overall shortage of resources.[367]

### 2. Indicated Seattle Respondents Initial Brief

#### (a) Burden of Proof and Legal Standard

719. Indicated Respondents[368] state that as claimant, Seattle bears the burden of proof[369] and must demonstrate, by the preponderance of the evidence, that the

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[364] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,211-16 (2001).

[365] Ex. SCL-76 at 14.

[366] Ex. PNR-1 at 165, Table 38.

[367] Ex. SCL-76 at 13:21-22.

[368] Indicated Respondents are Avista Energy, Inc. and Avista Corporation d/b/a Avista Utilities; Cargill Power Markets, LLC; El Paso Marketing Company, L.L.C. (f/k/a El Paso Marketing, L.P. and El Paso Merchant Energy, L.P.); PPL Montana, LLC and PPL EnergyPlus, LLC; Public Service Company of Colorado; Shell Energy North

(continued…)

Respondent committed the alleged violation."[370] Indicated Respondents assert that the *Mobile-Sierra* presumption applies to all of Seattle's claims for refunds under section 206 of the FPA because all of the sales at issue were made pursuant to the WSPP Agreement. Thus, for claims under section 206 of the FPA, Seattle must prove that each Respondent engaged in unlawful activity and that such activity directly affected specific contracts with Seattle, or that specific contracts imposed an excessive burden on consumers.[371] Indicated Respondents contend that this showing has been described as a "practically insurmountable" or "almost insurmountable" burden of overcoming the *Mobile-Sierra* presumption.[372]

720. With respect to claims pursuant to section 309 of the FPA, Indicated Respondents state that Seattle must prove that each Respondent engaged in specific violations of a substantive provision of the FPA or of its filed tariff or rate schedule, and that such violations resulted in an unjust and unreasonable rate.[373]

721. Indicated Respondents note that since the issuance of *Mobile*[374] and *Sierra*,[375] the Court has consistently limited the Commission's authority to abrogate freely negotiated

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America (US), L.P., d/b/a Coral Power, L.L.C. and; TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc.

[369] 5 U.S.C. § 556(d) (2012) ("[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof" and any sanction imposed must be "supported by and in accordance with reliable, probative and substantial evidence").

[370] *Nantahala Power & Light Co.*, 19 FERC ¶ 61,152 (1982) (concluding that the Administrative Procedure Act adopted a "traditional preponderance-of-the-evidence standard"); s*ee also Tex. Gas Serv. Co. v. El Paso Natural Gas Co.*, 136 FERC ¶ 63,010, at P 326 (2011) ("[a] party can meet the preponderance of the evidence standard by showing that the existence of a fact is more probable than its nonexistence") (internal quotation marks and citation omitted).

[371] Order on Remand at PP 17-24; Order Granting Interlocutory Appeal at PP 12-15.

[372] *See Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000) (citing *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 953 (D.C. Cir. 1983)).

[373] Order on Rehearing at P 32.

[374] *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956).

agreements. For example, in *Permian Basin*, the Court ruled that "[t]he regulatory system created by the [NGA] is premised on contractual agreements voluntarily devised by the regulated companies; it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity."[376] Additionally, in *Verizon Communications, Inc. v. FCC*, the Court clarified that its prior pronouncements concerning the impropriety of relieving a regulated entity of an "improvident bargain" did not apply just to the regulated entity, but applied to both parties to a negotiated contract.[377]

722. Next, Indicated Respondents discuss the Supreme Court's recent application of the *Mobile-Sierra* doctrine, which came in the context of market-based rates and claims of excessive charges by public utilities.[378] Indicated Respondents first note that the *Morgan Stanley* decision is directly applicable to Seattle's similar claims here, as the Commission recognized in its Order on Remand.[379] Indicated Respondents next state that the Court rejected arguments that the *Mobile-Sierra* presumption should not apply and specifically instructed that "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law … [and] [t]he presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*."[380] Indicated Respondents further note that the Court emphasized that the public interest "is the 'sole concern' in a contract case" when determining whether that contract should be modified,[381] and not "whether [the rates] are unfair to one of the parties that voluntarily assented to the contract."[382]

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[375] *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956).

[376] *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).

[377] *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002) ("[w]hen commercial parties … avail themselves of rate agreements, the principal regulatory responsibility [is] not to relieve a contracting party of an unreasonable rate …").

[378] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008).

[379] Order on Remand at P 21.

[380] *Morgan Stanley*, 554 U.S. at 530 (emphasis added).

[381] *Id.* at 545 n.3.

[382] *Id.* at 546-47.

723. Indicated Respondents assert that the Court also rejected the Ninth Circuit's conclusion that the Commission must determine whether a contract was formed in a dysfunctional market before applying the *Mobile-Sierra* presumption, stating that "one of the reasons that parties enter into wholesale-power contracts is precisely to hedge against the volatility that market imperfections produce."[383] The Court further explained that "[b]y enabling sophisticated parties who weathered market turmoil by entering long-term contracts to renounce those contracts once the storm has passed, the Ninth Circuit's holding would reduce the incentive to conclude such contracts in the future."[384] The Court also noted that "evaluating market 'dysfunction' is a very difficult and highly speculative task – *not* one that the FPA would likely require the agency to engage in before holding sophisticated parties to their bargains."[385]

724. Indicated Respondents further state that the Court acknowledged that the *Mobile-Sierra* presumption would not apply where the illegal actions of one of the parties to a contract led to the dysfunctional market conditions under which the contract was formed.[386] However, the Court cautioned that even where claims are raised that illegal actions of one of the parties to a contract led to the dysfunctional market, the Commission must find "a causal connection between unlawful activity and the contract rate."[387]

725. With respect to the "zone of reasonableness" test based on marginal cost, Indicated Respondents note that the Court rejected the Ninth Circuit's use of this test to determine if a rate was so high as to impose an excessive burden on consumers. Specifically, the Court stated that it "fails to accord an adequate level of protection to contracts,"[388] and that a "presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract based-regulation."[389] Indicated Respondents note that the Court went on to state that "under the *Mobile-Sierra* presumption, setting aside a contract rate requires a

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[383] *Id.* at 547.

[384] *Id.*

[385] *Id.* at 548.

[386] *Id.* at 547.

[387] *Id.* at 554-55.

[388] *Id.* at 548-49.

[389] *Id.* at 550 (citations omitted).

finding of 'unequivocal public necessity' or 'extraordinary circumstances'" and that a price above marginal costs alone fails to meet this standard.[390] Indicated Respondents also note that the Court found that the harm to the public interest must be "more than a small dent in the consumer's pocket."[391] Thus, a disparity in rates alone is not sufficient to overcome the *Mobile-Sierra* presumption.[392]

726. Lastly, Indicated Respondents state that the Commission has confirmed that the holdings in *Morgan Stanley* apply equally to this proceeding.[393] Thus, in order to avoid or overcome the *Mobile-Sierra* presumption, Seattle must prove, on a contract-specific basis, that each Respondent engaged in "unlawful market activity without a legitimate business reason … [that] directly affected the negotiation of specific bilateral contracts, resulting in unjust and unreasonable rates;"[394] that each Respondent "engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations" which "directly affected the particular contract or contracts to which the [Respondent] was a party;"[395] or that such unlawful activity "resulted in unjust and unreasonable" rates under each contract[396] that imposed an excessive burden on consumers which seriously harmed the public interest.[397] Indicated Respondents assert that the D.C. Circuit has characterized the burden imposed by the *Mobile-Sierra* doctrine as "practically insurmountable" and "almost insurmountable."[398]

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[390] *Id.* (citations omitted).

[391] *Id*.

[392] *PEPCO v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000).

[393] Order on Rehearing at P 17 ("the *Mobile-Sierra* public interest presumption applies to the short-term contracts at issue here, unless buyers can overcome or avoid the presumption"). *See also* Order on Remand at P 20.

[394] Order on Remand at P 23.

[395] *Id.* PP 20-21.

[396] *Id.* P 19.

[397] *See* Order Granting Interlocutory Appeal at PP 14-15.

[398] *See Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (Scalia, J.); *Kansas Cities v. FERC*, 723 F.2d 82 at 82, 87-88 (D.C. Cir. 1983).

### (b) Claims Pursuant to Section 206 of the FPA

#### (i) Allegations of Unlawful Activity by Respondents

727. Indicated Respondents contend that Seattle has not even attempted to make the central evidentiary showing of unlawful market activity that was required by the Commission.[399] Indicated Respondents note that both Mr. Hanser and Mr. Morter admitted that they were not alleging any illegal conduct by any of the Respondents in this case.[400] Indicated Respondents assert that Seattle presented no evidence of (1) duress, fraud or bad faith; (2) undue price discrimination; (3) False Export; (4) selling non-firm energy as firm; or (5) exercise of market power.[401] Moreover, Indicated Respondents aver that Seattle failed to even identify the specific contracts at issue between itself and the Respondents. Thus, Indicated Respondents conclude that Seattle has clearly failed to provide evidence demonstrating that "unlawful market activity directly affected the negotiation of specific bilateral contracts, resulting in unjust and unreasonable rates."[402]

#### (ii) Allegations that Contracts Imposed an Undue Burden on Consumers or Harmed the Public Interest

728. Indicated Respondents first argue that Seattle presented no probative evidence of excessive burden or serious harm to the public interest. Indicated Respondents assert that

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[399] Order on Remand at P 21 ("parties seeking refunds must submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract").

[400] Tr. 2074:10-15, 2116:24-2117:1 (Hanser); Tr. 3278:7-20 (Morter).

[401] With respect to the Section 309 Period, which is outside the scope of the relevant time period for section 206 claims, Seattle has argued that prices charged in excess of the "benchmarks" described in Mr. Hanser's Section 309 testimony demonstrate the exercise of market power and reflect an unjust and unreasonable rate. *See, e.g.*, Tr. 2070:20-2072:2 (Hanser). Indicated Respondents assert that this argument was not advanced with respect to Seattle's section 206 claims as Seattle did not present any "benchmark" analysis. Tr. 1901:17-22 (Hanser). *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 23 (June 20, 2013) (Order Granting in Part and Denying in Part Motion to Strike).

[402] Order on Remand at P 23.

the only evidence describing any alleged harm or burden that Seattle or its ratepayers experienced was the prior testimony of Ms. Paula Green and other public documents submitted by Mr. Hanser.[403] Indicated Respondents note that Ms. Green was a lay witness and the facts in her testimony were never independently sponsored or submitted by a Seattle fact witness in this stage of the proceeding. Indicated Respondents state that Mr. Hanser simply adopted Ms. Green's testimony and conducted no independent evaluation of her allegations.[404]

729. Indicated Respondents argue that Mr. Hanser's wholesale adoption of Ms. Green's statements is not proper expert testimony and should be given no weight. Indicated Respondents assert that proper expert testimony requires specialized knowledge to help the trier of fact understand the evidence and the expert must reach his conclusions using scientifically reliable processes and methods.[405] Indicated Respondents note that Mr. Hanser admitted that a lay witness could have presented the same testimony he repeated and purported to offer as expert testimony.[406] Indicated Respondents contend that Seattle should not be permitted to insert a fact witness's prior testimony through an expert witness.

730. Next, Indicated Respondents aver that Ms. Green's testimony does not provide any evidence of excessive burden or harm to the public interest. Indicated Respondents assert that to set aside a contract rate based on excessive burden or harm to the public interest, there must be a finding of "unequivocal public necessity or extraordinary circumstances," and not "the mere exceeding of marginal cost."[407] Additionally, Indicated Respondents note that the Commission considers "whether consumers' rates increased immediately upon the relevant contracts going into effect" and whether "the contracts imposed an excessive burden on consumers 'down the line,' relative to the rates they could have obtained (but for the contracts) after elimination of the dysfunctional market."[408] However, "simply identifying high prices" to overcome the *Mobile-Sierra*

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[403] Tr. 1897:18-20 (Hanser).

[404] *Id*.

[405] FED. R. EVID. 702(a), 702(d).

[406] *See* Tr. 1983:19-23 (Hanser).

[407] Order Granting Interlocutory Appeal at P 13 n.25 (quoting *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550-52 (2008)).

[408] *Id*. P 13.

presumption is inconsistent with the Commission's finding that "general allegations of market dysfunction in the Pacific Northwest are an insufficient basis for overcoming the *Mobile-Sierra* presumption."[409]

731. Indicated Respondents argue that Ms. Green's testimony does not tie any alleged burden or harm to specific contracts or Respondents.[410] Indicated Respondents note that Mr. Hanser admitted that he did not review any transaction data as part of his testimony covering the Section 206 Period, and there is no indication in the record that Ms. Green ever did so either.[411] Indicated Respondents aver that without evidence identifying individual contracts or transactions, it is impossible to evaluate whether a particular contract or transaction between a Respondent and Seattle imposed an excessive burden or seriously harmed the public interest.

732. With respect to the rate increases identified by Ms. Green, Indicated Respondents state that Mr. Hanser only alleged that the rate increase was the result of "increased costs for wholesale power that Seattle was forced to pay," but at no point tied the increase to any specific wholesale energy costs, much less any costs that resulted from Respondents' contracts or behavior.[412] Indicated Respondents note that Mr. Hanser did no analysis identifying specific wholesale energy costs, showing how Seattle assessed those costs and decided what rate increases were appropriate as a result, showing what alternatives Seattle considered to these rate increases, or any other analysis to tie the rate increases to wholesale energy costs in a manner that could be coherently assessed for purposes of an excessive burden analysis.

733. Moreover, Indicated Respondents assert that the rate increase included many matters having nothing to do with wholesale energy costs at all. For example, nearly twenty percent of the increase came from increases in transmission costs.[413] Indicated Respondents also assert that an additional portion of the increase was the result of

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[409] *Id*. P 15 (quoting Order on Remand at P 21).

[410] *See* Order on Rehearing at P 30 ("the Commission must evaluate each seller's conduct in relation to specific contract negotiations and/or whether the contract imposes an excessive burden on consumers").

[411] Tr. 1901:2-25 (Hanser).

[412] Ex. SCL-1 at 5:20; 34:5.

[413] Tr. 1981:3-1983:4 (Hanser).

capitalizing certain costs, and the effect of debt acquired before the period at issue.[414] Because Mr. Hanser failed to determine these effects, Indicated Respondents contend that there is no basis to determine the effect of wholesale energy costs on Seattle's rates and whether those costs did in fact constitute an excessive burden.

734. Next, Indicated Respondents argue that Seattle's increased wholesale power costs also reflect the consequence of Seattle's business decision to reduce its long-term purchases, sell its share of the Centralia coal plant, and increase reliance on the wholesale spot market,[415] which then coincided with the lowest water year on record in sixty years that limited hydroelectric generation output.[416] Indicated Respondents further note that the high prices in the market prevailed only for a short period of time and were largely the result of supply and demand conditions.[417] Indicated Respondents contend that none of these factors are consistent with the kind of excessive burden that courts and the Commission have held might justify the reformation of contract rates.

735. Furthermore, Indicated Respondents assert that even if the entire fifty-eight percent rate increase was attributable to wholesale energy costs, it would be consistent with other periods of supply shortage. For example, Indicated Respondents state that Seattle increased rates by approximately sixty-four percent between 1980 and 1982.[418] Additionally, there was a sixty percent increase in the 1970s.[419] Indicated Respondents

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[414] Ex. CCG-10 at 15 (independent consulting group's 2002 report on Seattle City Light finding that "SCL's current debt is primarily the result of a series of decisions made in the 1990's which when combined, created an enormous debt load for SCL … decision-makers decided to increase the debt load rather than increase rates or reduce operating costs").

[415] Tr. 1911:5-13 (Hanser); Ex. SCL-40 at 2 (Seattle City Light Issues Brief stating that for 2000 and 2001, Seattle is "more dependent on the market than we have been historically because of the sale of our share of the Centralia coal plant").

[416] Ex. SCL-10 at 10 ("[s]ince late 2000, SCL's ability to use hydroelectric resources to restrict market purchases to off-peak periods has been greatly limited because of water conditions that are among the lowest in sixty years of record").

[417] *See* Ex. PNR-1 at 7:5-9.

[418] Ex. CCG-17; Tr. 2101:20-2102:2 (Hanser).

[419] Ex. SCL-10 at 22.

state that there is no indication that Seattle either sought or could have obtained relief from these prior increases on grounds of "excessive burden."

736. Indicated Respondents also note that Seattle's average electric rates remained the lowest of the twenty-five largest cities in the United States in 2001.[420] Indicated Respondents assert that Mr. Hanser offered no "analysis of regional conditions and electric rate increases that … place [his] testimony regarding Seattle's rate increases in context" or that refutes the evidence of Seattle's lower than average rates.[421] Indicated Respondents state that for each year from 2002 to 2008, Seattle either had a rate decrease or no change to its rates, except in 2003 when there was a 1.4 percent increase.[422] Indicated Respondents conclude that Seattle's subsequent rates demonstrate that there was no excessive burden placed on consumers or any down the line effects from Seattle's purchases.

737. Next, Indicated Respondents state that other than Ms. Green's testimony, Mr. Hanser only provided excerpts of bond offerings from 2001 and 2003 to support Seattle's claim that increased wholesale power costs incurred by Seattle led to an excessive burden.[423] Indicated Respondents assert that none of these documents analyze how any increased amounts for wholesale energy contracts translated into specific rate increases, much less how those amounts were connected to the Respondents or harmed the public interest. Further, Indicated Respondents state that the documents demonstrate that Seattle maintained its AAA credit rating during and after the period at issue.[424]

738. Indicated Respondents aver that the bond offering documents also support the Respondents' position that higher wholesale power prices were the result of supply and demand and Seattle's own business decisions. For example, in the bond offering from 2001, Seattle explained to the investment community that its "financial results in 2000 were far below historical levels, due to a combination of subnormal water conditions and unusually high demand for power, which drove the cost of power supply to

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[420] Ex. PRX-260 at 3. *See also* Tr. 2208:6-14 (Hanser).

[421] Tr. 2200:19-23 (Hanser).

[422] Ex. CCG-17; Tr. 2102:2-6 (Hanser).

[423] Ex. SCL-1 at 32-35. *See also* Ex. SCL-38 and Ex. SCL-39.

[424] Ex. SCL-39 at 1. Indicated Respondents note that Mr. Hanser was unable to reconcile this AAA rating with the testimony he purported to adopt from Ms. Green that Seattle's credit rating was harmed. Tr. 2226:1-17 (Hanser).

unprecedented levels."[425] The 2001 offering further states that output from Seattle's "hydroelectric facilities is projected to be only 66 percent of the average output over the water conditions in the 49-year period from 1929 through 1978."[426] Similarly, in the 2003 offering, Seattle reported that it had increased rates in 2001 after it "was required to purchase large amounts of power in the wholesale market as a result of its 1996 decision to limit purchases from Bonneville, … the sale of Centralia Steam Plant in May 2000, and unusually poor water conditions in the water year beginning October 1, 2000."[427] Indicated Respondents contend that these documents confirm that any burden Seattle faced was the result of market forces and its own decisions, and do not support any claim of excessive burden or harm to the public interest as a result of the Respondents' sales to Seattle.

739. Next, Indicated Respondents argue that Seattle made no effort to tie any purported burden or harm to a contract with a Respondent. Seattle also presented no evidence that its consumers' rates would have been lower but for a contract with a particular Respondent. Indicated Respondents aver that Seattle has not submitted any evidence regarding any contract. Instead, Indicated Respondents state that Seattle provided transaction spreadsheets that list the hourly deliveries of electricity that Seattle received from all Respondents.

740. Indicated Respondents also assert that Seattle failed to consider the impact of electricity prices in the Pacific Northwest on the customers of other load serving entities. Indicated Respondents note that Mr. Hanser conceded that he performed no analysis of rate increases that other Pacific Northwest load serving entities experienced during the refund period and did not conduct "any analysis of regional conditions and electric rate increases" that provide context for Seattle's rate increases.[428] Indicated Respondents argue that Seattle simply asserts that all prices paid to all Respondents were too high, but fails to consider its own resource planning that caused Seattle's increase reliance on wholesale power.

741. Next, Indicated Respondents assert that market-based rates that reflect supply and demand conditions are consistent with the Commission's regulatory scheme and do not create an excessive burden. Indicated Respondents state that the Commission's

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[425] Ex. SCL-38 at 2.

[426] *Id.* at 3. *See* Tr. 1928:10-1929:21 (Hanser).

[427] Ex. SCL-39 at 2.

[428] Tr. 2200:14-23 (Hanser).

market-based rate program authorizes sellers of electricity to make wholesale sales of energy at prices purchasers are willing to pay. The Commission only authorizes those sellers who do not have, or have adequately mitigated, market power to charge market-based rates.[429] Thus, the Ninth Circuit held that "[w]here sellers do not have market power or the ability to manipulate the market (alone or in conjunction with others), it is not unreasonable for FERC to presume that rates will be just and reasonable."[430]

742. Indicated Respondents state that an integral component of the Commission's market-based rate program is that prices between sellers and purchasers are permitted to fluctuate in response to market forces. Indicated Respondents note that courts have determined that allowing market prices for sales to track market forces complies with the FPA because under the Commission's market-based rate principles and practices, there is adequate protection to ensure that the markets are not subject to manipulation.[431]

743. Indicated Respondents assert that Respondents' sales were made pursuant to a market-based rate tariff on file with the Commission. Thus, the Commission determined that each Respondent did not possess market power and that the Commission was able to monitor sales prices.[432] Indicated Respondents aver that Seattle has had a full opportunity to present evidence that a Respondent exercised market power or engaged in misconduct, but failed to do so.

744. As discussed above, Indicated Respondents reiterate that the prices in the Pacific Northwest were driven by market forces.[433] Indicated Respondents argue that Seattle

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[429] *See, e.g.*, *La. Energy and Power Auth. v. FERC*, 141 F.3d 364 (D.C. Cir. 1998).

[430] *Mont. Consumer Counsel v. FERC*, 659 F.3d 910, 914 (9th Cir. 2011).

[431] *See id*; *see also Blumenthal v. FERC*, 552 F.3d 875, 882 (D.C. Cir. 2009) ("what matters is whether an individual seller is able to exercise anticompetitive market power, not whether the market as a whole is structurally competitive").

[432] Indicated Respondents note that the Commission has already determined that any issues concerning post-approval reporting requirements are not at issue in this proceeding. *See, e.g.*, Order on Remand at PP 18-20 & n.43; Order on Rehearing at P 18.

[433] Ex. SCL-38 at 2; Ex. SCL-39 at 2. Professor Hogan includes the following factors as leading to the increase in electricity prices: (1) a reduction in hydro generation, which lead to increased reliance on expensive natural gas-fired generation; (2) reduced amounts of natural gas supply; (3) increased emission costs; (4) reduced output from QFs; (5) reduced nuclear output in California; and (6) high energy consumption.

(continued…)

failed to account for those market forces. Indicated Respondents note that Mr. Hanser admitted that he did not analyze Pacific Northwest demand,[434] and failed to analyze the effects of supply and demand fundamentals on price.[435] Indicated Respondents further state that Mr. Hanser did not disagree with evidence presented to him during his cross-examination of historically low water conditions that drove the cost of supply to "unprecedented levels," and he did not challenge Professor Hogan's factual findings with respect to other fundamental supply changes.[436]

745. Next, Indicated Respondents discuss Mr. Hanser's cointegration study. Indicated Respondents first note that the Commission has already determined that a causal relationship between any California dysfunction and Pacific Northwest market prices alone would not be sufficient to overcome the *Mobile-Sierra* presumption.[437]

746. Indicated Respondents also state that Mr. Hanser acknowledged that neither he nor his cointegration analysis purports to demonstrate a causal relationship between the dysfunction of the California organized market and energy prices in the Pacific Northwest bilateral market.[438] Rather, Mr. Hanser alleges, without support, that the California market was the "dominant" market in the West.[439] However, Indicated Respondents assert that the Pacific Northwest market was substantial, approximately one-half the size of the California market.[440] Additionally, Indicated Respondents note that Mr. Hanser later stated that for the purpose of his cointegration analysis, it does not matter which market is dominant.[441] Thus, Indicated Respondents conclude that Seattle

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Ex. PNR-1.

[434] Tr. 1949:10-23 (Hanser).

[435] Tr. 1960:13-1969:24 (Hanser).

[436] Tr. 1988:7-1989:10 (Hanser).

[437] Order on Remand at P 21.

[438] *See, e.g.*, Tr. 1967:3-16 (Hanser).

[439] Tr. 1969:4-6 (Hanser).

[440] Tr. 1974:1-4 (Hanser).

[441] Tr. 2266:4-7 (Hanser).

only submitted evidence that the prices for electricity in the California and Pacific Northwest markets are related, a conclusion never in dispute.[442]

747. Lastly, Indicated Respondents argue that it would not be in the public interest to interfere with market results. Indicated Respondents state that for a market to function, its participants must be able to rely on some level of certainty, and allowing buyers to retroactively change bilateral contracts that were negotiated at arms-length destroys the stability of contracts and undermines the Commission's market-based rate regime. Indicated Respondents note that the Commission has recognized that "uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments."[443] Indicated Respondents assert that Seattle entered into legitimate bilateral contracts containing rates driven by market fundamentals, and deviating from well-established principles recognizing the stabilizing effects of these contracts would only serve to hinder markets from functioning efficiently in the future.

### (c) Claims Pursuant to Section 309 of the FPA

748. For claims pursuant to section 309 of the FPA, Indicated Respondents state that Seattle must prove that each Respondent engaged in specific violations of a substantive provision of the FPA or of its filed tariff or rate schedule, and the violation resulted in an unjust and unreasonable rate.[444] Indicated Respondents assert that Seattle failed to meet this standard and has only claimed that all sellers violated their tariffs to the extent that they sold power to Seattle above Mr. Hanser's MMCP and Pivotal Unit benchmarks.[445]

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[442] *See* Ex. PNR-1 at 9:1-10:7.

[443] *See 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 6, *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 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), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012). *See also* Ex. PNR-1 at 51:4-53:2.

[444] Order on Rehearing at P 32.

[445] *See* Ex. SCL-110 at 34:22-28, 44:17-23.

749. Indicated Respondents first argue that Seattle's testimony for the Section 309 Period is limited to the period of January 1, 2000 to December 24, 2000.[446] Indicated Respondents note that Seattle has conceded that its testimony pertaining to Section 309 Period does not pertain to the Section 206 Period.[447]

750. Next, Indicated Respondents assert that Seattle has not demonstrated that any Respondent engaged in a specific violation of a substantive provision of the FPA or its tariff. Indicated Respondents note that the Commission clearly stated that no market-wide remedy is available in this proceeding, and that claimants must submit Respondent-specific, contract-specific evidence of unlawful conduct.[448] Indicated Respondents state that Seattle's benchmark analyses are irreconcilable with a Respondent-specific, contract-specific case, and present all of the problems that the Commission has previously weighed in determining not to consider market-wide relief in this proceeding.[449]

751. Indicated Respondents aver that Seattle failed to even identify the spot market contracts between itself and any one of the Respondents. Instead, Seattle based its claims on hourly delivery data.[450] Indicated Respondents contend that the hourly data provides

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[446] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 23 (June 20, 2013) (Order Granting in Part and Denying in Part Motion to Strike) ("any newly filed testimony that does not relate to the section 309 claim period will confuse the issues relevant to Seattle's section 309 claims and must be stricken."). To the extent Seattle also purports to have made section 309 claims for the Section 206 Period, Indicated Respondents argue that Seattle's claims must fail because it has not alleged any statute or tariff violations by the Respondents.

[447] City of Seattle, Washington June 14, 2013 Answer in Opposition to the Indicated Respondents' Expedited Motion to Strike at 6 ("Mr. Hanser's [June 3, 2013] testimony asserts section 309 claims only for the period January 1, 2000 through December 24, 2000"); *see also* Tr. 1901:23-25 (Hanser).

[448] Order on Remand at PP 23-24. *See also Puget Sound Energy, Inc*., 103 FERC ¶ 61,348, at P 35, *order on reh'g*, 105 FERC ¶ 61,183, at P 64 (2003) ("it is not possible to fashion a remedy that would be equitable to all the participants in the Pacific Northwest market").

[449] *See* Order on Remand at P 24 & n.56 (granting market-wide relief in a bilateral market would mean that "sellers following the law would be penalized because of someone else's bad conduct, an unfair and unreasonable result").

[450] Tr. 1961:19-1962:18 (Hanser).

no information about the trader negotiations, including who proposed the price or which deliveries are associated with which contracts.

752. Next, Indicated Respondents argue that even if Seattle's benchmark analyses were cognizable in this case, exceeding marginal cost does not constitute a violation of a statute or tariff within the meaning of section 309. Indicated Respondents state that in *Morgan Stanley*, the Court specifically rejected a similar argument, explaining that "[a] presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract-based regulation."[451]

753. Indicated Respondents assert that Seattle can identify no source of law that prevented the Respondents from selling at prices that Mr. Hanser now condemns with his benchmark analysis. Indicated Respondents assert that Seattle has offered no evidence that FPA Section 205, the WSPP Agreement, or any of the Respondents' market-based rate authorizations contained any particular limitation on purchase or sales prices.[452] Indicated Respondents argue that this is particularly relevant given that the Commission has instituted price caps in other contexts, including in relation to the Western Energy Crisis.[453] Additionally, Indicated Respondents aver that Mr. Hanser's cointegration study likewise fails to show any violation of a statute or tariff within the meaning of section 309.

754. Next, Indicated Respondents state that Seattle attempts to use its benchmarks to prove the existence of market power.[454] Indicated Respondents first assert that Seattle's

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[451] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550-51 (2008) (internal citations omitted). Indicated Respondents acknowledge that the *Mobile-Sierra* inquiry that the Supreme Court considered in *Morgan Stanley* is distinct from the section 309 inquiry at issue here.

[452] Ex. SCL-115 at 11:13-15 ("I do agree with several observations made by Respondents' witnesses that neither the WSPP tariff nor the Respondents' Market-Based Rate authority required Respondents to have sold power to Seattle for prices equal to their marginal costs …").

[453] *See San Diego Gas & Elec. Co. v. Sellers of Energy & Ancillary Servs.*, 93 FERC ¶ 61,294 (2000). *See also Morgan Stanley Capital Grp. Inc. v. Cal. Indep. Sys. Operator Corp.*, 92 FERC ¶ 61,112, at 61,429-30 (2000); *San Diego Gas & Elec. Co. v. Sellers of Energy & Ancillary Servs.*, 95 FERC ¶ 61,418 (2001).

[454] *See* City of Seattle, Washington August 23, 2013 Prehearing Brief at 11, 15-16; Tr. 2043:1-2044:2, 2084:15-2085:1 (Hanser).

investigation of "market power" is the opposite of Respondent-specific, and is instead aimed at obtaining the market-wide remedy that the Commission has repeatedly rejected.[455]

755. Indicated Respondents also contend that Seattle's marginal cost-based benchmarks are not credible evidence of market power. Indicated Respondents state that to conduct a proper market power analysis, one "would have had to consider the circumstances surrounding the execution of buyers' and sellers' transactions with Seattle and whether the transaction prices were affected by physical or economic withholding of supply," and "assess factors such as market share, market concentration, transmission constraints, and other factors that the Commission has assessed under the hub and spoke test."[456] Indicated Respondents note that the Commission's tests applying these considerations include the delivered price test,[457] the hub-and-spoke test,[458] and the Herfindahl-Hirschman Index (HHI).[459] Indicated Respondents assert that Mr. Hanser admitted that he did not attempt to perform any of the methodologies considered by the Commission and other authorities for determining the existence of market power.[460]

756. Indicated Respondents state that because the Commission has previously adopted, or referenced, several reliable methodologies for evaluating market power, raw price data, like those in Mr. Hanser's benchmarks, are the beginning of the market power inquiry, not the end. Thus, when a market participant like Seattle identifies "high prices," it may create inquiry notice for market participants or the Commission to investigate whether market power is being exercised. For example, Mr. Cavicchi testified that a price could be high enough to invite inquiry as to whether a specific generator withheld

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[455] Order on Remand at P 24; Order on Rehearing at PP 28-29.

[456] Ex. JDG-1 at 18:1-19:6.

[457] *Electricity Market Transparency Provisions of Section 220 of the Federal Power Act*, 130 FERC ¶ 61,039, at P 11 (2010).

[458] *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, FERC Stats. & Regs. ¶ 31,044, at 30,117 (1996), *reconsideration denied*, Order No. 592-A, 79 FERC ¶ 61,321 (1997).

[459] *Analysis of Horizontal Market Power under the Federal Power Act*, 138 FERC ¶ 61,109, at P 4 & n.9 (2012).

[460] Tr. 1948:25-1960:16 (Hanser).

supply.[461] Indicated Respondents argue that Seattle has had ample opportunity to investigate whether any of the Respondents possessed market power and engaged in misconduct that violated a statute or tariff, but has not conducted any such inquiry.[462]

757. Indicated Respondents also contend that Mr. Hanser's MMCP benchmark is not a meaningful indicator of market power in the Pacific Northwest. Indicated Respondents note that even in the organized California market for which it was designed, the MMCP was never used to determine the existence of market power.

758. Moreover, Indicated Respondents state that the "MMCPs were constructed based on what was considered to be a marginal unit in the California market" and were "not constructed based on the universe of units that were serving or could serve the Pacific Northwest."[463] Thus, Mr. Cavicchi explained that "MMCPs are applicable to the California organized wholesale markets for the purposes of the Commission California refund proceeding and have no relationship to the Pacific Northwest bilateral spot market."[464] Indicated Respondents further state that the Commission rejected the use of the MMCP market-wide remedy adopted for the organized California markets as inappropriate for the bilateral Pacific Northwest spot market where "each seller receives only what a specific buyer agrees to pay for a given transaction and each buyer as the opportunity to negotiate a lower price."[465]

759. Indicated Respondents assert that there is no basis for assuming that the MMCP has any relationship to price formation in the Pacific Northwest bilateral markets. Indicated Respondents note that prices in the Pacific Northwest were generally higher than those in California.[466] Indicated Respondents aver that this makes the MMCP a poor proxy for prices in the Pacific Northwest. Additionally, Indicated Respondents assert that any reliance on Mr. Hanser's cointegration analysis would be inappropriate because the

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[461] Tr. 3359:14-17 (Cavicchi).

[462] *See, e.g.,* Tr. 2168:24-2169:11 (Hanser).

[463] Tr. 2019:15-2020:2 (Hanser).

[464] Ex. JDG-1 at 17:5-10.

[465] Order on Remand at P 24.

[466] Tr. 1978:2-4 (Hanser). *See also* Ex. PNR-1 at 224.

analysis shows only how prices move in relation to each other, but does not explain or inform absolute levels.[467]

760. Next, Indicated Respondents discuss Mr. Hanser's Pivotal Unit Benchmark. Indicated Respondents argue that the Pivotal Unit Benchmark is inappropriate because it fails to consider opportunity costs or scarcity rents.[468] Indicated Respondents note that a 2000 Staff report confirms that "a generator's true marginal cost is the generator's opportunity cost of selling into a particular market."[469] By excluding opportunity costs and scarcity rents, Indicated Respondents contend that the Pivotal Unit Benchmark is a lower bound of competitive prices.[470]

761. Furthermore, Indicated Respondents aver that the Pivotal Unit Benchmark is wrongly limited to only one element−the value of fuel burned to produce a megawatt of electricity−of one type of generating facility−natural gas-fired generation.[471] Indicated Respondents state that the benchmark ignores an individual seller's actual marginal costs[472] and does not consider the cost to purchase energy for later resale.[473]

762. Indicated Respondents also state that Mr. Hanser's revised his Pivotal Unit Benchmark analysis by substituting actual natural gas costs for a proxy of the costs and excluding sales below the benchmarks from consideration.[474] Indicated Respondents

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[467] Tr. 1977:18-1978:1 (Hanser).

[468] Tr. 2031:13-15 (Hanser).

[469] Ex. SCL-111 at 101. *See also* Tr. 3372:7-3373:3 (Cavicchi).

[470] *Compare* Tr. 2186:5-7 (Hanser) (testifying that "the Pivotal Unit benchmark is, in some sense, an absolute upper bound on anything that could look like a competitive market.") *with* Tr. 4126:18-4127:6 (Hogan) (describing that aside from identifying evidence of withholding, a correct way of determine a competitive price would be to estimate the costs of the marginal unit "and try to estimate the scarcity and opportunity costs that [Mr. Hanser] left out to get away from the lower bound to something that's more realistic as an estimate of competitive price").

[471] Ex. SCL-115 at 8:8-9.

[472] Tr. 2016:1-7, 2086:15-18 (Hanser).

[473] Tr. 2083:20-2084:7 (Hanser).

[474] Tr. 2033:1-7 (Hanser).

aver that transactions between buyers and sellers in the marketplace reflected the actual natural gas costs, not post hoc reconstructed natural gas costs.[475] Indicated Respondents state that if actual gas prices are used and all sales are considered, many of the alleged "premiums" turn negative.[476] Indicated Respondents further assert that even when using constructed natural gas costs, the Respondents' sales to Seattle were priced below the Pivotal Unit Benchmark more than sixty percent of the time.[477]

763. Regardless, Indicated Respondents state that the alleged "premiums" that Mr. Hanser calculated over his benchmarks for the Section 309 Period were less than ten percent of Seattle's wholesale energy costs in 2000.[478] Therefore, Indicated Respondents conclude that Seattle failed to provide evidence that Respondents' contracts resulted in unjust and unreasonable rates.

764. Lastly, Indicated Respondents contend that even if sales above the benchmark are a violation, Seattle should be barred from recovery under the unclean hands doctrine because it engaged in the same violation. Indicated Respondents state that the Commission has made clear that under section 309, the award of refunds or restitution is a form of "equitable relief," and as such, should not be awarded to a party who engaged in the very same activity for which it is seeking redress.[479] Indicated Respondents assert that Seattle was selling at prices comparable to those at which Respondents sold to

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[475] Tr. 3349:1-12 (Cavicchi).

[476] *See* Ex. JDG-11.

[477] Ex. SCL-115 at 8:19-20; Tr. 2066:19-21 (Hanser).

[478] *See* Tr. 2211:5-2214:9 (Hanser).

[479] *See Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67, 73, 76 (D.C. Cir. 1992) (finding that section 309 of the FPA confers the power to order refunds to FERC, but that "refunds are a form of equitable relief, akin to restitution, and the general rule is that agencies should order restitution only when 'money was obtained in such circumstances that the possessor will give offense to equity and good conscience if permitted to retain it'") (citations omitted). *See also Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814 (1945) (defining the unclean hands doctrine as "closing the door of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief").

Seattle.[480] Indicated Respondents note that when asked about Seattle's pricing, Mr. Hanser stated that he "wouldn't condone Seattle's behavior."[481]

### (d) Proper Definition of Spot Market

765. Indicated Respondents state that spot market transactions are transactions with a duration of 24 hours or less, prescheduled no more than 24 hours in advance of delivery, consistent with the Western Electricity Coordinating Council's (WECC) prescheduling calendar and hourly scheduling practices and timelines.[482] Indicated Respondents assert that this definition is based on firsthand knowledge of Pacific Northwest markets and published sources.[483] Furthermore, Indicated Respondents note that the Commission has expressly adopted this definition of spot market in the WECC: "Spot market sales in the WECC are sales that are 24 hours or less and are entered into the day of or day prior to delivery."[484]

766. Indicated Respondents aver that Seattle has not offered any credible evidence that would undermine Indicated Respondents' definition. Indicated Respondents note that Seattle presented no fact witness with knowledge of the Pacific Northwest markets at the time.[485] Additionally, Indicated Respondents state that Mr. Morter, Seattle's only fact witness, admitted that his testimony was not based on communications with anyone with knowledge of the Pacific Northwest markets at the time.[486]

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[480] Ex. JDG-1 at 19:10-21; *see also* Ex. TAE-23 at 11:10-21; Tr. 2018:25-2019:6 (Hanser).

[481] Tr. 2042:18-23 (Hanser).

[482] All Respondents provide the same definition of spot market transactions. *See, e.g.,* Ex. AVE-1 at 8:10-13.

[483] *See* Ex. JDG-1 at 7:3-6; Ex. CCG-1 at 7:2-17; Tr. 3365:5-23 (Cavicchi).

[484] *W. Elec. Coordinating Council*, 133 FERC ¶ 61,026, at P 1 n.3 (2010); *see also San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418, at n.3 (2001) ("the terms 'spot markets' or 'spot market sales' means sales that are 24 hours or less and that are entered into the day of or day prior to delivery").

[485] Tr. 1897:18-20, 2150:11-13 (Hanser); Tr. 3154:4-8, 3157:18-3158:1, 3222:13-23 (Morter).

[486] Tr. 3158:16-3159:16, 3236:20-3237:21 (Morter).

767. Indicated Respondents state that to support his definition of spot market, Mr. Morter testified that he relied on the testimony of witnesses from a prior proceeding and information from the websites of Bonneville Power Administration (BPA) and the Department of the Interior (DOI).[487] However, Indicated Respondents note that Mr. Morter is not an expert witness and did not present his qualifications to review other entities' websites or prior testimony from witnesses. Thus, Indicated Respondents aver that there is no basis on which Mr. Morter's testimony should be given any weight.[488]

768. Next, Indicated Respondents argue that the information that Mr. Morter cited for purposes of coming up with his definition of spot market does not support Seattle's position. Indicated Respondents note that Mr. Morter's exhibits include testimony from a number of witnesses who define spot market consistently with the Respondents' witnesses.[489] Additionally, the definition of spot market from a witness for BPA directly contradicts the definition of spot market that Mr. Morter supports.[490] Indicated Respondents also aver that Mr. Morter ignores portions of the testimony of PacifiCorp witness Stan Watters, such as when he testifies that the Commission should not order refunds in this proceeding.[491] Indicated Respondents also state that Mr. Morter confuses two different terms from the BPA website – spot-market price and short-term power purchases in the forward markets.[492]

769. Furthermore, Indicated Respondents note that despite defining spot market in relation to the buyer's long-term planning process, Mr. Morter testified that he did not review Seattle's long-term resource plan,[493] and Seattle presented no evidence of its

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[487] *See* Ex. SCL-95 at 7:13-17.

[488] *See Pub. Serv. Co. of N.M.*, 11 FERC ¶ 63,002 (1980) (Harfeld, ALJ) ("Witness Robison's testimony on this point, consisting largely of statements of third persons not present and not subject to cross-examination, is entitled to little weight. Such testimony is pure hearsay, and, although not excludable from administrative hearings on that basis *per se*, its value is questionable for much the same reasons that hearsay is, with certain exceptions, inadmissible in judicial proceedings").

[489] *See, e.g.*, Ex. SCL-37 at 17:3-8; Ex. SCL-82 at 36.

[490] *See* Ex. SCL-82 at 27.

[491] *See* Ex. SCL-83 at 2.

[492] *See* Ex. SCL-95 at 7:18-8:11.

[493] Tr. 3160:16-3161:7 (Morter).

long-term resource planning.[494] Indicated Respondents also assert that Seattle's trading desk distinguished transactions as hour-ahead, day-ahead, or other.[495] Indicated Respondents note that this is consistent with the databases provided by Mr. Morter with his testimony.[496]

770. With respect to Mr. Hanser's testimony, Indicated Respondents note that Mr. Hanser has only minimal experience with the Pacific Northwest market[497] and did not speak with anyone who actually traded energy in the Pacific Northwest to form his definition of spot market.[498] Additionally, Indicated Respondents state that Mr. Hanser conceded that he has never seen this definition of spot market outside of testimony presented in this hearing,[499] and has never advanced this definition of spot market in anything he has written or published.[500] Indicated Respondents assert that Mr. Hanser did not undertake any type of expert analysis of the hearsay information he purported to adopt,[501] and merely relied upon the same material that Mr. Morter relied upon.[502]

771. Lastly, Indicated Respondents contend that Seattle's definition of spot market sales is inconsistent with common industry and other market usage of the term "spot sale."[503] Moreover, Indicated Respondents aver that Seattle's definition is unworkable because it is dependent on the intention of the Seattle trader when he or she made the purchase (i.e. whether or not Seattle deemed the transaction to be part of its long-term

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[494] Tr. 3174:22-3175:3 (Morter).

[495] *See* Tr. 3210:14-13 (Morter).

[496] Ex. SCL-95 at 10:10-24.

[497] Tr. 1895:6-1896:6, 2150:11-13 (Hanser).

[498] Tr. 2153:11-14 (Hanser).

[499] Tr. 2152:16-22 (Hanser).

[500] Tr. 2153:6-9 (Hanser).

[501] Tr. 1924:15-1925:18, 2151:10-2152:15 (Hanser).

[502] *See* Ex. SCL-76 at 11:10-12.

[503] *See* Ex. AVI-67 at 14-16; Ex. AVE-12 at 9:2-4; Ex. CPM-2 at 6:3-4; Ex. EP-2 at 6:19-7:1; Ex. PPL-10 at 5:17-20; Ex. PSC-4 at 6:9-10.

planning process).[504] Indicated Respondents note that the confirmation agreements memorializing the sales by the Respondents to Seattle did not specify whether a particular transaction was part of Seattle's long-term planning process.[505]

### 3. PPL Montana, LLC and PPL EnergyPlus, LLC Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

772. PPL argues that Seattle has failed to demonstrate that PPL engaged in unlawful activity. PPL notes that Seattle's only two witnesses, Mr. Hanser and Mr. Morter, both stated that they were not alleging any illegal conduct by any of the Respondents.[506] PPL notes that in the Final Joint Statement of Issues, Seattle stated that it has not alleged undue price discrimination, False Export, or selling non-firm energy as firm.[507] PPL further asserts that Ms. Spear's uncontradicted testimony demonstrates that PPL did not, and could not engage in undue price discrimination, False Export, or selling non-firm energy as firm.[508]

773. Next, PPL states that Seattle suggested that it was alleging duress, fraud, or bad faith and the exercise of market power against at least some Respondents,[509] but failed to present any evidence against PPL at hearing. PPL avers that Seattle presented no evidence of market power or any anti-competitive behavior by PPL, nor even suggested that PPL's pricing and behavior was inconsistent with the Commission's market-based rate regime.

774. PPL states that Seattle also claims that other sellers in Western markets engaged in a variety of actions that violated provisions of the FPA, the Commission's regulations, their tariffs, and/or the WSPP Agreement.[510] PPL asserts that accusations of gaming by

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[504] *See* Ex. JDG-1 at 10:18-11:7; Ex. AVI-67 at 21:14-20; Ex. PPL-10 at 6:6-17.

[505] *See* Tr. 3283:20-3284:2 (Morter).

[506] Tr. 2074:10-15, 2116:24-2117:1 (Hanser); Tr. 3278:7-20 (Morter).

[507] Final Joint Statement of Issues at 14, 19, 23. *See also* Tr. 2118:10-2121:5 (Hanser).

[508] Ex. PPL-1 at 8-11.

[509] *See* Final Joint Statement of Issues at 3-5, 27-29.

[510] Ex. SCL-1 at 4:18-20.

other sellers or general dysfunction in the Western energy markets were expressly rejected by the Commission as grounds for a refund claim in this proceeding.[511] Moreover, PPL notes that Mr. Hanser admitted that he provided no competent evidence to support his claims regarding other sellers.[512]

775. PPL states that at hearing, Mr. Hanser testified that the only conduct he identified with respect to PPL for consideration at the hearing was "that PPL allegedly charged prices above the benchmarks [he] calculated."[513] Mr. Hanser alleged that this is the basis for claim that PPL violated "the FPA, the Commission's regulations, their tariffs, and/or the WSPP Agreement."[514] However, PPL asserts that Mr. Hanser did not conduct a "benchmark analysis" with respect to the Section 206 Period.[515] Thus, PPL concludes that Seattle failed to provide any evidence of unlawful activity by PPL, as required by the Commission.

776. Next, PPL avers that having failed to present evidence of unlawful activity by PPL, Seattle cannot demonstrate that unlawful activity affected the negotiation of specific bilateral contracts. PPL states that Mr. Hanser, in his Section 206 testimony, did not even review PPL's transactions.[516] PPL further notes that Seattle did not identify the specific contracts between PPL and Seattle. Rather, Seattle only submitted spreadsheets that included price, quantity, and delivery start and end information.[517] PPL states that Mr. Morter, who sponsored the spreadsheets, admitted that the spreadsheets do not identify contracts,[518] and that he had no personal knowledge of the transactions between PPL and Seattle.[519] PPL further notes that the data do not include any information related

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[511] Order on Remand at PP 21, 24; Order on Rehearing at P 26.

[512] Tr. 2074:10-15, 2116:24-2117:1 (Hanser).

[513] Tr. 2071:7-13 (Hanser).

[514] Ex. SCL-1 at 4:18-20.

[515] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 23 (issued June 20, 2013) (Order Granting in Part and Denying in Part Motion to Strike).

[516] Tr. 1901:2-25 (Hanser) (confirming that he did not review any sales or transaction data between Seattle and the respondents for his Section 206 testimony).

[517] Ex. SCL-91; Ex. SCL-103.

[518] Tr. 3297:21-3299:2 (Morter).

to the negotiation of the contracts, such as which party initially offered the price or the date on which the parties agreed on the price.[520]

777. With respect to Mr. Hanser's cointegration analysis, PPL contends that the cointegration analysis is not relevant to PPL's sales to Seattle because the analysis evaluates prices only at Mid-C and COB,[521] even though PPL's delivery points to Seattle were hundreds of miles away.[522]

778. Next, PPL argues that its sales to Seattle were legitimate business behavior. PPL asserts that it simply sold energy at prevailing prices in the marketplace. PPL notes that Mr. Morter acknowledged that any rational seller would sell at the market price because otherwise "they're leaving money on the table."[523] PPL further states that Seattle sold energy at the same or higher prices.[524] Thus, PPL argues that if this activity somehow did not constitute legitimate business behavior, then Seattle itself transacted with unclean hands and cannot maintain a claim for refunds in any event.[525]

779. Lastly, PPL asserts that based on the Respondents' definition of spot market, many of the sales that Seattle seeks refunds for are outside the scope of this proceeding. PPL states that approximately $10.5 million in sales by PPL to Seattle during the Section 206 Period were not made in the Pacific Northwest bilateral spot market, but are associated

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[519] Tr. 3154:4-8, 3157:25-3158:1 (Morter).

[520] *See* Tr. 3298:21-3299:2 (Morter).

[521] Ex. SCL-1 at 22:20-21; Ex. SCL-110 at 66:16-17.

[522] Ex. PPL-7 at 3:21-24 (stating that ninety-eight percent of hourly deliveries for which Seattle is claiming refunds were made to Garrison, Hot Springs, Amps, Burke, or LaGrande); Ex. PPL-10 at 3:17-18 (explaining that virtually all of PPL's sales during the Section 309 Period were delivered to the boundary of the Montana Power Company control area).

[523] Tr. 3181:22-3182:16 (Morter).

[524] Ex. PPL-7 at 7; Ex. PPL-4 at 8-9; Ex. JDG-1 at 19-20; Ex. JDG-6.

[525] *See Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814 (1945) (defining the unclean hands doctrine as "clos[ing] the door of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief").

with three term forward contracts, each entered into weeks before the start of delivery and for a duration of a month or longer.[526] PPL contends that the non-spot contracts fall outside the narrow scope of this proceeding, and any claims by Seattle in connection with these contracts should be rejected.[527]

### (b) Claims Pursuant to Section 309 of the FPA

780. PPL asserts that Seattle has not demonstrated that PPL engaged in a specific violation of a substantive provision of the FPA or its filed tariff or rate schedule. PPL states that the only conduct identified by Seattle's witnesses was that "PPL allegedly charged prices above the benchmarks [Mr. Hanser] calculated."[528] However, PPL avers that Seattle failed to explain what tariff or source of law prohibited PPL from selling at those prices. Additionally, PPL contends that Seattle failed to identify any specific contracts or contract rates between PPL and Seattle.[529]

781. Furthermore, PPL states that even if the benchmarks were considered relevant, PPL had a negative "premium" when actual natural gas costs and sales below the benchmark are considered.[530] PPL states that netting the sales above and below the benchmark takes account of that fact that multi-hour contracts on average may not result in a "premium" because the price may fluctuate above and below the "benchmark" in individual hours.[531] PPL states that the negative "premium" is consistent Mr. Hanser's initial calculations, which showed that PPL had a negative average "premium" for its sales to Seattle in every month of 2000, except August.[532] PPL asserts that even for the

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[526] Ex. PPL-1 at 9:1-14; Ex. PPL-4 at 13:1-14:18. *See also* Ex. PPL-3.

[527] *See* Order on Remand at P 2 ("[t]his matter concerns bilateral wholesale energy contracts entered into in the Pacific Northwest spot market").

[528] Tr. 2071:7-13 (Hanser).

[529] PPL states that Seattle's data for the Section 309 Period are similarly flawed as the data for the Section 206 Period.

[530] Ex. JDG-11.

[531] *See* Tr. 2052:10-2059:12 (Hanser).

[532] Ex. SCL-110 at 42.

single month with a positive premium, Seattle never attempted to tie the prices in August 2000 to any real world facts that would show a violation occurred.[533]

782. Lastly, PPL asserts that based on the Respondents' definition of spot market, many of the sales that Seattle seeks refunds for are outside the scope of this proceeding. PPL states that for the Section 309 Period, Ms. Spear identified a written confirmation of a forward contract with Seattle for approximately $2 million that was executed weeks prior to the first delivery and had a three month term.[534]

### 4. Constellation Energy Commodities Group, Inc. Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

783. Constellation argues that Seattle presented no evidence that Constellation committed any specific unlawful activity,[535] or that such activity resulted in unjust and unreasonable rates in any contract between Constellation and Seattle. Constellation avers that Seattle made no claims of duress, fraud, or bad faith; undue price discrimination; False Export; selling non-firm energy as firm, or exercise of market power.[536] Constellation asserts that Mr. Hanser's Section 206 testimony only makes allegations of market activity by non-respondent sellers, and contains no allegations regarding Constellations activities.[537] Constellation states that the Commission specifically rejected Seattle's approach, stating that "in the context of short-term bilateral contract sales, a market-wide refund remedy for tariff violations would be appropriate only if a complainant clearly demonstrated that all sellers had engaged in tariff violations."[538]

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[533] Tr. 2029:7-2031:12 (Hanser).

[534] Ex. PPL-10 at 7:3-8:4. *See also* Ex. PPL-11.

[535] Tr. 2074:10-15, 2116:24-2117:1 (Hanser); Tr. 3278:7-20 (Morter).

[536] *See* Final Joint Statement of Issues at 14, 19, 23. *See also* Tr. 2118:13-2121:20 (Hanser).

[537] *See* Ex. CCG-1 at 2-5.

[538] *California ex rel. Brown, v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 77 (2011).

784. Constellation states that Mr. Hanser's relies only on his theory that the prices in the Pacific Northwest market exceeded what he considered competitive levels.[539] Specifically, Mr. Hanser uses his cointegration analysis to assert that markets in California and the Pacific Northwest are interrelated, and therefore, the "uneconomic actions" by non-respondent sellers in California affected prices in the Pacific Northwest.[540] Constellation notes that Seattle claims that it faced "economic duress" due to the alleged "uneconomic conduct" in California, and that certain sellers exercised "bad faith" in negotiating transactions with Seattle based on prevailing market prices when Seattle needed to buy power to serve its load.[541]

785. Constellation argues that Mr. Hanser presents no evidence that Constellation engaged in any such "uneconomic conduct,"[542] and Mr. Hanser's analysis fails to demonstrate a causal relationship between Constellation's actions and the prices Constellation charged Seattle.[543] Constellation further notes that Mr. Hanser also agreed that his cointegration analysis does not indicate that any unlawful conduct occurred, is not a specific transaction analysis, and does not show a direct link or casual connection between unlawful conduct – or even uneconomic conduct – and a specific seller's contract.[544]

786. Constellation also notes that Professor Hogan found that Mr. Hanser's statistical analysis is flawed because it failed to isolate the various factors that caused high prices in the Pacific Northwest.[545] Thus, Constellation concludes that Mr. Hanser's cointegration analysis does not, and cannot, meet the legal requirements under *Mobile-Sierra* of showing that illegal activity affected the price in particular contracts.

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[539] Tr. 2121:16-20 (Hanser).

[540] Ex. SCL-1 at 23:1-3.

[541] *See* Final Joint Statement of Issues at 3-5.

[542] *See* Tr. 2074:12-15 (Hanser).

[543] *See* Ex. SCL-76 at 25:3-6. *See also* Tr. 1966:25-1967:16 (Hanser).

[544] Tr. 1979:13-23, 1977:11-12, 2090:7-10 (Hanser).

[545] Tr. 4138:18-4139:7 (Hogan); Ex. PNR-1 at 42:7.

787. Next, Constellation asserts that Seattle presents no evidence addressing contract negotiations with Constellation from the Section 206 Period.[546] Thus, Constellation contends that claims that Seattle lacked bargaining power in negotiations are nothing more than speculation. Conversely, Constellation states that it presented the testimony of Mr. Marlatt, who had extensive knowledge about all of the bilaterally-negotiated transactions that took place during the Section 206 Period, and knew the basis for the prices Constellation charged in its contracts with Seattle.[547]

788. Furthermore, Constellation avers that Seattle did not even identify the specific contracts related to its section 206 claims.[548] Constellation states that Mr. Marlatt did provide evidence that identified the Constellation/Seattle transactions by transaction ID number, showing the term, strike date, delivery date, price, duration, time, and delivery point.[549] Based on this data, Mr. Marlatt showed Constellation's "all-in" delivered energy prices, which encompass the total costs Constellation incurred in meeting obligations under its transactions with Seattle.[550] Constellation asserts that the data show that Constellation's transactions during the Section 206 Period were just and reasonable and reflect costs and margins that a marketer reflects in its market-based sales.

789. Constellation also asserts that that it charged market-based rates that reflect supply and demand in a manner consistent with a seller in a competitive market. Constellation notes that Professor Hogan testified that the prices sellers charged in the Pacific Northwest "were consistent with tight market conditions" and that "market conditions are sufficient to explain the price levels at the time."[551] Professor Hogan stated that the

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[546] Tr. 1894:12-22, 2074:19-22, 2161:15-24 (Hanser); Tr. 3153:1-24 (Morter). Constellation notes that Mr. Morter admits that prior to joining Seattle in 2012, he never even worked in the Pacific Northwest market in any capacity. *See* Tr. 3153:21-3154:8 (Morter)

[547] Ex. CCG-12 at 2:18-21.

[548] *See, e.g.*, Tr. 3272:8-3273:18 (Morter); Tr. 3298:1-24 (Morter); Ex. CCG-12.

[549] Ex. CCG-12 at 4-14; Ex. CCG-13.

[550] *See* Ex. CCG-12 at 3-4.

[551] *See* Ex. PNR-1 at 11:17-23.

reduction in supply due to the decreased output of hydro-power was the most important market condition affecting prices at the time.[552]

790. Next, Constellation notes that it entered into two monthly transactions with Seattle in January 2001 for the month of February of 2001.[553] Constellation states that these transactions represent approximately forty-five percent of the total revenue associated with sales from Constellation to Seattle.[554] Constellation contends that these two transactions constitute forward, not spot, transactions. Furthermore, Constellation asserts that even under Seattle's proposed definition, the two contracts should be excluded because the transactions were entered into in the current month for deliveries in the next month.[555]

791. Constellation also asserts that Seattle wrongly included "bookout" transactions.[556] Constellation states that "bookouts" are mutually-agreed upon transactions that constitute a financial offset one way or another between the parties.[557] Constellation states that "bookouts" are a standard industry practice and since there is no physical flow and no payment, there cannot be a refund associated with the transactions.[558]

792. Constellation further avers that Seattle sold energy at prices that were comparable to, or higher than, the prices Constellation charged Seattle for power.[559] Constellation states that Mr. Cavicchi analyzed the transaction data and determined that Seattle sold power to other entities at prices that were comparable to, or higher than, the prices

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[552] *Id*. at 33-36.

[553] Ex. CCG-13; Ex. CCG-15; Ex. CCG-16.

[554] CCG-1 at 6.

[555] Tr. 3211:22-3212: 9 (Morter).

[556] Constellation states that in "bookouts," instead of flowing power both ways, the power is offset and no power actually flows. Tr. 2170:8-10 (Hanser).

[557] Tr. 2170:13-16 (Hanser).

[558] Ex. CCG-14 at 8:13-9:17 (describing the offsets for bookouts that occurred between Constellation and Seattle during the Section 206 Period); Ex. CCG-15.

[559] *See* Ex. CCG-14 at 7:8-8:2; Ex. CCG-12 at 4:13-15.

Constellation charged Seattle during that very same hour.[560] Constellation asserts that Seattle actively participated in the Pacific Northwest market and profited from tight supply conditions.[561] Thus, Constellation concludes that Seattle does not have "clean hands" and should not be rewarded refunds.[562]

793. Next, Constellation argues that Seattle applied the wrong legal standard in its attempt to overcome the *Mobile-Sierra* presumption by showing "excessive burden on consumers." Constellation avers that Seattle wrongly relied on its cointegration study to claim that prices in the Pacific Northwest were unreasonably high. However, Constellation notes that Seattle does not make any claim that Constellation's contract rates seriously harmed the public interest, or that any unfair dealings at the contract formation stage directly influenced the contract rate. Constellation contends that Seattle's theory that high prices in the Pacific Northwest avoid the *Mobile-Sierra* presumption ignores the Commission's clear instruction regarding the *Mobile-Sierra* presumption.[563]

794. Additionally, Constellation notes that Professor Hogan asserted that "high" prices alone do not establish undue burden or serious harm to consumers so as to overcome *Mobile-Sierra*, and that "in the absence of withholding and in the absence of something which is affecting the market clearing prices, then the excess burden is zero."[564] Constellation asserts that Seattle made no showing and presented no evidence that

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[560] *See* Ex. CCG-15. Specifically, Mr. Cavicchi found 291 instances where Seattle purchased energy from Constellation in an hour and simultaneously sold power to another entity in the Pacific Northwest at a higher price in that same hour. *See* Ex. CCG-1 at 6:6-9.

[561] *See* Ex. CCG-1 at 6:6-9.

[562] Constellation states that "[c]ustomer refunds are a form of equitable relief, akin to restitution, and the general rule is that agencies should order restitution only when money was obtained in such circumstances that the possessor will give offense to equity and good conscience if permitted to retain it." *Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67, 75-76 (D.C. Cir. 1992). Constellation further notes that Seattle's own witness agreed that Seattle should provide credits or refunds to those entities that purchased power from Seattle during this period. *See* Tr. 3243:4-8 (Morter).

[563] Order on Rehearing at P 14 (alleging "high contract rates across an entire market" is insufficient to overcome the *Mobile-Sierra* presumption).

[564] Tr. 4141:12-15 (Hogan).

Constellation or any other respondent withheld electricity from the market.[565] Constellations further notes that Mr. Morter testified that market fundamentals led to high prices in the Pacific Northwest.[566]

### (b) Claims Pursuant to Section 309 of the FPA

795. Constellation argues that Seattle failed to meet its burden to demonstrate that Constellation engaged in any specific violation of the FPA or a tariff. Constellation states that Seattle's market power allegations, based on Mr. Hanser's benchmark analyses, are contrary to established court and Commission precedent.[567]

796. Constellation also asserts that Seattle engages in a collateral attack on the Commission's market-based rate program by asserting that prices outside a "zone of reasonableness" based on hypothetical marginal costs are unjust and unreasonable. Constellation argues that Seattle seeks to re-litigate the Commission's previous findings regarding Constellation's market-based rate application.[568]

797. Next, Constellation discusses Mr. Hanser's benchmark analysis.[569] Constellation first notes that the benchmark analysis ignores the fact that some of the sellers, like Constellation, acted as pure power marketers and did not own any generating assets in this market. Thus, Constellation's actual costs reflect the cost of the power that it purchased and delivered to Seattle, not the costs of some hypothetical generating unit in California or in the WECC.[570] Constellation states that Mr. Hanser admitted that he did

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[565] *See* Tr. 2186:13-20 (Hanser); Tr. 4108:21-4110:6 (Hogan).

[566] Tr. 3256: 24-3261:10 (Morter).

[567] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548 (2008) (holding that the zone of reasonableness test "fails to afford an adequate level of protection to contracts"). *See also W. Elec. Coordinating Council*, 133 FERC ¶ 61,026, at PP 14-15, 19 (2010).

[568] *See California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 125 FERC ¶ 61,016, at PP 24-29 (2008).

[569] Mr. Hanser concedes that the sole basis for his claim of a violation of section 309 is that prices respondents charged exceeded his benchmarks. Tr. 2121:16-20 (Hanser).

[570] Ex. CCG-14 at 4:1-5.

not prepare a benchmark for entities that only acted as marketers, and that he did not consider Constellation's purchase costs as a marketer of the power.[571] Accordingly, Constellation concludes that the benchmarks bear no relevance to determining the just and reasonable market-based rates for Constellation's sales or determining its costs of power sales as a non-generation-owning, power marketer.

798. Constellation also asserts that Mr. Hanser ignored the fact that, in adopting the MMCP in the California Refund proceeding, the Commission found that the CAISO market suffered from inherent design flaws that are not relevant in the Pacific Northwest.[572] Constellation states that as a result of the California market design, the ISO purchased roughly eighty percent of the energy to supply California consumers in the spot market.[573] Constellation notes that there has been no determination that the Pacific Northwest market design was similarly flawed.

799. Furthermore, Constellation contends that the Commission did not find that California market sellers charged uncompetitive rates based on a comparison of actual prices to the MMCP price. Rather, the Commission found that the California market design and market rules were flawed and could potentially allow the exercise of market power.[574] Moreover, the Commission acknowledged the MMCP was not a perfect substitute for competitive price, but only a proxy for the rate that would have resulted, but for the unworkable and ill-conceived California market design. Thus, Constellation asserts that the application of MMCP as a test to determine if sellers exercised market-power in their bilaterally-negotiated contracts with Seattle is improper and unprecedented.

800. Constellation also states that even assuming the appropriateness of the benchmarks, Respondents' sales were typically lower than the benchmark. Constellation notes that Mr. Hanser acknowledged that he would not be concerned if sellers exceeded the benchmarks from time to time.[575] Constellation asserts that collectively, Respondents

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[571] Tr. 2086:19-24, 2091:23-2092:2 (Hanser).

[572] Specifically, LSEs were forced to purchase virtually all of their energy from the CalPX; could not enter into long-term forward contracts; and were required to bid generation into the market.

[573] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,359-60 (2000).

[574] *Id.*

[575] Tr. 2043:13-2044:15 (Hanser).

charged over the Pivotal Unit Benchmark only 38.6 percent of the time.[576] Constellation notes that Mr. Hanser makes no judgment as to whether 38.6 percent requires the Commission to take any action in this case.[577]

801. Lastly, Constellation argues that equity demands that the Commission not order refunds. Constellation states that the Commission may require the remedy of "disgorgement" of profits "[i]n the event an entity acquires unjust profits through a violation of a statute, regulation or order."[578] Constellation asserts that Mr. Hanser and Mr. Morter both concede that they do not even allege Constellation engaged in unlawful activity and Seattle provided no evidence that Constellation acquired "unjust profits."

802. Constellation states that Seattle's sales to Constellation greatly exceeded the amount (in both volume and revenue) of Constellation's sales to Seattle during the Section 309 Period.[579] Specifically, Seattle sold eighty-seven percent more megawatt-hours to Constellation and received seventy-six percent more revenue.[580] Additionally, Constellation states that Seattle's prices to Constellation significantly exceeded the marginal-cost based benchmarks that Seattle developed in each month of the Section 309 Period[581] and charged Constellation higher prices in October of 2000 than Constellation charged Seattle.[582] Constellation notes that Mr. Hanser stated that he "would not condone SCL's behavior in this market" if Seattle sold energy above the MMCP.[583]

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[576] Ex. SCL-115 at 8:18-20.

[577] *See* Tr. 2069:22-25 (Hanser).

[578] *Enforcement of Statutes, Regulations and Orders*, 123 FERC ¶ 61,156, at P 42 (2008); *Barclays Bank PLC,* 144 FERC ¶ 61,041, at P 148 (2013) (disgorgement prevents unjust enrichment by depriving "wrongdoers of the profits obtained from their violations").

[579] Ex. CCG-12 at 14:3-12; Ex. CCG-13.

[580] *See* Ex. CCG-12 at 14:5-12.

[581] *Id.* at 12:1-13:15 & Table 1.

[582] *See* Tr. 2079:22-2083:8 (Hanser).

[583] Tr. 2042:18-20 (Hanser).

803. Constellation asserts that Seattle cannot equitably benefit from what it classifies as "unjust prices" that it charged in its sales to Constellation, while at the same time demand that Constellation refund equal or lower charges for its sales to Seattle. Constellation contends that Seattle does not have "clean hands" that would permit it to demand refunds from Constellation.[584]

### 5. Public Service Company of Colorado Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

804. PSCo argues that Seattle has failed to demonstrate that PSCo violated the WSPP Agreement or PSCo's market-based rate tariff, or otherwise engaged in unlawful market activity during the Section 206 Period.[585] PSCo notes that Mr. Hanser fails to make any specific reference to PSCo at all in his prefiled testimony.[586] With respect to Seattle's claims that seller's exercised market power, PSCo states that in October 2000, PSCo filed a revised market-based rate tariff with an updated market power analysis,[587] and the Commission determined that PSCo did not possess the ability to exercise market power.[588]

805. PSCo also contends that the prices Seattle paid were not the result of unlawful activity by PSCo or any other respondent, but were instead the result of legitimate market forces. PSCo also notes that Seattle has not identified any specific contracts between

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[584] *Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67 (D.C. Cir. 1992) (finding that section 309 of the FPA confers upon FERC the power to order refunds, but that "refunds are a form of equitable relief, akin to restitution, and the general rule is that agencies should order restitution only when 'money was obtained in such circumstances that the possessor will give offense to equity and good conscience if permitted to retain it'") (citations omitted). *See also Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814 (1945) (defining the unclean hands doctrine as "closing the door of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief").

[585] Tr. 2074:12-15 (Hanser); Tr. 3278:7-20 (Morter). *See* Ex. S-21 at 5:18–6:2.

[586] Tr. 1956:15-1957:2 (Hanser).

[587] *See* Ex. PSC-5.

[588] *See* Ex. PSC-6

PSCo and Seattle, has not produced a witness with firsthand knowledge or such contracts,[589] or provided any analysis regarding such contracts.

806. Additionally, PSCo states that Seattle had the opportunity to negotiate a different price, and that it was not forced to enter into a transaction.[590] PSCo avers that Mr. Hanser attempts to shift the burden of proof in this proceeding when claiming that "[n]one of the Respondents have submitted any evidence identifying a single bilateral contract where the seller would have charged a lower price if Seattle had bargained harder."[591] PSCo states that as a Respondent, it is not required to submit any such evidence. PSCo contends that Seattle's case is merely an assertion that it paid high prices for spot market energy.

807. Next, PSCo asserts that its sales to Seattle were part of a prudent resource planning strategy that ensured PSCo possessed adequate generation and resources necessary to serve its native load. PSCo cites its 1999 Integrated Resource Plan as an example of the manner in which PSCo and its regulators approached an imminent resource need.[592] Specifically, PSCo made short and medium term purchases from independent power producers and added peaking capacity on its system. PSCo notes that this peaking capacity ultimately provided PSCo with excess energy that it could sell to Seattle and others.

808. PSCo states that in making sales, it took on a number of risks, which it was willing to do in light of actual market prices.[593] For example, PSCo took an aggressive approach in forecasting the amount of surplus energy that it would have available for sale, and operated its system accordingly, including running units close to their operating limits. PSCo notes that if its load forecasts were not accurate, which did in fact happen, PSCo was required to make its own spot market purchases at market prices to serve its load.

809. PSCo asserts that the market was sufficiently competitive to enable purchasers to be selective about the energy product that they were purchasing. Thus, buyers, including Seattle, dictated certain key terms of transactions to PSCo, such as firmness and point of

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[589] *See* Tr. 1896:2-17 (Hanser).

[590] *See* Order on Remand at P 18.

[591] *See* Ex. SCL-76 at 38:4-6.

[592] *See* Ex. PSC-1.

[593] *Id.* at 20:19-24:18.

delivery.[594] PSCo notes that because buyers sought financially firm energy, when PSCo made sales, there was a risk of damages if PSCo was unable to deliver energy for any reason, including loss of transmission.[595]

810. Next, PSCo argues that Seattle's own evidence supports PSCo's assertion that its sales were the result of legitimate business behavior. PSCo notes that Mr. Hanser testified that Respondents purchased wholesale power "[a]t prices that were at or near the prices Seattle purchased wholesale power."[596] PSCo asserts that this demonstrates that PSCo's prices to Seattle were driven by its attempt to recoup the purchase price of energy that was resold. PSCo also states that its sales were at the prevailing market price. PSCo further avers that Mr. Morter acknowledged that Seattle also sold energy at prevailing prices.[597]

811. Lastly, PSCo argues that Seattle failed to submit evidence to support its position that the prices it paid to PSCo imposed an excessive burden on consumers or seriously harmed the public interest. PSCo notes that Seattle's own evidence demonstrates that legitimate market factors, rather than any actions on the part of PSCo, prompted the increase in energy prices during the Section 206 Period.[598]

### (b) Claims Pursuant to Section 309 of the FPA

812. PSCo states that Seattle does not make any specific allegation with respect to any particular sale by PSCo to Seattle during the Section 309 Period, nor has Seattle pointed to any specific violation of the Federal Power Act or PSCo's market-based rate tariff.[599] PSCo contends that Seattle has only made general allegations of unlawful market activity by Respondents and claims that PSCo's prices were too high. PSCo asserts that Seattle wrongly alleges that because the prices were too high, PSCo must have been a pivotal supplier, and therefore, PSCo market-based rate authority must be retroactively revoked.

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[594] *Id.* at 21:9-18.

[595] *Id.* at 22:5-16.

[596] *See* Ex. SCL-76 at 38:13-16.

[597] *See* Tr. 3181:22-3182:16 (Morter).

[598] *See* Ex. SCL-38 at 2; Ex. SCL-39 at 2. *See also* Ex. S-21 at 6:3-8.

[599] Order on Rehearing at P 32.

813. PSCo also contends that the there are numerous deficiencies in Mr. Hanser's benchmark analysis, including (1) the MMCP benchmark is for an entirely different market; (2) the benchmarks ignore transmission costs that PSCo incurred to deliver energy to Seattle at a geographically remote location; (3) the benchmarks did not provide PSCo with any sort of "credit" for recovery of fixed costs incurred with building and operating generating units that produced energy sold to the City of Seattle; and (4) the benchmarks failed to consider any liquidated damages that PSCo paid in connection with its sales of financially firm energy.[600]

814. Lastly, PSCo argues that Seattle ignores the fact that Seattle engaged in the exact same conduct. PSCo asserts that the record demonstrates that Seattle also purchased energy in the spot market and sold that energy at prevailing market prices.[601] Thus, PSCo concludes that the Seattle's request for refunds under section 309 should be denied.[602]

### 6. El Paso Power Marketing Company, LLC Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

815. El Paso contends that Seattle failed to allege facts demonstrating that El Paso engaged in unlawful activity that directly affected contract negotiations and resulted in unjust and unreasonable rates.[603] El Paso avers that although Seattle initially made allegations of specific unlawful activity against other market participants,[604] its direct case does not even mention El Paso.[605] Furthermore, El Paso states that Mr. Hanser was not aware of the prices that El Paso charged Seattle for power in the Pacific Northwest spot market during the Section 206 Period.[606] El Paso argues that Seattle's claims

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[600] *See* Tr. 3139:14-3141:11 (Imbler).

[601] *See* Tr. 2180:9-20 (Hanser).

[602] *See Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67, 73, 76 (D.C. Cir. 1992).

[603] Order on Remand at P 21.

[604] *See* Ex. SCL-1 at 11:23-19:34.

[605] *See* Ex. SCL-1 through SCL-3, Ex. SCL-10, Ex. SCL-11, Ex. SCL-15, Ex. SCL-19, Ex. SCL-29, Ex. SCL-37 through SCL-41; Tr. 1956:21-1957:2 (Hanser); Ex. EP-1 at 13:6-9.

[606] *See* Ex. S-22 at 13; Tr. 1901:2-9 (Hanser).

regarding dysfunction in the California or Pacific Northwest markets and allegations of unlawful market activity by other market participants are insufficient as a basis for refund liability in this proceeding.[607]

816. El Paso also argues that Seattle has failed to demonstrate a causal connection between unlawful activity by El Paso and unjust and unreasonable rates under a specific bilateral contract.[608] El Paso states that Seattle failed to even identify the specific contracts with El Paso,[609] and submitted only hourly delivery information.[610] Thus, El Paso asserts that there is no way to analyze the nexus between a contract and alleged unlawful activity. El Paso further states that almost all the deliveries listed by Seattle were made pursuant to bilateral monthly forward contracts and should be excluded from the scope of this proceeding.[611]

817. Next, El Paso argues that it engaged in lawful market activity with a legitimate business reason.[612] El Paso notes that it did not engage in any market behavior prohibited under the terms of its power marketing authority, nor did it violate any of the conditions imposed by the Commission during this period.[613] El Paso states that it did not have a significant share of the market, abided by the terms of its power marketing authority, and had no means or ability to manipulate prices in the Pacific Northwest, and it did not do so.[614]

818. El Paso states that all its transactions in the Pacific Northwest were pure power marketing transaction.[615] El Paso's trading personnel canvassed the market for offers

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[607] *See* Order on Remand at P 21; Order on Rehearing at PP 26, 30.

[608] Order on Remand at PP 2, 18, 23.

[609] *See* Ex. SCL-1 through SCL-3; Ex. SCL-10; Ex. SCL-11; Ex. SCL-15; Ex. SCL-19; Ex. SCL-29; Ex. SCL-37 through Ex. SCL-41.

[610] *See* Tr. 3272:8-3274:23 (Morter); Ex. EP-2 at 10:21-11:3.

[611] *See* Ex. SCL-88; Ex. EP-1 at 7:11-14:8; Ex. EP-2 at 11:4-13; Ex. EP-SCL-1.

[612] *See* Ex. EP-1 at 10:1-14:8.

[613] *Id.* at 6:4-10.

[614] *Id.*

[615] *Id.* at 4:17-5:14.

from potential sellers of energy in order to assemble a portfolio of supplies to sell and simultaneously, explored the opportunities to sell the power to be purchased.[616] El Paso states that it executed economic transactions with a variety of parties.[617] El Paso asserts that given the numerous competitive sellers operating in the Pacific Northwest market at the time, El Paso was not able to set the market price when it transacted in the Pacific Northwest and was a price taker.[618]

819. Lastly, El Paso asserts that Seattle failed to demonstrate that any contract rate imposes an excessive burden on consumers or seriously harms the public interest. El Paso notes that Seattle did not even attempt to analyze the prices that El Paso charged Seattle during the Section 206 Period[619] and did not show the rates that consumers "could have obtained (but for the contracts) after elimination of the dysfunctional market."[620] Additionally, as discussed above, El Paso states that Seattle presented no evidence regarding specific contracts.

820. El Paso states that Seattle had competitive alternatives to its purchases from El Paso throughout 2000 and 2001.[621] El Paso notes that there were numerous sellers operating in the Pacific Northwest market and trading activity in the Pacific Northwest was vibrant and robust.[622] El Paso asserts that Seattle purchased and sold power to over sixty different entities during the Section 206 Period,[623] and there were over one hundred signatories to the WSPP Agreement.[624]

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[616] *Id.* at 10:3-19.

[617] *Id.*

[618] *Id.* at 10:20-12:7.

[619] *See* Tr. 1901:2-25, 1961:3-7 (Hanser).

[620] *See* Order on Rehearing at P 27 n.53.

[621] *See* Ex. EP-1 at 10:20-11:11; Ex. EP-2 at 9:3-17.

[622] *See* Ex. EP-1 at 10:20-11:2; Ex. EP-2 at 9:3-11.

[623] *See* Ex. EP-1 at 11:3-11.

[624] *See* Tr. 3114:25- 3115:21 (Price).

821. Like other Respondents, El Paso notes that Seattle engaged in similar transactions at similar prices, and Seattle should not be able to claim that the contract rates that it paid imposed an excessive burden on consumers while simultaneously denying that the contract rates that it charged during the same period somehow did not impose such an excessive burden or seriously harm the public interest.[625]

### (b) Claims Pursuant to Section 309 of the FPA

822. El Paso argues that Seattle has failed to meet its burden under FPA section 309.[626] El Paso states that Seattle acknowledged that Mr. Hanser did not attempt to show that a seller had committed an unlawful act that directly affected the price that Seattle paid for power.[627] Additionally, Mr. Hanser and Mr. Morter admitted that they do not make any allegations regarding unlawful activity or other misconduct by El Paso during the Section 309 Period.[628] El Paso notes that Mr. Hanser did not review any of the contracts between El Paso and Seattle (other than the prices and hourly deliveries) and did not investigate any of the contract negotiations.[629] Additionally, El Paso notes that like during the Section 206 Period, it engaged in lawful market activity with a legitimate business reason during the Section 309 Period.[630]

823. El Paso states that Seattle's only allegation regarding El Paso with respect to Seattle's section 309 claims appears to involve the price that El Paso charged Seattle.[631] El Paso argues Seattle failed to provide any evidence that the prices it paid were anticompetitive or the result of an exercise of market power. El Paso notes that Seattle's

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[625] *Id.* at 13:21-25.

[626] *See* Ex. EP-2 at 12:8-17; Ex. S-23 at 6:16-23.

[627] Tr. 350:23-351:1 (Mr. Hanser "didn't put any testimony in on showing [unlawful activity]").

[628] Tr. 2144:24-2145:5 (Hanser); Tr. 3278:7-16 (Morter).

[629] *See* Tr. 1964:14-1965:9 (Hanser); Ex. JDG-1 at 16:4-5. El Paso notes that the data submitted by Seattle includes only hourly delivery data and do not identify specific contracts. *See* Tr. 3272:8-18 (Morter); Ex. EP-2 at 10:21-24.

[630] *See* Ex. EP-2.

[631] El Paso repeats arguments made by other Respondents concerning Mr. Hanser's benchmark analyses.

witnesses acknowledged that the purchases Seattle made from Respondents were generally at prevailing market prices.[632]

824. El Paso also contends that Seattle made wholesale power sales to multiple counterparties at prices similar to—and sometimes above—the prices at which it purchased wholesale power in the Pacific Northwest.[633] For example, during January 2000, Seattle charged El Paso a higher price than the price that El Paso charged to Seattle.[634]

825. Next, El Paso states that Seattle's analysis shows that El Paso charged prices that were actually less than Mr. Hanser's marginal cost-based benchmarks. El Paso notes that for every month during the Section 309 Period, El Paso charged Seattle an average price that was lower than Mr. Hanser's Pivotal Unit Benchmark.[635] Furthermore, El Paso states that after adjusting Mr. Hanser's analysis to account for actual gas market prices and hourly prices both above and below the benchmarks,[636] the premiums based on the Pivotal Unit Benchmark become negative for the entire Section 309 Period.[637]

826. Lastly, El Paso states that almost all the deliveries listed by Seattle were made pursuant to bilateral monthly forward contracts and should be excluded from the scope of this proceeding.[638] El Paso also notes that the transaction data include deliveries related to contracts that were negotiated and executed prior to January 1, 2000.[639]

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[632] Ex. SCL-117 at 17:8-10; Tr. 3278:21-3279:5 (Morter).

[633] *See* Ex. EP-2 at 9:18-25; Ex. JDG-1 at 19:7-20:7; Ex. JDG-6.

[634] *See* Ex. EP-2 at 10:1-6. *See also* Ex. SCL-106 at 206-07.

[635] Ex. SCL-110 at 42. For the entire period, El Paso charged Seattle an average of $110.54 less than Mr. Hanser's Pivotal Unit Benchmark price. Tr. 2146:13-22 (Hanser).

[636] *See* Ex. JDG-7 at 3:7-17; Ex. JDG-8 through JDG-10.

[637] *See* Ex. JDG-11. El Paso charged Seattle a total of $231,780 less than Mr. Hanser's Pivotal Unit Benchmark price for "day-ahead" and "hour-ahead" transactions, and $3,411,353 less than Mr. Hanser's Pivotal Unit Benchmark price for "other" transactions. *Id.*

[638] *See* Ex. EP-2 at 11:4-13. *See also* Ex. EP-SCL-1.

[639] *See* Tr. 3274:2-10 (Morter).

### (c) Seattle's Claims Barred by Prior Settlement

827. El Paso argues that Seattle's refund claims against El Paso are barred by El Paso's settlement with the Attorney General of the State of Washington (Washington Attorney General) and Seattle's express acceptance of the related benefits of the settlement.

828. On June 24, 2003, El Paso Corporation, El Paso Natural Gas Company, and El Paso Merchant Energy, L.P. entered into a settlement with a number of entities, including the Washington Attorney General, which released El Paso from claims related to this proceeding.[640] On August 8, 2003, the settling parties, including Washington Attorney General, filed a joint motion for partial dismissal of El Paso from the specified proceedings, including this proceeding.[641] El Paso states that on January 6, 2004, the Commission issued an order partially dismissing El Paso from these proceedings.[642] In addition, the Commission vacated the Chief Judge's October 9, 2001 and September 23, 2002 Initial Decisions in Docket No. RP00-241.[643]

829. El Paso states that in 2004 and 2005, the City of Seattle enacted a series of ordinances authorizing Seattle City Light to accept millions of dollars from the Washington Attorney General's settlement with El Paso.[644] According to the ordinances, "the Washington State Attorney General negotiated a restitution settlement with El Paso Energy with the intention to remedy harm suffered by consumers from the energy rate increases that resulted from the West Coast energy crisis of 2000-2001."[645] As a result of

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[640] *See* Master Settlement Agreement, Docket No. RP00-241-000, et al., at § 6.7 (filed June 27, 2003) (Master Settlement Agreement).

[641] *See* California Parties and Indicated Attorneys General, Joint Motion for Partial Dismissal of El Paso from Specific Proceedings, Docket Nos. EL00-95-089, EL00-98-075, EL01-10-013, *et al.* (filed Aug. 8, 2003).

[642] *See San Diego Gas & Elec. Co. v. Sellers of Energy & Ancillary Servs.*, 106 FERC ¶ 61,005 (2004) ("[t]he movants' motion to dismiss the complaints against El Paso … with prejudice as to California Parties and Indicated AGs is hereby granted").

[643] *See Pub. Util. Comm'n of Cal. v. El Paso Natural Gas Co.*, 105 FERC ¶ 61,201, at P 60 (2003), *rehearing denied*, 106 FERC ¶ 61,315, at P 51 (2004).

[644] City of Seattle, Washington, Ordinance No. 121926 (Sept. 23, 2005); *see also* City of Seattle, Washington, Ordinance No. 121714 (Jan. 25, 2005); City of Seattle, Washington, Ordinance No. 121695 (Dec. 20, 2004).

[645] *See* City of Seattle, Washington, Ordinance No. 121926 (Sept. 23, 2005).

the settlement, Seattle received millions of dollars for both its business customers and its residential customers.[646]

830. El Paso argues that Seattle's claims against El Paso in this proceeding are barred by El Paso's settlement with the Washington Attorney General and Seattle City Light's express acceptance of the related benefits of the settlement. Although Seattle was not a signatory to the Master Settlement Agreement, El Paso states that the Commission has ruled that "when a third party reaps the benefits of a contract, it cannot later disclaim the obligations that the agreement imposes on it."[647] El Paso notes that the courts have also have recognized this principle.[648]

### 7. Avista Corporation D/B/A Avista Utilities Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

831. Avista Utilities asserts that by its own admission, Seattle has made no allegations of unlawful activity against Avista Utilities. Avista Utilities avers that both Seattle witnesses admitted that they made no claims of unlawful conduct against Avista Utilities.[649] Moreover, Avista Utilities notes that Seattle's direct testimony makes no reference whatsoever to Avista Utilities.[650] Avista Utilities asserts that its testimony affirmatively demonstrates that its sales to Seattle were consistent with legitimate business behavior

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[646] City of Seattle, Washington, Ordinance No. 121926 (Sept. 23, 2005); City of Seattle, Washington, Ordinance No. 121695 (Dec. 20, 2004).

[647] *Gas Tech. Inst.*, 109 FERC ¶ 61,164, at P 45 (2004) ("GTI cannot now, having garnered the benefits of the 1998 settlement, turn its back on the obligations contained within that settlement").

[648] *See, e.g.*, *Skelton v. Gen. Motors Corp.*, 860 F.2d 250, 259 (7th Cir. 1988) (quoting *Bi-County Properties v. Wampler*, 378 N.E.2d 311 (Ill. App. Ct. 1978)) (recognizing that a "party may become bound to a contract by accepting its benefits, even though he did not sign it" and that "an acceptance of benefits under a contract, may be sufficient to constitute a ratification binding on the party accepting the benefits as if he had signed the contract").

[649] Tr. 2074:10-15, 2116:24-2117:1 (Hanser); Tr. 3278:7-20 (Morter).

[650] *See* Ex. AVI-1 at 78:14-79:3.

832. Furthermore, Avista Utilities asserts that Seattle did not even identify the specific sales contracts between Avista Utilities and Seattle that are at issue in this proceeding.[651] Avista Utilities also notes that based on Seattle's data provide no information regarding the negotiations of contracts.

833. Next, Avista Utilities argues that Seattle failed to demonstrate that its contracts with Avista Utilities imposed an excessive burden or seriously harmed the public interest. Avista Utilities notes that like Seattle, it was a load-serving entity in the Pacific Northwest. Therefore, Avista Utilities was coping with the same challenges as Seattle during the relevant period. Avista Utilities states that Mr. Hanser failed to consider this, including whether other load-serving entities had any rate increases in 2000 and 2001.[652] Thus, Avista Utilities contends that Seattle fails to explain why transferring wealth from Avista Utilities' ratepayers to Seattle's ratepayers would serve the "public interest."

### (b) Claims Pursuant to Section 309 of the FPA

834. Avista Utilities asserts that Seattle made no Respondent-specific or transaction-specific allegation of a statutory or tariff violation against Avista Utilities. Avista Utilities contends that Seattle's generic, marginal cost-based allegations are insufficient to entitle it to a remedy under section 309. Avista Utilities also notes that Seattle engaged in conduct that cannot be distinguished in any principled way,[653] and thus, should not be entitled to a remedy under section 309.[654]

835. Next, Avista Utilities contends that earlier in this proceeding, the Commission has determined that it would be unfair to award refunds to governmental entities like Seattle

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[651] Ex. AVI-1 at 38:7-14. *See* Tr. 1961:19-1962:18 (Hanser); Ex. J-AVI-2 at 2 n.3 ("[t]he use of the term 'sales' herein does not constitute a stipulation by Avista Utilities that Exhibits A and B identify specific bilateral contracts"); Ex. J-AVI-3.

[652] Tr. 2200:10-23 (Hanser).

[653] Avista Utilities states that during the Section 309 Period, it was also a load serving entity, and Avista Utilities and Seattle were regular trading partners in the market. The highest price at which Seattle sold to Avista Utilities in that period was $300/MWh. Ex. J-AVI-3. The highest price at which Avista Utilities sold to Seattle was $450/MWh. Ex. J-AVI-3. Avista Utilities sold to Seattle at a price higher than $300 in only 28 hours.

[654] *Towns of Concord, Norwood, & Wellesley v. FERC* 955 F.2d 67, 75 (D.C. Cir. 1992).

when the Commission is powerless to direct Seattle to make refunds for its own high-priced sales.[655] Avista Utilities avers that the Ninth Circuit's opinion in *Port of Seattle v. FERC* did not reverse the Commission's determination not to award refunds.[656] Instead, "[t]he Ninth Circuit remanded this proceeding to the Commission to reconsider two substantive issues: (1) whether refunds are warranted for purchases of energy made by CERS … and (2) new evidence of market manipulation …."[657]

### 8. Avista Energy, Inc. Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

836. Avista Energy asserts that by its own admission, Seattle has made no allegations of unlawful activity against Avista Energy.[658] Avista Energy asserts that its testimony affirmatively demonstrates that its sales to Seattle were consistent with legitimate business behavior.

837. Avista Energy notes that Seattle's pre-filed testimony makes only one reference to Avista Energy, stating that "[a]ccording to [California Parties Witness Dr. Peter Fox-Penner's testimony in the EL00-95 proceeding] … Avista Energy entered into a long-term parking arrangement with Chelan County Public Utility District."[659] Avista Energy avers that Seattle mischaracterizes the agreement between Avista Energy and the Chelan PUD by calling it a "parking" agreement,[660] and notes that there is no ruling that "parking," in and of itself, is unlawful.[661] Avista Energy states that the relationship between Avista Energy and the Chelan PUD was investigated by Staff in

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[655] *Puget Sound Energy, Inc*., 103 FERC ¶ 61,348, at P 39 (2003) ("[i]t would not do justice to allow these parties [government entities] to receive refunds for their high-priced purchases while they are exempt from providing refunds for any high priced sales they may have made").

[656] *Port of Seattle v. FERC*, 499 F.3d 1016, 1036 (2007).

[657] Order on Rehearing at P 3.

[658] Tr. 2074:10-15, 2116:24-2117:1 (Hanser); Tr. 3278:7-20 (Morter).

[659] Ex. SCL-1 at 17:20-23.

[660] Ex. AVE-1 at 10:17-11:12.

[661] *Id*. at 21:5-7.

Docket No. EL02-115, and there was no finding of impropriety.[662] Furthermore, Avista Energy contends that Seattle made no effort to link this "parking arrangement" with any particular spot sale from Avista Energy to Seattle. Thus, Avista Energy concludes Mr. Hanser made no allegations against Avista Energy and that Mr. Hanser's assertion borrowed from Dr. Fox-Penner's prior testimony should be given no weight.[663]

838. Avista Energy further asserts that Seattle did not even identify the specific contracts between Avista Energy and Seattle.[664] Avista Energy states that the data submitted, including the stipulated data, are not contracts and provide no information regarding the negotiations of contracts. Rather, the data simply identify aggregated deliveries by volume and hour across the relevant period.[665]

839. Avista Energy also argues that Seattle failed to demonstrate that its contracts with Avista Energy imposed an excessive burden or seriously harmed the public interest.

### (b) Claims Pursuant to Section 309 of the FPA

840. Avista Energy asserts that Seattle failed to meet its burden regarding its section 309 claims. Avista Energy states that during the Section 309 Period, Avista Energy and Seattle were regular trading partners in the market, and accordingly, both made sales to one another at relatively high prices.[666] Avista Energy notes that Seattle actually sold Avista Energy more than twice as much power in the spot market as Avista Energy sold Seattle during the Section 309 Period. Avista Energy argues that it would be inequitable

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[662] *Id*. at 11:8-12.

[663] *Id*. at 9:11-16.

[664] Ex. AVI-1 at 38:7-14; Tr. 1961:19-1962:18 (Hanser); Ex. J-AVE-2; Ex. J-AVE-3.

[665] *See* Ex. J-AVE-2 at 2 n.3 ("[t]he use of the term "sales" herein does not constitute a stipulation by Avista Utilities that Exhibits A and B identify specific bilateral contracts"); Ex. J-AVE-3 at 2 n.3.

[666] The highest price at which Seattle sold to Avista Energy in that period was $525/MWh. Ex. AVE-SCL-2. Avista Energy sold to Seattle at a higher price in only one hour: a sale at $750/MWh on December 8, 2000. Ex. AVE-SCL-2. Avista Energy's next highest prices were two hours of sales to Seattle at $500/MWh, and the rest of Avista Energy's sales were at lower prices. *Id.*

for Seattle to be entitled to a remedy under section 309 when Seattle itself engaged in conduct that cannot be distinguished in any principled way.[667]

### 9. Cargill Power Markets, LLC Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

841. Cargill argues that Seattle has failed to demonstrate that Cargill violated the WSPP Agreement or Cargill's market-based rate tariff, or otherwise engaged in unlawful market activity during the Section 206 Period.[668] Cargill contends that the prices Seattle paid were not the result of unlawful activity by Cargill, but were instead the result of legitimate market forces. Cargill further notes that Seattle has not produced any evidence with respect to any contract between Seattle and Cargill, has not produced a witness that transacted with Cargill, and has not examined the contracts between Seattle and Cargill.[669]

842. Cargill also states that Mr. Hanser testified that "Respondents' bilateral negotiations to purchase power resulted in approximately the same prices that Seattle paid for wholesale power."[670] Thus, Cargill states that to the extent that Cargill made an offer to Seattle, Cargill typically would do so at a price that was at or near the price that Cargill paid for the energy that it then sold to Seattle. Cargill notes that this was particularly important because as a marketer, Cargill owned no generation and had to sell energy at prices that were at or above the price Cargill paid for that energy. Cargill avers that it is appropriate business behavior for a power marketer to sell energy at the prevailing market price, which includes a price similar to or slightly higher than the price that Cargill paid for that energy.[671]

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[667] *Towns of Concord, Norwood, & Wellesley v. FERC* 955 F.2d 67, 75 (D.C. Cir. 1992).

[668] *See* Ex. S-21 at 5:18-6:2. *See also* Tr. 2074:10-15, 2116:24-2117:1, 2120:20:23 (Hanser); Tr. 3278:7-20 (Morter). Cargill also notes that Mr. Hanser fails to make any specific reference to Cargill at all in his prefiled testimony. *See* Tr. 1956:15-1957:2 (Hanser).

[669] *See* Tr. 1896:2-1896:17, 1961:3-1961:7 (Hanser).

[670] *See* Ex. SCL-76 at 38:13-16.

[671] Cargill notes that Seattle also sold energy at prevailing market prices and used its hydroelectric resources to store energy for later sales when market prices were higher.

(continued…)

843. Additionally, Cargill states that Seattle had the opportunity to negotiate a different price and that it was not forced to enter into a transaction.[672] Cargill notes that Mr. Morter testified that Seattle could have attempted to negotiate with Cargill, but refused to do so if Cargill did not accept the price that Seattle was initially willing to pay for energy.[673] Cargill asserts that the evidence demonstrates that Cargill was a price-taker and therefore, the primary cause of the price for Seattle's spot market purchases was Seattle's own conduct.

844. Next, Cargill argues that Seattle failed to demonstrate that its contracts with Avista Energy imposed an excessive burden or seriously harmed the public interest. Cargill asserts that Seattle's own evidence demonstrates that legitimate market factors, rather than any actions on the part of Cargill, prompted the increase in energy prices during the Section 206 Period.[674]

#### (b) Claims Pursuant to Section 309 of the FPA

845. Cargill contends Seattle failed to demonstrate that either: (1) Cargill violated a filed tariff or rate schedule or (2) Cargill violated a statutory requirement of the Federal Power Act.[675] Cargill contends that Seattle has only made general allegations of unlawful market activity by Respondents and claims that Cargill's prices were too high. Cargill states that Mr. Hanser does not make any specific allegation with respect to any particular sale by Cargill to Seattle during the Section 309 Period.

### 10. TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. Initial Brief

846. TransAlta contends that Seattle has failed to establish any unlawful act by TransAlta resulted in unjust and unreasonable rates. TransAlta states that the only

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*See* Tr. 3250:14-3251:8, 3181:22-3182:16 (Morter). Cargill also avers that Mr. Morter admitted that instances existed where Seattle would be purchasing energy in the very same hour that it was selling energy at prices similar to those for which it now seeks refund. *See* Tr. 3245:16-23 (Morter).

[672] Ex. CPM-1.

[673] *See* Tr. 3262:9-3267:13 (Morter).

[674] *See* Ex. SCL-38 at 2; *See* Ex. SCL-39 at 2.

[675] Order on Rehearing at P 32.

alleged violation Seattle has asserted against TransAlta was to rely on Mr. Taylor's False Export analysis. TransAlta notes that those allegations are unfounded. Moreover, TransAlta states that Mr. Taylor's analysis relates specifically to CERS's transactions, and Seattle has no basis to assert a claim.

### 11. Commission Trial Staff Initial Brief

#### (a) Claims Pursuant to Section 206 of the FPA

847. Trial Staff states that Seattle failed to establish that any Respondent engaged in unlawful market activity, or that any such unlawful market activity directly affected specific contracts to which Seattle was a party. Thus, Trial Staff asserts that the *Mobile-Sierra* presumption applies to the contracts at issue in this proceeding.

848. Trial Staff avers that Mr. Hanser does not even attempt to make specific allegations against any Respondent in this proceeding, nor does he provide any evidence relating to any specific unlawful activity by any particular seller, whether a Respondent or not.[676] Trial Staff notes that Mr. Hanser initially alleged that "sellers in Western markets" engaged in such unlawful acts as physical withholding of power, Enron-type games, anomalous bidding practices, and economic withholding of power,[677] but did not conclude that any of the Respondents engaged in these activities.[678] Trial Staff states that Mr. Hanser confirmed that he did not attempt to investigate or establish any allegation of wrongdoing on the part of any Respondent.[679] Thus, Seattle did not make any allegation or any showing that a Respondent's illegal activities caused dysfunctional market conditions under which the contracts were formed.

849. Next, Trial Staff states that Mr. Hanser only maintained that the California market had unjust and unreasonable prices created by "sellers'" unlawful activities that were reflected in Seattle's wholesale contracts in the Pacific Northwest. Trial Staff contends that Mr. Hanser wrongly asserts that the Commission has found that prices in the Pacific Northwest market reflected the dysfunctional and unlawful activities in California. Trial Staff avers that the Commission has not made such a finding, and has only stated that the two markets were interconnected, interrelated, and integrated, sharing certain common

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[676] Ex. S-21 at 5-6.

[677] Ex. SCL-1 at 11:23-19:13.

[678] Ex. S-21 at 9-14.

[679] Tr. 2118:10- 2121:5 (Hanser).

factors that can affect the price in each market.[680] Trial Staff states that the Commission also found, however, that the California and Pacific Northwest markets were different in important ways.[681] Trial Staff argues that the noted commonalities do not establish the requisite causality to show that any specific unlawful activity anywhere directly affected the contracts at issue in this proceeding.

850. Trial Staff also states the Mr. Hanser conducted a cointegration analysis to establish a link between the California and Pacific Northwest markets. However, Trial Staff notes that Mr. Hanser admitted that his cointegration analysis was not intended to, and cannot, establish causation.[682] Moreover, Trial Staff states that Mr. Hanser acknowledged that the analysis does not say "why there might be a relationship between prices in one market and another."[683] Trial Staff avers that the appearance of similar movement in prices between the two markets could reflect nothing more than similar scarcity problems. Trial Staff notes that it is uncontested that drought conditions in the Pacific Northwest caused water shortages rarely seen before,[684] and the record is clear that "between 1996 and 1999, California added about 700 MW of generation while its peak load grew by some 5,500 MW."[685]

851. Trial Staff asserts that Mr. Hanser did not attempt to distinguish between the many economic, physical, and psychological forces at work that likely caused prices to be volatile in the Pacific Northwest and in California. Thus, Trial Staff contends that the cointegration analysis lacks relevance and does not establish anything meaningful that

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[680] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,357-58 (2000); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,115, at 61,356 (2001).

[681] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418, at 62,545 (2001) ("the West is a single market which is at once inextricably interrelated, yet characterized by important differences").

[682] Ex. SCL-76 at 25:3-6; Tr. 2178:21-2179:13 (Hanser).

[683] Tr. 2179:14-17 (Hanser).

[684] Ex. SCL-110 at 75:23-76:3 ("[i]n 2000, and the first nine months of 2001, SCL was required to purchase large amounts of power in the wholesale market as a result of unusually poor water conditions in the water year beginning October1, 2000").

[685] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,294, at 61,992 (2000).

can help resolve this proceeding, which must be resolved by focusing on specific seller violations.

852. Trial Staff further argues that even if it was shown that specific unlawful activities by sellers in California directly caused Seattle's specific contracts with Respondents to be unjust and unreasonable, it still would fail to meet the requirements necessary overcome the *Mobile-Sierra* presumption. Trial Staff notes that the Order on Rehearing made clear that evidence of unlawful activity by a non-contracting party was insufficient.[686] Moreover, Trial Staff asserts that even if Mr. Hanser had established specific unlawful activity on the part of the Respondents, he did not show a causal link to the specific contract rates at issue.[687]

853. Next, Trial Staff contends that the transaction data provided by Seattle are incomplete and unreliable because they lack information necessary for identifying specific transactions, include "book-out" transactions that Seattle has admitted caused no harm, and utilize an expansive definition of "spot sale."

854. First, Trial Staff states that the information provided by Seattle only includes a listing of hourly deliveries made to Seattle and "fail[s] to include other relevant information that would be necessary to completely understand the nature of the transactions."[688] Trial Staff notes that the spreadsheets "do not identify either the actual bilateral contract or the verbal agreement under which the specific deliveries were made," and therefore, do not include the date the contract was entered into, the term of the contract, and other important terms and conditions.[689] Trial Staff asserts that such information is need to understand whether the transaction was for an hour ahead, day ahead, within month, balance of month, monthly, quarterly, or annual term.[690] Trial Staff notes that Mr. Morter acknowledged the limited focus of this data[691] and admitted that he

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[686] Order on Rehearing at P 26.

[687] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 554-55 (2008).

[688] Ex. S-23 at 9:12-15.

[689] *Id.* at 9:16-17.

[690] *Id.* at 9:21-23.

[691] Tr. 3214:5-14 (Morter).

has no first-hand knowledge of the transactions.[692] Mr. Morter also acknowledged that he had no experience with the California organized markets or the Pacific Northwest bilateral market prior to January 2012.[693] Trial Staff contends that the lack of information about specific contracts and specific contract negotiations is contrary to the Commission's directive in its Order on Remand, and therefore, Seattle has failed to even identify specific contracts or contract negotiations that may have been affected.

855. Second, Trial Staff argues that Seattle inappropriately included "book-out" transactions. Trial Staff states that "book-outs" occur when two or more entities enter into a series of transactions with offsetting delivery and payment obligations, such that the energy actually delivered and the payments actually made can be netted out. Trial Staff asserts that it is unclear how an identical rate offered by two different entities would be unlawful for one entity and not the other when, such as here, the rates are market-based.[694] Moreover, Trial Staff states that Mr. Morter acknowledged that there would be no harm associated with these transactions.[695] Thus, Trial Staff concludes that there is no justification for the inclusion of book-outs.

856. Third, Trial Staff contends that Mr. Morter's expansive definition of "spot sale" relies in part on an incomplete understanding of Trial Staff's position in an earlier, distinct phase of this litigation. Trial Staff notes that it previously stated that "Staff believes that the most appropriate limitation for spot market sales in the [Pacific Northwest] is one month,"[696] but also went on to say that "parties should be permitted to show specifically, for transactions longer than one month but not more than one year, that particular contracts were not part of long term planning and thus should be considered spot transactions."[697] Trial Staff asserts that Seattle has made no attempt to make a specific showing regarding its long-term planning.[698] Lastly, Trial Staff states that it

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[692] Tr. 3153:1-3154:8 (Morter).

[693] Tr. 3157:18-3158:1 (Morter).

[694] Ex. S-23 at 10.

[695] Tr. 3243:10-11(Morter).

[696] Ex. SCL-82 at 42.

[697] *Id.*

[698] Tr. 3175:2-3 (Morter).

currently does not take a position on the definition of "spot sale" because Seattle has not supported its claim to be entitled to refunds.

857. Lastly, Trial Staff argues that Seattle failed to show that the contracts between Respondents and Seattle impose an excessive burden or seriously harm the public interest. Trial Staff asserts that Seattle failed to account for other factors or entities which could have caused the alleged public harm.[699] Thus, Trial Staff concludes that Seattle did not show that any harm was caused by the Respondents.[700] Moreover, Trial Staff asserts that Seattle did not demonstrate a particular contract caused the harm, as required by the Commission.[701] Lastly, Trial Staff argues that Seattle fails to recognize the Commission's rejection of the California Parties' argument that the Commission should permit evidence that the rates, as a whole, imposed an undue burden on the public."[702]

### (b) Claims Pursuant to Section 309 of the FPA

858. Trial Staff states that "refund claimants may attain the relief under FPA section 309 (if at all) by demonstrating a seller's specific violation of a substantive provision of the FPA or tariff, compliance with which the Commission can enforce by taking actions 'necessary and appropriate.'"[703] Trial Staff asserts that the *Mobile-Sierra* requirements established by the Commission for the section 206 contracts apply with equal force for the section 309 claims. Trial Staff further states that to overcome the *Mobile-Sierra* presumption, "evidence that *specific contract rates* imposed an excessive burden on consumers" may be considered,[704] but reliance on high prices alone has "been previously rejected by the Supreme Court as a basis for overcoming *Mobile-Sierra*."[705] Thus, Trial Staff concludes that the focus of the inquiry to determine "whether a buyer can avoid

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[699] Ex. S-21 at 18:15-19:14.

[700] Ex. S-23 at 16:3-17:8.

[701] Order Granting Interlocutory Appeal at P 1.

[702] Order on Rehearing at P 28.

[703] *Id.* P 32.

[704] *Id.* P 27 (emphasis added).

[705] *Id.* P 30.

application of the *Mobile-Sierra* public interest presumption, is individual contracts and the conduct of the seller as it relates to the formation of each contract."[706]

859. Trial Staff argues that Mr. Hanser failed to demonstrate any specific seller's violation of any substantive provision of the FPA or a tariff, as required by the April 5 Order on Rehearing. Trial Staff asserts that Mr. Hanser also failed to tie specific violations to particular transactions or Respondents.[707]

860. Trial Staff states that Mr. Hanser only alleges that: (1) prices paid by Seattle were driven by the same fundamentals as the prices in California; (2) a causal relationship existed between the market dysfunction and unlawful behavior present in California and the prices observed in the Pacific Northwest; (3) the prices paid by Seattle reflected the unlawful behavior present in the California markets as demonstrated by Mr. Hanser's benchmark analysis; and (4) those price were outside of any zone of reasonableness."[708]

861. With respect to Mr. Hanser's claim that the Pacific Northwest and California markets were driven by the same fundamentals, Trial Staff contends that Mr. Hanser fails to distinguish between various "fundamentals" that may have driven each market and does not establish that the fundamentals were the same for both markets. Trial Staff further argues that Mr. Hanser does not demonstrate a causal link existed between the two markets, or that any unlawful behavior was committed in the Pacific Northwest by the Respondents or anyone else. Moreover, Trial Staff asserts that Mr. Hanser's benchmarks are inappropriate, do not establish unlawful behavior, and are unrelated to any "zone of reasonableness" adopted by the Commission or the courts.

862. First, Trail Staff states that Mr. Hanser's analysis does not separate out any of the individual forces at work that likely caused prices to be volatile in the Pacific Northwest from those fundamentals affecting the prices in California. Trial Staff notes that market fundamentals, such as the unprecedented drought in the Pacific Northwest,[709] the massive financial dysfunction in California, transmission difficulties, and other factors likely caused prices in the Pacific Northwest and in California to reflect scarcity, risk, and opportunity costs. Trial Staff argues that Mr. Hanser only points to observed similarities in the movement of prices between these markets, but makes no attempt to identify which

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[706] *Id.* P 26.

[707] Tr. 2071:8-17 (Hanser).

[708] Ex. SCL-110 at 75:2-12; Ex. SCL-115 at 11:20-21.

[709] Ex. SCL-115 at 42:5-7; Tr. 2209:6-22 (Hanser).

fundamental forces had which effects in these geographically and economically different markets.[710]

863. Second, Trial Staff states that the Commission has not found that a causal relationship existed between market dysfunction and alleged unlawful behavior in California and the prices in the Pacific Northwest markets. Additionally, Trial Staff avers that Mr. Hanser admitted that his cointegration analysis did not establish any causal link between the two markets.[711] Trial Staff asserts that if the prices in California and the Pacific Northwest were directly and causally linked, the two benchmarks used by Mr. Hanser – one from California and one from the Pacific Northwest – should be, if not the same, much closer than they are.[712]

864. Furthermore, Trial Staff states that general allegations of market dysfunction do not satisfy the Commission's directive to demonstrate a seller's "specific violation of a substantive provision of the FPA or a tariff."[713] Trial Staff also notes that the Commission was clear in rejecting evidence of unlawful activity by a non-contracting party."[714]

865. Third, Trial Staff states that Mr. Hanser's claim that Respondents' prices violated section 205 of the FPA because they were too high is based on his view that the prices were outside of a "zone of reasonableness determined by the seller's marginal cost of producing power."[715] Trial Staff states that Mr. Hanser compares the Respondents' prices to two marginal cost benchmarks – the MMCP and the Pivotal Unit Benchmark.

866. Trial Staff asserts that Mr. Hanser did not attempt to examine or establish any particular seller's marginal cost, so he could not assert or show any specific violation by a particular Respondent.[716] Because Mr. Hanser did not examine a particular seller's costs,

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[710] Tr. 4137:6-20 (Hogan).

[711] Tr. 2178:21-2179:16 (Hanser).

[712] Ex. SCL-110 at 37:7-10, Table III-2.

[713] Order on Rehearing at P 32.

[714] *Id.* P 26.

[715] Ex. SCL-110 at 34:22-24, 44:19-23.

[716] Tr. 2241:9-12 (Hanser).

Trial Staff contends that Mr. Hanser's argument is the same argument rejected by the Commission concerning general market dysfunction and uniformly high prices.[717]

867. Additionally, Trial Staff avers that Mr. Hanser's use of the MMCP to address prices in the Pacific Northwest is inappropriate. Trial Staff notes that the MMCP was designed for the California energy markets and the dysfunction in those organized markets. Trial Staff states that the MMCP was not developed to establish or respond to any specific alleged violations or unlawful behavior.[718] The Commission made clear that the primary focus was on market design flaws and other negative events.[719]

868. Furthermore, Trial Staff asserts that for both the MMCP and Pivotal Unit Benchmark, Mr. Hanser failed to include the recovery of fixed costs, a reasonable profit, opportunity costs, or transmission costs.[720] Thus, some sellers inevitably sold energy above Mr. Hanser's benchmarks in every hour. Trial Staff argues that this demonstrates that Mr. Hanser's benchmarks are not a reasonable or a workable methodology to gauge the lawfulness of a market-based price. Moreover, Trial Staff avers that Mr. Hanser's test is particularly poor policy in a time when supply is short. Trial Staff states that sellers would be required to sell below their marginal costs, and potentially at a loss, or not sell at all in hours when energy is really needed.[721]

869. Lastly, Trial Staff states that there are no Commission or court orders establishing a specific "zone of reasonableness" based on the seller's marginal cost that may be used

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[717] Order on Rehearing at P 30.

[718] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,294, at 61,998 (2000) (stating that the Commission did not make "findings about whether particular rates charged by specific sellers during the summer of 2000 were unjust or unreasonable or that any individual sellers exercised or abused market power").

[719] *Id*. ("a variety of factors have converged to drastically skew wholesale prices under certain conditions: significant over-reliance on spot markets which by their very nature can produce dramatic price increases when supply is tight; significant increases in load combined with lack of new facilities as well as reduced availability of supply from out of state; chronic underscheduling; and lack of demand responsiveness to price").

[720] Tr. 2091:9-2092:5, 2125:18-20, 2031:13-15 (Hanser). Trial Staff asserts that there is no evidence that the ten percent adder for risk premiums in the MMCP is appropriate to account for these factors.

[721] Tr. 2242:3-9 (Hanser).

to adjudicate any specific rate in this proceeding. Trial Staff asserts that although courts have relied on the concept of a zone of reasonableness as a basic principle in ratemaking,[722] the zone of reasonableness is not calculated by reference to marginal costs. Trial Staff notes that the Supreme Court has explicitly stated that "the general principle that rates cannot exceed marginal cost contradicts *Mobile-Sierra*."[723] Rather, courts ask:

> whether [the price] is high enough to both maintain the producer's credit and attract capital. To do this, it must … yield to equity owners a return 'commensurate with returns on investments in other enterprises having corresponding risks,' as well as cover the cost of debt and other expenses …[724]

870. Trial Staff further states that the Commission recognized in Order No. 697-A that its zone of reasonableness "may take into account all relevant public interests," which may "appropriately include non-cost factors, such as the need to stimulate additional investment."[725] Thus, Trial Staff asserts that the Commission's zone of reasonableness does not preclude recovery of fixed costs, costs reflecting risk, or transmission costs, nor does it make it an unlawful act to realize a reasonable profit, including opportunity costs. Finally, Trial Staff states that the when a seller has been determined to lack market

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[722] *Farmers Union Cent. Exch., Inc. v. FERC*, 734 F.2d 1486, 1502 (D.C. Cir. 1984) ("an agency may issue, and courts are without authority to invalidate, rate orders that fall within a 'zone of reasonableness,' where rates are neither less than 'compensatory' nor 'excessive'").

[723] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 551 (2008). The Court also stated that "the standard for reforming a particular contract validly entered into under a market-based scheme is [not] whether the rates approximate marginal cost." *Id*.

[724] *Farmers Union*, 734 F.2d at 1502.

[725] *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, at P 407, *clarified*, 124 FERC ¶ 61,055, *order on reh'g*, Order 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), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012).

power, the Commission has determined that whatever price is agreed to between that seller and a willing buyer will be within the zone of reasonableness.[726]

871. Lastly, Trial Staff notes that Seattle's transaction data for the Section 309 Period suffers from the same flaws as the data submitted for its section 206 claims.

### 12. City of Seattle, Washington Reply Brief

872. Seattle contends that it met its burden and demonstrated that each Respondent charged market-based prices in violation of Section 205 of the FPA, and therefore, is liable for refunds under section 309 of the FPA. In its reply brief, Seattle repeats a summary of the testimony and exhibits that it submitted in this proceeding and argues that this evidence is sufficient to meet its burden.

873. With respect to Respondents' claim that their market-based tariffs did not contain price caps that restricted them from charging Seattle prices that exceeded the MMCP or any other benchmark, Seattle argues that market-based prices are limited by "just and reasonable" requirements and must fall within a "zone of reasonableness." Seattle also avers that Respondents provided no evidence demonstrating that the MMCP is not an appropriate upper limit on the "zone of reasonableness."

874. Next, Seattle addresses Respondents' claim that the MMCP is not a proper benchmark for the Pacific Northwest bilateral market. Seattle contends that the differences between the Pacific Northwest and California markets do not prove, one way or another, that the MMCP should not be used. Seattle asserts that Respondents provided no evidence of how differences between the markets would affect prices in a functional market free of manipulation. Seattle notes that in the California Refund Case, the Commission used the MMCP to mitigate bilateral OOM transactions in the Pacific Northwest.[727] Additionally, when setting the West-Wide price cap in June 2001, the

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[726] Order No. 697-A at P 409 ("[w]hen the Commission determines that a seller lacks or has mitigated market power, it is making a determination that the resulting rates will be established through competitive forces, not the exercise of market power, and thus will fall within a zone of reasonableness").

[727] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515-16 (2001); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,178 (2001). *See also* California Parties, Motion Requesting Consolidation and Severance of Specified Proceedings, Docket Nos. EL00-95-000, EL00-98-000, EL01-10-000, *et al.*, at 55 (filed May 22, 2009); *Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1053 (9th Cir. 2006) ("[t]he OOM transactions

(continued…)

Commission determined that the structural differences between the Pacific Northwest and California markets did not constitute a barrier to using the same mitigation formula for both markets.

875. Next, Seattle contends that Respondents wrongly claim that their prices were consistent with the market fundamentals in a tight supply situation. Seattle argues that this evidence is irrelevant to whether Respondents charged prices that violated section 205 of the FPA. Seattle notes that Respondents did not use its market fundamentals evidence to prove a "zone of reasonableness" that can be used to determine whether their market-based rates are "just and reasonable." Seattle also states that the in California Refund Case, the Commission acknowledged that market fundamentals were among a long list of factors that created the Western Energy Crisis and still concluded that the MMCP should be used to remedy OOM purchases in the Pacific Northwest.[728] Seattle further notes that the Commission has never relied on market forces alone to ensure market-based rates fall within a "zone of reasonableness."[729]

876. Next, Seattle argues that there is no merit to Respondents' claim that Seattle's "marginal cost" theory was rejected in *Morgan Stanley*. Seattle asserts that the Court expressly stated that whether market-based rates were unlawful under the FPA was not before the Court.[730] Seattle further contends that its theory is not even based on marginal costs, but is based on (1) the fact that the Commission has already determined that the MMCP represents the highest lawful price that sellers can charge for wholesale energy in the California markets and (2) the relationship between prices in the Pacific Northwest and California markets. Moreover, Seattle notes that the Commission's use of the MMCP was upheld by the Ninth Circuit.[731]

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at issue here were bilaterally negotiated sales of power at different prices than the market clearing price established in the auction market").

[728] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,211-16 (2001).

[729] *California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1011 (9th Cir. 2004); *Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011).

[730] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 538 (2008) ("[w]e have not hitherto approved, and express no opinion today, on the lawfulness of the market-based-tariff system, which is not one of the issues before us").

[731] *See Pub. Utils. Comm'n of Cal.*, 462 F.3d at 1052-53.

877. With respect to Respondents claim that the MMCP is too low because Pacific Northwest prices were higher than California prices, Seattle asserts that the Commission has already held that the MMCP is the upper limit for the "zone of reasonableness" for market-based prices for the wholesale energy markets in California, and that Mr. Hanser demonstrated that it was appropriate to use the MMCP for the Pacific Northwest. Seattle further notes that the MMCP is conservative in favor of Respondents. Seattle contends that Respondents did not provide evidence to rebut these conclusions.

878. Next, Seattle argues that Respondents did not provide evidence that their conduct was "legitimate business behavior." Seattle contends that charging unjust and unreasonable prices cannot be justified as legitimate. Seattle further asserts that the need to make a profit also cannot justify prices that are not just and reasonable.

879. Seattle also responds to asserts that claims under section 309 are limited to the period from January 1, 2000 to December 24, 2000. Seattle states that the Commission's Order on Rehearing allows Seattle to submit claims for refunds under section 309 for the period of January 1, 2000 through June 20, 2001.[732]

880. With respect to the Respondents' argument that "bookout" transactions should be excluded, Seattle states that sales of wholesale power that are "booked out" cannot be distinguished in any meaningful way from sales that are not booked out. Moreover, Seattle asserts that the argument is moot because it will offset its sales during the remedy phase of the proceeding.

881. Next, Seattle argues that Respondents wrongly rely on statements made by Seattle's witnesses concerning allegations of unlawful activity. Seattle contends that it submitted evidence in this proceeding that demonstrates that each Respondent charged Seattle an unlawful market-based rate. Additionally, Seattle states that neither witness is an attorney and neither offered legal opinions on whether Respondents' market activities were lawful or unlawful.[733] Moreover, Seattle notes that Mr. Hanser stood by his non-legal conclusions concerning the markets and did not withdraw any testimony regarding these issues.[734]

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[732] Order on Rehearing at P 32.

[733] Seattle notes that Respondents' motions to strike were granted in part on the grounds that Mr. Hanser was offering legal conclusions. *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 31 (July 29, 2013) (Order Granting Indicated Respondents Motion to Strike).

[734] Tr. 2269:13-2270:21 (Hanser).

882. With respect to the identification of contracts, Seattle asserts that the terms of each contracts are the WSPP Agreement and the agreed upon price, quantity, flow date, and delivery point. Seattle states that it provided a database with the requisite information. Seattle contends that it did not have to produce or examine the trader tapes of each transaction because under the WSPP Agreement, each Respondent is required to make its own recording of those conversations, and the information can be confirmed by looking at the invoices sent to Seattle.

883. Seattle also states that it has demonstrated that Respondents' sales and market activity created an undue burden on Seattle's consumers, harmed the public interest, and were discriminatory. Seattle contends that Respondents wrongly argue that the public is best served by not interfering with the markets because market forces may or may not produce market-based prices for wholesale energy that are just and reasonable.

884. Lastly, Seattle argues that El Paso wrongly relies on a prior settlement with the Washington Attorney General. Seattle notes that the Washington Attorney General was not a claimant and did not submit evidence in this case.[735] Additionally, the Washington Attorney General never represented Seattle in this proceeding and, by law, could not have represented Seattle in this proceeding.[736] Nor did Seattle participate in the settlement discussions, sign the settlement agreement, or authorize the Washington Attorney General to sign on Seattle's behalf.[737]

885. Furthermore, Seattle asserts that El Paso acknowledged that the releases granted pursuant to the settlement agreement were not intended to affect the rights of other non-settling parties in this case.[738] Seattle contends that El Paso understood and intended that some portion of the settlement funds allocated to the Washington Attorney General would be used for the benefit of energy consumers in Washington, which would include consumers in Seattle, and that such benefit was not intended to affect the rights of

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[735] *See* Washington State Attorney General, Brief to the Administrative Law Judge on Pacific Northwest Refund Issues, Docket No.EL01-10-000, at 5 (filed Sept. 17, 2001).

[736] City of Seattle, Washington November 7, 2012 Declaration of William H. Patton at P 2.

[737] *Id*. P 3.

[738] California Parties and Indicated Attorneys General, Joint Motion for Partial Dismissal of El Paso from Specific Proceedings, Docket Nos. EL00-95-089, EL00-98-075, EL01-10-013, *et al.* (filed Aug. 8, 2003) ("[t]hese releases are not intended to affect the rights of other, non-settling parties in any of the Subject Proceedings").

non-settling parties like Seattle. Moreover, Seattle notes that in 2007, El Paso did not take the position that Seattle was bound by the settlement agreement.[739]

### 13. Indicated Seattle Respondents Reply Brief

#### (a) Conflation of Section 206 and Section 309 Claims

886. Indicated Respondents contend that Seattle ignores the differences between the two distinct statutory provisions and how *Mobile-Sierra* applies to each provision. Indicated Respondents assert that section 309 provides relief in a narrower set of circumstances than does section 206.[740] Indicated Respondents argue that Seattle wrongly claims that it may be entitled to relief under section 309 if it demonstrates that the contract rates were not just and reasonable or if the contracts impose an excessive burden on consumers. Indicated Respondents aver that under section 309, Seattle must show a violation of a statute or tariff. Indicated Respondents also contend that Seattle offered no legal reasoning to explain why the Commission's residual power under section 309 should apply during a period when Seattle is free to make allegations (including allegations of statutory and tariff violations) under section 206.

887. Additionally, Indicated Respondents contend that Seattle improperly conflates factual issues. Indicated Respondents state that Seattle provided no benchmark analysis with respect to the Section 206 Period, and there is no evidence to support its claims that prices charged by the Respondents were above competitive levels. Indicated Respondents further note that the undersigned specifically directed that Seattle's "competitive benchmark" analyses do not apply to the period beginning December 25, 2000.[741]

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[739] *See* El Paso Marketing, LP, Joint Offer of Settlement, Docket Nos. EL00-95-000, EL00-98-000, EL01-10-000, *et al.* (filed Apr. 2, 2007). *See also* City of Seattle, Washington, Notice of Election to Opt-Out of the El Paso Settlement, Docket Nos. EL00-95-000, EL00-98-000, EL01-10-000, *et al.* (filed Apr. 23, 2007).

[740] *California. ex rel. Brown*, 135 FERC ¶ 61,178, at P 82 (2011) ("the California AG cannot circumvent the temporal limitation of FPA section 206 by seeking relief under FPA section 309"). *See also AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1748 (2011); *see accord Tex. & Pac. Ry. Co. v. Abilene Cotton Oil Co.*, 204 U.S. 426, 446 (1907); *Telesaurus VPC, LLC v. Power*, 623 F.3d 998, 1011 (9th Cir. 2010); *Balt. & Ohio R.R. Co. v. Ala. Great S. R.R. Co.*, 506 F.2d 1265, 1270 n.21 (D.C. Cir. 1974).

[741] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 23 (June 20, 2013) (Order Granting in Part and Denying in Part Motion to Strike).

### (b) Claims Pursuant to Section 206 of the FPA

#### (i) Allegations of Unlawful Activity by Respondents

888. Indicated Respondents assert that the *Mobile-Sierra* presumption applies to the contracts at issue because Seattle did not demonstrate that any Respondent engaged in unlawful activity. Indicated Respondents note that Seattle's initial brief makes no mention of any particular Respondent in connection with any unlawful activity or particular contract.[742]

889. Indicated Respondents state that for the first time in its initial brief, Seattle alleges that each Respondent acquired and exercised market power. However, Indicated Respondents contend that no Seattle witness offered testimony or analysis of any kind as to the acquisition of market power by any Respondent.[743] Additionally, Indicated Respondents assert that Seattle did not even address evidence that demonstrates that Respondents did not acquire market power.[744]

890. Next, Indicated Respondents contend that they never asserted that any price charged under a market-based rate regime is always just and reasonable, or that prices charged under market-based rates are not subject to the FPA. Rather, Indicated Respondents argue that in the absence of evidence of market power or manipulation by a seller, as is the case here, the Commission may presume that market-based rates are just and reasonable.

891. Indicated Respondents further aver that contrary to Seattle's assertion, *Montana Consumer Counsel* expressly found that the Commission can presume that prevailing market rates are just and reasonable if there is no evidence of market power or manipulation.[745] Specifically, the court stated that "[w]here sellers do not have market power or the ability to manipulate the market (alone or in conjunction with others), it is not unreasonable for FERC to presume that rates will be just and reasonable."[746]

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[742] The only mention of a Respondent by name is to identify it as a respondent and to identify any stipulations with a particular respondent.

[743] Indicated Respondents Initial Br. at 38, 49-59.

[744] *See* Ex. AVE-10. *See also* Ex. PPL-4 at 6:12-9:12; Ex. TAE-8 at 63:9-17; Ex. EP-1 at 5:15-6:10; Ex. SNA-9 at 6:21-7:1; Ex. PSC-1.

[745] *Mont. Consumer Counsel v. FERC*, 659 F.3d 910, 918-19 (9th Cir. 2011).

[746] *Id.*

Additionally, Indicated Respondents note that the D.C. Circuit has held that "what matters is whether an individual seller is able to exercise anticompetitive market power, not whether the market as a whole is structurally competitive."[747] Indicated Respondents contend that once a seller has passed the Commission's tests for market-based rate authority, as all of the Respondents have, and there is no other evidence of market power or manipulation by the sellers, as is the case here, then the market is assumed to be sufficiently competitive to set a just and reasonable price, and the rates charged are not unlawful.

892. With respect to Seattle's assertions regarding high prices, Indicated Respondents note that high prices may occur in competitive markets, especially during times of scarcity,[748] and that high prices act as a signal in competitive markets for investment in new generation.[749] Indicated Respondents contend that Seattle's statements regarding peak prices were misleading because there is no evidence that Seattle bought power from any Respondent at the "record-breaking prices."

893. Next, Indicated Respondents address Seattle's claim that the rates in the Pacific Northwest were unduly discriminatory in comparison to the OOM sales in California. First, Indicated Respondents aver that Seattle's suggestion that its purchases were made at unduly discriminatory prices if they exceeded the MMCP ignores the Order on Remand, which stated that Seattle must "demonstrate that a particular seller engaged in unlawful market activity in the spot market and that such unlawful activity directly affected the particular contract or contracts to which a seller is a party."[750] Second, Indicated Respondents assert that sellers sold energy at market prices and the MMCP was an after-the-fact remedial construct for California organized spot markets. The

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[747] *Blumenthal v. FERC*, 552 F.3d 875, 882 (D.C. Cir. 2009).

[748] *See Blumenthal*, 118 FERC ¶ 61,205, at P 32 (2007) ("just because market-based rates exceed cost-based rates during conditions of scarcity does not mean that such market-based rates become unjust or unreasonable during these periods). *See also N.Y. Indep. Sys. Operator, Inc.*, 131 FERC ¶ 61,169, at P 81 (2010) (finding that in market-based regime in times of scarcity generators have the opportunity "to receive compensation above their marginal costs").

[749] Ex. NW3-1 at 14. Indicated Respondents note that the Commission has approved price caps as high as $3,500/MWh to represent scarcity price levels and ensure reliability. Ex. PNR-1 at 41. *See also Midwest Indep. Transmission Sys. Operator, Inc.*, 119 FERC ¶ 61,311 (2007).

[750] Order on Remand at P 21.

Commission simply found that OOM sales were inextricably tied to those markets.[751] Thus, Indicated Respondents assert that the MMCP does not represent discriminatory actions by sellers.

894. Indicated Respondents also assert that Seattle's argument ignores the Commission's determination that the MMCP or another market-wide remedy does not apply in this proceeding. Indicated Respondents further note that the Commission also concluded that these bilateral sales were subject to the *Mobile-Sierra* presumption, a finding it did not make as to the sales to which it applied the MMCP.

895. Furthermore, Indicated Respondents contend that Seattle failed to show that the complaining customer is "similarly situated" to the customer allegedly favored.[752] Indicated Respondents state that Seattle did not refer to any evidence in the record and merely asserted that it was similarly situated to the California ISO. Indicated Respondents assert that unlike the CAISO, Seattle did trade energy for profit and sought to get the highest price it could for the energy it sold.[753] Moreover, Seattle operated its resources to maximize sales revenue, using its hydro system as a mechanism for storing energy to be sold later at a premium.[754] Indicated Respondents note that Seattle derived approximately $100 million in sales of energy in the spot market during the periods at issue in this proceeding.[755]

896. Additionally, Indicated Respondents aver that all of the participants in the market were "price takers" in the sense that transactions were at prevailing market prices.[756] Indicated Respondents also state that purchasers, including Seattle, were able to dictate certain key terms of transactions to PSCo, such as firmness and point of delivery.[757]

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[751] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,516 (2001).

[752] *See, e.g., Pub. Serv. Co. of Ind., Inc. v. FERC*, 575 F.2d 1204, 1212-13 (7th Cir. 1978). *See, also NRG Power Mktg., LLC v. FERC*, 718 F.3d 947, 958 (D.C. Cir. 2013).

[753] *See* Tr. 3182:2-16 (Morter).

[754] Tr. 3250:14-3251:8 (Morter). *See also* SCL-10 at 9-10.

[755] *See* Tr. 2180:9-20 (Hanser).

[756] *See, e.g.*, Tr. 3090:13-3091:17 (Toole).

[757] *See* Ex. PSC-1 at 21:9-22:16.

Lastly, Indicated Respondents assert that Seattle's attempt to place itself in the same position as the California ISO ignores an important difference between the California and Pacific Northwest markets, such as Seattle's ability to enter into forward contracts.

897. Lastly, Indicated Respondents respond to Seattle's assertion that the reserve margins demonstrate that there was adequate supply, and therefore, market fundamentals do not explain high prices. Indicated Respondents note that Mr. Hanser acknowledged that this data, which was presented in Professor Hogan's testimony,[758] should not be used to show that reserves were adequate.[759] Indicated Respondents state that Professor Hogan offered this data because it showed that reserve margins during the periods at issue in this proceeding were much lower than in prior years, and in most cases, by far the lowest during the entire 11 year period.[760] Thus, the data support Professor Hogan's conclusion that supply and demand during the time were at historically tight levels.

**(ii) Allegations that Contracts Imposed an Undue Burden on Consumers or Harmed the Public Interest and Are Unduly Discriminatory**

898. Indicated Respondents repeats its argument that none of Seattle's excess burden analysis was tied to any specific contract or Respondent.

899. With respect to Seattle's claims that it acted prudently when reducing its entitlement to BPA power and selling its share in the Centralia generating facility, Indicated Respondents assert that prudence at the time is not the issue. Rather, Indicated Respondents state that those decisions resulted in Seattle's increased reliance on wholesale power, which in part, caused higher rates for Seattle's customers.

900. Indicated Respondents also argue that Seattle wrongly asserts that the unclean hands doctrine deals with remedy. Indicated Respondents state that this doctrine is about liability and is not a mechanism to allow Seattle to deduct the proceeds of its misconduct from refunds ordered from Respondents. Rather, the doctrine forecloses a claim for refunds at the outset.[761] Additionally, Indicated Respondents assert that Seattle's status

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[758] *See* Ex. PNR-1 at 165.

[759] Tr. 2008:13-17 (Hanser).

[760] Ex. PNR-1 at 164:11-21; *see also* Tr. 1996:8-1999:8 (Hanser).

[761] *See, e.g., Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814-15 (1945). *See also La. Pub. Serv. Comm'n v. Entergy Servs., Inc.*, 142 FERC

(continued…)

as a non-FERC jurisdictional entity does not protect it from the application of the unclean hands doctrine, which applies to all who seek equity.[762]

### (c) Claims Pursuant to Section 309 of the FPA

901. Indicated Respondents argue that Seattle's theory that making a sale in excess of the average region-wide marginal costs violates a seller's market-based rate tariff or the FPA would bring uncertainty and disruption to the many U.S. power and gas markets reliant on market-based rate sales. Indicated Respondents further note that the Commission has recognized that high prices—including prices higher than those at which Respondents made sales to Seattle—play an important role in energy markets.[763]

902. Indicated Respondents also assert that Seattle's "speed limit" analogy[764] is not applicable because there is no marginal cost "price limit" for sellers with market-based rates. Furthering the analogy, Indicated Respondents contend that Seattle is asking the Commission to devise a retroactive speed limit, and hand out tickets to drivers who had no possible way of ascertaining that speed limit.

### (d) Proper Definition of Spot Market

903. Indicated Respondents assert that fundamental differences between the wholesale market design in the Pacific Northwest and California do not require a different definition of the spot market. Indicated Respondents note that it is widely-accepted that spot market transactions are commodity market trades for immediate delivery, and across the country, in both bilateral and organized markets, the same definition of spot market is

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¶ 61,211, at P 53 (2013) (affirming order invoking Commission's "equitable discretion to deny refunds" that it has the statutory authority under section 206(c) to award).

[762] *See Precision Instrument*, 324 U.S. at 815.

[763] *See, e.g., Midwest Indep. Transmission Sys. Operator, Inc.*, 123 FERC ¶ 61,297, at P 106 (2007) (approving price caps as high as $3,500/MWh to represent scarcity price levels and ensure reliability); *see accord ISO New England, Inc.*, 138 FERC ¶ 61,027, at P 108 (2012).

[764] Seattle asserts that netting contracts above and below the MMCP is like letting a motorist that speeds through a school zone escape liability for his traffic violation simply because he obeyed the speed limit on some other occasions. Seattle Initial Br. at 28.

used.[765] Moreover, Indicated Respondents note that BPA's witness who testified in this proceeding in 2001 did not testify that spot market transactions should extend out to five years as Mr. Morter had suggested.[766] Rather, BPA's witness testified that "Pacific Northwest spot market bilateral sales should be limited to real-time sales (within the same day, next hour), prescheduled sales (for the following 24-hour period), and within month and balance of the month sales (those sales that occur after the first of any month, for some short duration within the month, or for the remainder of the month)."[767] Similarly, PacifiCorp witness Stan Watters acknowledged that the most common definition for spot sales included transactions with a duration as 24 hours or less.[768]

904. With respect to Seattle's characterization of the Respondents' spot market definition as self-serving, Indicated Respondents assert that Seattle's definition can be characterized the same way because it extends the number of potential transactions subject to refund.

### 14. Constellation Energy Commodities Group, Inc. Reply Brief

#### (a) Claims Pursuant to Section 206 of the FPA

##### (i) Allegations of Unlawful Activity by Respondents

905. Constellation asserts that Seattle failed to meet its burden in showing that Constellation engaged in unlawful activity that affected specific contracts. Constellation argues that Seattle misinterprets Commission precedent regarding the relationship between the California market and the Pacific Northwest market. Constellation acknowledges that the Commission's December 19, 2001 Order found that the California markets were "not competitive and were subject to manipulation" during the Section 206 Period.[769] However, Constellation states that the Commission held that "systematic dysfunction" in the single-clearing-price auction market, not sellers' actions, rendered the

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[765] *See* Ex. JDG-1 at 7:3-16; Tr. 3365:5-14 (Cavicchi).

[766] *See* Tr. 3226:25-3227:3, 3228:18-21 (Morter).

[767] Ex. SCL-82 at 27.

[768] *See* Ex. SCL-83 at 5.

[769] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275 (2001).

market uncompetitive.[770] Moreover, the Commission rejected claims that "sellers' bidding strategies resulted in market clearing prices rising above competitive levels."[771]

906. Furthermore, Constellation avers that Seattle wrongly suggests that the Commission has already determined that Constellation, and other sellers in the instant proceeding, manipulated the California market. Constellation asserts that the Commission never made any determination that any market manipulation occurred during the Section 206 Period and found that the CAISO auction market structure suffered design flaws.[772] Constellation also states that Seattle implies that sellers made "material misrepresentations" in their sales to Seattle. Constellation avers that this implication is unsubstantiated, improper, and without basis in the record.

907. Next, Constellation asserts that Seattle wrongly relies on Ninth Circuit's *Montana Consumer Counsel* opinion to support a claim that FERC cannot rely on market forces to fulfill its obligations under the FPA to ensure prices are just and reasonable. Constellation acknowledges that the court stated that "FERC may not substitute prevailing market prices for its own judgment."[773] However, the court immediately upheld the Commission's approach to determining market power using specific data screens to determine if the seller possesses market power before granting market-based rate authority.[774]

#### (ii) Allegations that Contracts Imposed an Undue Burden on Consumers or Harmed the Public Interest and Are Unduly Discriminatory

908. Constellation first notes that in its initial brief, Seattle admitted that spot market sales from respondents to Seattle accounted for "less than 1 percent of [Seattle's] total load" during the relevant period.[775] Constellation argues that this admission undercuts

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[770] *Id.* at 62,218.

[771] *Id.* at 62,202.

[772] *Id.* at 62,171.

[773] *Id.*

[774] *Mont. Consumers Council v. FERC*, 659 F.3d 910, 918-19 (2011).

[775] Seattle Initial Br. at 6.

Seattle's later assertions that the rates charged imposed an excessive burden on Seattle's consumers.

909. Next, Constellation addresses Seattle's allegation that the Respondents' exercise of market power had the potential to cause brownouts and blackouts in the Pacific Northwest, and, therefore, Respondents' contract rates with Seattle were contrary to the public interest. Constellation states that its sales to Seattle obviously reduced the likelihood of blackouts and Seattle provided no evidence that any seller withheld power.[776] Further, Constellation argues that retroactively abrogating contracts during times of scarcity would discourage sellers from entering into contracts, reducing needed supplies.[777]

910. Constellation also contends that Seattle wrongly claims that Respondents discriminated against Seattle in favor of California. Constellation notes that the Joint Statement of Issues, with which Seattle agreed, does not contain an allegation of "discrimination," and Seattle cannot raise this new issue in its Initial Brief now that the record is closed. Additionally, Constellation states that there is no evidence of a flawed market design in the Pacific Northwest, and therefore, adopting different pricing in the two markets would not discriminate against Seattle's customers. Constellation also notes that Seattle was not similarly situated to the CAISO because Seattle had the ability to enter forward contracts and was not a grid operator that was forced to buy energy at the last minute.

### (b) Claims Pursuant to Section 309 of the FPA

911. With respect to Seattle's claims regarding the record high prices in the Pacific Northwest, Constellation states that the true reasons for the "high prices" on December 11 included weather forecasts that turned out to be incorrect.[778]

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[776] *See* Tr. 2118:13-2119:1 (Hanser).

[777] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 551 (2008) ("uncertainties regarding rate stability and contract sanctity can have a chilling effect on investments and a seller's willingness to enter into long-term contracts and this, in turn, can harm customers in the long run").

[778] *See* Staff Report to the Federal Energy Regulatory Commission on Northwest Power Markets in November and December 2000 (Feb. 1, 2001), *available at* http://www.ferc.gov/legal/maj-ord-reg/land-docs/draft0131b.pdf.

912. Next, Constellation asserts that Seattle wrongly claims that the Commission has already determined that the MMCP represent a competitive price in the Pacific Northwest because of the mitigation of CAISO's OOM transactions. Constellation notes that the Commission did not conclude that all OOM transactions require mitigation, and that if the Commission did decide to mitigate the OOM sales, they would be mitigated in the context of the California Refund proceeding.[779]

913. Constellation also argues that Seattle mischaracterizes Respondents' claim regarding "netting" transactions below the MMCP. Constellations asserts that Mr. Cavicchi did not testify that Mr. Hanser should have "netted" the amounts, but instead testified as to the inherent flaws in Mr. Hanser's analysis, which ignores all the instances that the rates fell below Seattle's proposed MMCPs.[780]

914. Next, Constellation states that Seattle asserts that the Commission rejected arguments to the MMCP based on its failure to include opportunity costs, transmission-related costs, and scarcity rents. Constellation notes that the Commission's discussion in the order Seattle cites pertains to the unique attributes of the California market and highlights the fact that these markets are substantially dissimilar. Specifically, the Commission held that in the CAISO market "opportunity costs are not appropriate because energy that is available in real time cannot be sold elsewhere."[781] However, Constellation avers that in the Pacific Northwest, sellers had numerous counterparties with whom to transact. Additionally, Constellation notes that the Commission's order does not discuss whether transmission costs may be included in the MMCP calculation in a bilateral market.[782]

#### (c) Conflation of Section 206 and Section 309 Claims

915. Constellation contends that Seattle improperly blends the Section 206 and 309 Periods together, arguing that it can submit identical claims for refunds for both temporal

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[779] *See Cal. Pub. Util. Comm'n v. FERC*, 456 F.3d 1025, 1052 (9th Cir. 2006) ("it is [] significant to note that FERC did not order refunds for all [CAISO] OOM transactions. Rather, FERC ordered that all [CAISO] OOM spot transactions to be examined to decide which ones would be subject to potential refund").

[780] *See* Ex. JDG-7 at 5:8-11.

[781] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,212 (2001).

[782] *Id.* at 62,211.

periods at issue in this case. Constellation states that under FPA section 206, FERC has the authority to investigate whether a particular rate is "just and reasonable." If FERC finds the rate unjust and unreasonable, it may order sellers to pay refunds to those who bought energy,[783] but such refunds are limited to a period following the "refund effective date," which is triggered by the filing of the complaint.[784] Constellation asserts that the refund effective date under section 206 places all market participants on notice that they may be subject to refunds.[785] In this proceeding, Constellation states that the refund effective date is December 25, 2000.[786]

916. Constellation states that unlike section 206, FPA section 309 gives FERC remedial authority to order refunds if it finds violations of a filed tariff.[787] Constellation notes that in the Order on Rehearing, the Commission held that it "may order refunds, if appropriate, for transactions between January 1, 2000 and December 24, 2000, under its FPA section 309 authority."[788] Constellation asserts that the Commission clearly delineated between the two periods and statutory sections in accordance with federal law and statute.[789] Additionally, Constellation states that the Ninth Circuit has also clearly held that the time period applicable to a section 206 proceeding does not apply to a section 309 proceeding.[790] Constellation states that the separation between the two periods and statutory sections in this proceeding is important because, although the *Mobile-Sierra* protections apply to both,[791] under the law Seattle must first make a

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[783] 16 U.S.C. § 824e(a) (2012).

[784] 16 U.S.C. § 824e(b) (2012).

[785] *See Port of Seattle v. FERC*, 499 F.3d 1016, 1031-32 (9th Cir. 2007).

[786] *See id*.

[787] 16 U.S.C. § 825h (2012). *See Consol. Edison Co., Inc. v. FERC*, 347 F.3d 964, 967 (D.C. Cir. 2003).

[788] *See* Order on Rehearing at P 32.

[789] *Id*.

[790] *See Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1049 (9th Cir. 2006) ("[t]o the extent that FERC is claiming that the § 206 time limits apply to § 309 proceedings, FERC is wrong").

[791] *See* Order on Rehearing at P 13.

threshold showing of a violation under section 309. Thus, there are different legal standard applicable to each period.

917. However, Constellation argues that even if the Commission deems Seattle's section 309 claims to apply to the Section 206 Period, Seattle's failure to establish any unlawful violation to support its section 206 claims likewise defeats any claim under section 309.

### 15. Avista Utilities and Avista Energy Joint Reply Brief

918. Avista Entities state that Seattle's initial brief failed to provide Respondent specific or contract-specific allegations against Avista Utilities or Avista Energy. Avista Entities note that Seattle provides only a generic case and seeks an improper market-wide remedy. Avista Entities note that Seattle has repeatedly confused the two distinct Avista entities.[792] Avista Entities contend that this illustrates Seattle's approach to its case of not identifying specific Respondents or contracts and seeking a market-wide remedy.

### 16. PPL Montana, LLC and PPL EnergyPlus, LLC Reply Brief

919. PPL states that Seattle failed to even mention of PPL in Seattle's initial brief, other than to identify it as a respondent, and presented no evidence specific to PPL or PPL's contracts with Seattle. PPL notes that Seattle provided only generalized allegations of market power and tariff violations, but submitted no market power analysis or discussion of PPL's tariff.

### 17. Cargill Power Markets, LLC Reply Brief

920. Cargill states that Seattle claims that it is similar to the California ISO because both "were price takers that were forced to pay outrageously high prices in order to serve their load."[793] Cargill asserts that this is inaccurate because the record demonstrates that Cargill was often a price-taker within the Pacific Northwest market, including in its transactions with Seattle.[794] Cargill also argues that Seattle wrongly claims that its

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[792] *See* Ex. SCL-76 at 16:12-21; City of Seattle, Washington August 23, 2013 Prehearing Brief at 14-15.

[793] Seattle Initial Br. at 39.

[794] *See* Tr. 3090:13-3091:17 (Toole).

energy trading was conducted simply to serve its load or for balancing purposes. Cargill states that Seattle's trading was designed to maximize revenue.[795]

### 19. Public Service Company of Colorado Reply Brief

921. PSCo asserts that Seattle wrongly claims that, as a load-serving entity, it was a price taker that was forced to buy energy at whatever price and under whatever terms were thrust upon it. PSCo notes that it submitted unrefuted testimony demonstrating that the market was sufficiently competitive to enable purchasers to be selective about the energy product that they were purchasing. Thus, purchasers, such as Seattle, were able to dictate certain key terms of transactions to PSCo.[796] PSCo also contends that the record in this proceeding clearly contradicts Seattle's argument that PSCo exercised market power. PSCo states that the Commission determined that PSCo did not possess market power and could continue charging market-based rates during the exact time period for which Seattle seeks refunds.[797]

### 20. Commission Trial Staff Reply Brief

#### (a) Claims Pursuant to Sections 205, 206, and 309 of the FPA

922. Trial Staff asserts that all of Seattle's allegations rely on an assertion that each Respondent acquired and exercised market power. However, Trial Staff argues that Seattle provided no analysis as to how each Respondent acquired market power. Trial Staff states that Seattle assumes that sellers had market power because the price was too high – above the MMCP. Trial Staff contends that Seattle's failure to examine each Respondent's alleged market-power means Seattle failed to meet its burden. Thus, Seattle did not demonstrate a violation of market-based tariffs or section 205 of the FPA.

923. With respect to Seattle's assertion that it only needs to show that the market in the Pacific Northwest and the prices it produced were dysfunctional, non-competitive, and somehow subject to manipulation, Trial Staff contends that Seattle did not make such a showing. Furthermore, Trial Staff states that the Commission specifically held that it was not sufficient for complainants to simply show "a general link between the dysfunctional spot market in California and the Pacific Northwest spot market" or that the Pacific

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[795] *See* Tr. 3182:2:16 (Morter).

[796] *See* Ex. PSC-1 at 21:9-18.

[797] *See* Ex. PSC-6.

Northwest spot market was generally dysfunctional.[798] Trial Staff asserts that Seattle's allegations rely exclusively on a general analysis of wholesale energy markets and Seattle makes no attempt to specifically analyze any Respondent or even the Respondents as a group.

924. Next, Trial Staff specifically addresses Seattle's claim that prices above the MMCP indicate a seller's exercise of market power. Trial Staff first notes that Seattle only performed an MMCP analysis for the Section 309 Period, but in its Initial Brief, the MMCP is conflated into Seattle's sole measure for all claims based on individual wrongdoing, including claims for the Section 206 Period. Trial Staff also avers that the MMCP never been used by the Commission or courts as a means to establish market power.[799] Furthermore, Trial Staff contends that Seattle's market power allegation is circular – Respondents must have acquired market power because their prices were too high, which allowed them to charge prices that were too high as they exercised that market power. Lastly, Trial Staff notes that although Seattle charged prices in excess of the MMCP, it has not admitted that it had or was exercising market power.

925. Trial Staff also argues Seattle misconstrues the legal framework of market-based rates in asserting that Respondents believe they are not "subject to the rule of law" such that a party can charge "any price they please." Trial Staff states that Seattle relies on the Ninth Circuit's statement that "the Commission cannot fulfill its duty under the FPA to make sure that prices for wholesale energy are 'just and reasonable' by relying on market forces alone."[800] However, Trial Staff notes that the Ninth Circuit was clear that FERC did fulfill its duty under the FPA by "screening individual sellers for market power."[801]

926. With respect to Ms. Steffy's statement that there was "no zone of reasonableness," Trial Staff asserts that this statement was in the context of the Commission having determined that the seller did not have market power. Trial Staff states that this statement was nothing more than a recognition that the courts have held that when the Commission goes beyond "market forces alone" to determine that a particular Respondent lacks

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[798] Order on Remand at P 21. *See also* Order on Rehearing at P 30.

[799] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC 61,294, at 61,998 (2000) (the Commission did not make findings "about whether particular rates charged by specific sellers during the summer of 2000 were unjust or unreasonable or that any individual sellers exercised or abused market power").

[800] *Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011).

[801] *Id.* at 917.

market power, that determination also constitutes a determination that prices negotiated between that entity and a buyer were, by definition, within the zone of reasonableness—and therefore just and reasonable.[802]

927. Trial Staff asserts that Commission orders determined that each Respondent did not have market power, and established that each Respondent's filed rate was its market-based tariff. As such, Trial Staff states that each Respondent was obliged to charge prices for wholesale power consistent with its filed rate, its market-based tariff, and did not have authority to do otherwise.[803]

**(b) Allegations that Contracts Imposed an Undue Burden on Consumers or Harmed the Public Interest and Are Unduly Discriminatory**

928. Trial Staff argues that Seattle failed to demonstrate that the contracts between Respondents and Seattle impose an excessive burden or seriously harm the public interest. Trial Staff notes that Seattle did not isolate an undue burden caused by any Respondent individually or as a group of Respondents. Trial Staff asserts that Seattle wrongly relies on allegations that Respondents exercised market power in charging prices above the MMCP.

929. With respect to Seattle's claim that unlawful actions by sellers had the potential to cause brownouts and blackouts in the Pacific Northwest, Trial Staff states that these events did not actually occur and Seattle provided no evidence that the events would have been the result Respondents' actions.

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[802] *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, at P 409, *clarified*, 124 FERC ¶ 61,055, *order on reh'g*, Order 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), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011), *cert. denied*, 133 S. Ct. 26 (2012). *See also Montana Consumer* 659 F.3d at 916-917; *PJM Interconnection, L.L.C.*, 121 FERC ¶ 61,173, at P 21 (2007).

[803] *Associated Gas Distribs. v. FERC*, 898 F.2d 809, 810 (D.C. Cir. 1990) ("[u]nder the filed rate doctrine, a regulated entity may not charge, or be forced by the Commission to charge, a rate different from the one on file with the Commission for a particular good or service").

930. Lastly, Trial Staff addresses Seattle's discrimination claim. Trial Staff asserts that Seattle's argument is not an accusation leveled at the Respondents, but a complaint against the Commission and its Order on Remand. Specifically, Trial Staff avers that Seattle's discrimination theory blames the Commission for "permitting" the Respondents to discriminate. Trial Staff notes that the Respondents took no actions in limiting the price in California to the MMCP.

## B. Findings and Conclusions

### 1. Burden of Proof and Standard of Review

931. As discussed above, Seattle bears the burden of proof because it is the proponent of an order to abrogate the subject contracts and to require refunds.[804] In order to *avoid* the *Mobile-Sierra* presumption that the specific bilateral contracts the Seattle seeks to abrogate are just and reasonable under Issue 1(A), Seattle bears the burden of demonstrating that a particular Respondent engaged in "unfair dealing at the contract formation stage,"[805] which "alter[ed] the playing field for contract negotiations,"[806] and had "a causal connection … [to] the contract rate."[807] In other words, a particular Respondent must have "engaged in unlawful market activity in the spot market and … such unlawful activity directly affected the particular contract or contracts to which [TransCanada] was a party."[808] Absent a showing of unlawful activity by a Respondent that affected a particular contract with Seattle, the presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest* .[809]

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[804] 5 U.S.C. § 556(d) (2012) ("[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof" and any sanction imposed must be "supported by and in accordance with reliable, probative and substantial evidence").

[805] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008).

[806] *Id*. at 554; Order on Remand at P 20.

[807] *Morgan Stanley*, 554 U.S. at 555.

[808] Order on Remand at P 21.

[809] *Id.*

### 2. Spot Market Definition

932. Seattle and the Respondents disagree over the proper definition of spot market transactions applicable to this proceeding. Seattle advocated for a broad definition that included transactions with durations of up to one year.[810] Conversely, the Respondents uniformly defined spot market transactions as sales with durations of twenty-four hours or less, prescheduled no more than twenty-four hours in advance of delivery, consistent with the Western Electricity Coordinating Council's (WECC) prescheduling calendar and hourly scheduling practices and timelines.[811]

933. As numerous witnesses who actually traded in the Pacific Northwest during the relevant time period testified, Seattle's definition of spot market is inconsistent with common industry and other market usage of the term "spot" sale.[812] A definition of spot

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[810] Specifically, Seattle's proposed definition of spot market included (1) a sale that lasts one month or less, and (2) a sale that lasts longer than one month but less than one year if the sale was not part of the purchaser's long-term planning process. Ex. SCL-81 at 4-6; Ex. SCL-15 at 3-9.

[811] *See* Ex. AVE-1 at 8:10-13; Ex. AVE-12 at 8:16-9:15; Ex. AVI-1 at 80:1-2; Ex. AVI-67 at 20:13-22:2; Ex. CPM-1 at 5:1-22; Ex. CPM-2 at 5:3-6:4; Ex. EP-1 at 7:14-24; Ex. EP-2 at 6:1-8:3; Ex. PPL-1 at 9:1-14; Ex. PPL-10 at 5:7-6:17; Ex. PSC-1 at 7:9-8:7; Ex. PSC-4 at 5:4-7:2. *See also* Ex. SCL-115 at 33:22-24 ("Respondents uniformly take the position that, for the purposes of this case, 'spot' sale should be defined as a transaction that is for 24 hours or less and that is entered into the day of or day prior to delivery").

[812] *See* Ex. AVI-67 at 14-16 ("Having worked in the Pacific Northwest power market for over 30 years, I can state that Mr. Morter's definition of the 'spot market' is aberrant and at odds with the universal understanding of market participants"); Ex. AVE-12 at 9:2-4 ("Furthermore, my definition of a spot transaction is the commonly accepted definition in the Pacific Northwest power industry"); Ex. CPM-2 at 6:3-4 ("My proposed definition reflects trading practices that are widely established in the industry"); Ex. EP-2 at 6:19-7:1 ("During this period, spot market was not defined in relation to a particular purchaser's long-term planning process. Rather, my experience with common commercial practices in the Pacific Northwest during the period from January 1, 2000 through December 24, 24 2000 is that a spot market transaction was any transaction with a duration of 24 hours or less that is prescheduled no more than 24 hours in advance of delivery, with an allowance for the conventions of scheduling for weekends and holidays"); Ex. PPL-10 at 5:17-20 ("In my experience spot market transactions are uniformly understood to include only day-ahead or real-time transactions, consistent with the WECC pre-scheduling calendar and hourly scheduling practices and timelines.");

(continued…)

market that includes longer-term forward contracts or that varies based on Seattle's purchasing practices is both illogical and inconsistent with actual trading practices in the Pacific Northwest.[813] Moreover, the Respondents' experts adopted the same definition of spot market as the witnesses with firsthand knowledge of Pacific Northwest markets, citing published sources.[814] Indeed, the Commission has expressly adopted this definition of spot market in the WECC: "Spot market sales in the WECC are sales that are 24 hours or less and are entered into the day of or day prior to delivery,"[815] and that is the definition of spot market adopted by the undersigned for use in this proceeding.[816]

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Ex. PSC-4 at 6:9-10 ("My proposed definition reflects trading practices that are widely established in the industry").

[813] *See supra* note 812.

[814] *See* Ex. JDG-1 at 7:3-6; Ex. CCG-1 at 7:2-17; Tr. 3365:5-23 (Cavicchi) ("I believe the definition of a spot market is a purchase made for immediate or nearly immediate delivery …. I've stated clearly in the testimonies honestly that I'm really not aware of any markets, whether they be electricity or other markets, that have any other definition other than what I just described. And I think if you look in -- I cited one well-known economics text. I think if you look in any kind of economics dictionary, any kind of basic economics book, there's a general agreement that when you buy a product for immediate delivery, that's considered the spot market. Any other purchases that are made for delivery in the future are made based on expectations of supply/demand conditions in the future and typically fix a price as of the date you transact for when you take that delivery in the future.").

[815] *W. Elec. Coordinating Council*, 133 FERC ¶ 61,026, at P 1 n.3 (2010); *see also San Diego Gas & Elec. Co. v. Sellers of Energy & Ancillary Servs*., 95 FERC ¶ 61,418, at P 2 n.3 (2001) ("[T]he terms 'spot markets' or 'spot market sales' means sales that are 24 hours or less and that are entered into the day of or day prior to delivery.").

[816] As discussed more fully below, even under Seattle's proposed definition, Seattle failed to demonstrate that it is entitled to refunds in this proceeding.

### 3. Seattle's Claims Pursuant to Section 206 of the FPA

#### (a) Issue 1(A): Seattle Failed to Demonstrate that Any of the Subject Respondents Engaged in Unlawful Market Activity or that Specific Contract Rates Were Directly Affected

934. The Commission's Order on Remand makes clear that parties seeking refunds must "demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract."[817] Mr. Philip Q Hanser, the sole witness Seattle presented in its Section 206 direct case covering the period of December 25, 2000 through June 20, 2001 (Section 206 Period), and one of only two witnesses Seattle presented in this proceeding, clarified in response to questioning from the undersigned Presiding Judge that he was "not alleging any illegal conduct by any of the Respondents in this case."[818] Mr. Wayne L. Morter, Seattle's only other witness, stated that he too was "not making any allegations regarding unlawful activity or misconduct by El Paso … or any other Respondent."[819] These admissions are fatal to Seattle's Section 206 claims under Issue 1(A) because they demonstrate that Seattle has not made the central evidentiary showing of unlawful market activity by any Respondent as required by the Commission to abrogate the subject contracts or to obtain refunds.[820]

935. As part of his general allegations, Mr. Hanser initially alleged that "sellers in Western markets" engaged in such unlawful acts as physical withholding of power, Enron-type games, anomalous bidding practices, and economic withholding of power.[821] However, in response to cross-examination questions specifically addressing these

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[817] Order on Remand at 21 (citing *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 554 (2008); *California ex rel. Brown*, 135 FERC ¶ 61,178, at P 77 (2011); *Nev. Power Co. v. Enron Power Mktg. Inc.*, 125 FERC ¶ 61,312, at P 28 (2008)).

[818] Tr. 2074:10-15; 2116:24-2117:1 (Hanser).

[819] Tr. 3278:7-20 (Morter).

[820] Order on Remand at P 21 ("parties seeking refunds must submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract").

[821] Ex. SCL-1 at 11:23-19:13.

allegations, Mr. Hanser confirmed that he was not asserting that any named Respondent in this proceeding had engaged in these or any other acts of wrongdoing.[822] Mr. Hanser was asked about a wide range of potential unlawful market activity that, if established, might meet the Commission's requirements in this proceeding to establish that the *Mobile-Sierra* presumption that the subject spot market contract rates were "just and reasonable" should not apply. Mr. Hanser was asked, for example, whether he alleged that any Respondent:

- engaged in various forms of simple business fraud;
- acted inconsistent with permissible conduct under the California Power Exchange (CalPX) and CAISO tariffs, including the MMIP [Market Monitoring and Information Protocol] provisions against withholding, anomalous market behavior, and gaming;
- acted inconsistent with scheduling and bidding procedures of the CAISO tariff;
- engaged in manipulation depending on the filing of false and misleading schedules;
- withheld energy from the CalPX through Enron-style gaming;
- withheld energy in any market in order to elevate prices during the Section 206 Period;
- withheld energy from Seattle during the Section 206 Period;
- used various strategies to game CAISO's congestion management system during the Section 206 Period;
- made False Exports, engaged in a get shorty strategy, or engaged in a multiparty False Export;
- sold non-firm energy as firm energy; and
- artificially raised prices by using energy exchanges.

[822] Tr. 2118:10-2121:5 (Hanser).

In each and every instance, Mr. Hanser answered "no, I do not."[823]

936. Trial Staff witness Ms. Chrystina Steffy testified in response to Mr. Hanser and also affirmed that Mr. Hanser does not provide any evidence relating to any specific unlawful activity by any particular seller, whether a Respondent or not, as required by the first prong of the "unlawful activity" exception to the *Mobile-Sierra* presumption under Issue 1(A).[824]

937. With respect to the period from January 1, 2000 to December 24, 2000 (Section 309 Period), which is outside the scope of the time period relevant for its Section 206 claims, Seattle has attempted to argue that prices charged in excess of the "benchmarks" described in Mr. Hanser's Section 309 testimony demonstrate the existence of market power and reflect an unjust and unreasonable rate; [825] however, that argument was not timely raised with respect to the Section 206 Period.[826] In any event, for the reasons discussed under the Section 309 analysis, the "benchmarks" offered in support of that argument are not sufficient to demonstrate the existence of market power in the Pacific Northwest or that the subject contract rates were unjust and unreasonable.

938. As previously stated, Mr. Wayne L. Morter, Seattle's only other witness, stated that he too was "not making any allegations regarding unlawful activity or misconduct by El Paso … or any other Respondent."[827] Mr. Morter also attempts to define the specific

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[823] Tr. 2118:10-2121:5 (Hanser).

[824] Ex. S-21 at 5-6.

[825] *See, e.g.*, Tr. 2070:20-2072:2 (Hanser).

[826] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at P 23 (June 20, 2013) (Order Granting in Part and Denying in Part Motion to Strike) (granting Respondents' timely motion to strike those portions of Mr. Hanser's Section 309 testimony that purported to relate to the Section 206 Period and holding that, given that the City of Seattle had already submitted testimony and exhibits related to the Section 206 Period in September 2012 and March 2013, and that the filing period pertaining to the Section 206 Period had already closed, permitting the City of Seattle yet another bite of the apple as to its Section 206 claims through the back door of its Section 309 filing would not only have contributed to the confusion of an already voluminous and complicated record, but would have provided Seattle with an unfair litigation advantage not supported by the Commission's April 5, 2013 Order on Rehearing).

[827] Tr. 3278:7-20 (Morter).

bilateral contracts for which Seattle is seeking refunds in this proceeding. Mr. Morter provided eleven spreadsheets with his Section 206 testimony that purport to show spot purchases made by Seattle between December 25, 2000 and June 20, 2001 from the eleven Respondents against which Seattle was asserting claims as of March 12, 2013.[828] These spreadsheets, however, are of limited use in this proceeding because they lack information necessary for identifying specific transactions and because, as discussed above, Mr. Morter utilized an unsupported and overly expansive definition of "spot sale" that may include transactions that last up to one year.

939. The Commission's Order on Remand stated:

> [P]arties seeking refunds must submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract. With regard to this showing of a causal connection, a party seeking refunds must submit evidence that demonstrates that the seller's behavior 'directly affect[ed]' contract negotiations.[829]

940. Thus, in order to show a causal link between the seller's behavior and specific contracts and contract negotiations, Seattle must first identify the specific contracts. Trial Staff witness Steffy correctly observed that Mr. Morter's spreadsheets only provide the hourly deliveries made to Seattle and "fail to include other relevant information that would be necessary to completely understand the nature of the transactions."[830] Most importantly, Ms. Steffy notes that the spreadsheets "do not identify either the actual bilateral contract or the verbal agreement under which the specific deliveries were made" and therefore, do not include the date the contract was entered into, the term of the contract, and other important terms and conditions.[831] Such information would enable an

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[828] Ex. SCL-84 through SCL-94. Additionally, Mr. Morter provided nine spreadsheets with his Section 309 testimony that purport to show spot purchases made by Seattle between January 1, 2000 and December 24, 2000 from the nine Respondents against which Seattle was asserting claims as of June 3, 2013. Ex. SCL-97 through SCL-105.

[829] Order on Remand at 21 (citing *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 554 (2008); *California ex rel. Brown*, 135 FERC ¶ 61,178, at P 77 (2011); *Nev. Power Co. v. Enron Power Mktg. Inc.*, 125 FERC ¶ 61,312, at P 28 (2008)).

[830] Ex. S-23 at 9:12-15.

[831] *Id.* at 9:16-17.

understanding of whether the transaction was for an hour ahead, day ahead, within month, balance of month, monthly, quarterly, or annual term.[832] On cross-examination, Mr. Morter acknowledged the limited focus of his data. Specifically, Mr. Morter acknowledged that his data includes the price, the quantity, and the first day of flow, but does not include the transaction date or whether the transaction is for the next hour, the next day, or month ahead.[833] Accordingly, Mr. Morter's testimony fails to identify specific contracts or contract negotiations that may have been affected by allegations of specific seller unlawful activity as required by the Commission's Order on Remand.

941. Seattle failed to both identify the specific contracts at issue and allege any unlawful activity by any Respondent. Thus, Seattle did not demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract.[834]

#### (b) Issue 1(B): Seattle Failed to Demonstrate that the Subject Spot Market Contract Rates Imposed an Excessive Burden on Consumers or Seriously Harmed the Public Interest

942. In a subsequent order in this proceeding, the Commission clarified that a party to a contract could also overcome the *Mobile-Sierra* presumption by presenting evidence that a particular contract imposes an excessive burden or seriously harms the public interest.[835] However, as correctly pointed out by Respondents and Trial Staff, in reversing the Ninth Circuit on the issue of the showing required to prevail in setting aside contract rates otherwise presumed to be just and reasonable, the Supreme Court clarified in *Morgan Stanley* that a contract rate does not impose an excessive burden simply because it is above marginal cost.[836] Instead, the Commission can set aside a contract rate only in the event of "unequivocal public necessity" or "extraordinary

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[832] *Id.* at 9:21-23.

[833] Tr. 3214:5-14 (Morter).

[834] Order on Remand at 21.

[835] Order Granting Interlocutory Appeal at PP 12-15.

[836] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548-50 (2008).

circumstances."[837] The Court stated that these two conditions "[i]n no way can be … thought to refer to the mere exceeding of marginal cost."[838]

943. Seattle did not offer a "benchmark analysis" in support of its "excessive burden" claim for the Section 206 Period as it did for the Section 309 Period.[839] Mr. Hanser provided additional testimony following the Commission's Order on Rehearing on harm to the public interest, but that testimony was also limited to Section 309 claims for the Section 309 Period.[840] Nor did Seattle's witness Mr. Morter offer any testimony on excessive burden or harm to the public interest.[841] With regard to its Section 206 claims, Seattle relied on the testimony of Mr. Hanser to present the 2001 testimony of Ms. Paula Green and other public documents to assert excessive burden or harm to the public interest.[842]

944. The most obvious and fundamental failure of Ms. Green's testimony, as presented by Mr. Hanser, is that, contrary to the direction of the Commission, it does not tie any alleged burden or harm to specific contracts or Respondents.[843] Mr. Hanser in fact admitted that he did not review any transaction data at all as part of his testimony

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[837] *Morgan Stanley*, 554 U.S. at 550.

[838] *Id*.

[839] Tr. 1901:17-22 (Hanser) (admitting that no "benchmark analysis" was done for the Section 206 Period). In any event, for the reasons discussed under the Section 309 analysis, the "benchmarks" offered are not sufficient to demonstrate that Respondents' contracts imposed an excessive burden on consumers or seriously harmed the public interest.

[840] Ex. SCL-110 at 75-81 (providing testimony on financial harm to Seattle as a result of loss of retained earnings and costs of issuing bonds).

[841] *See* Ex. SCL-81 at 3:16-4:7 (describing the purpose of his testimony as addressing the definition of "spot" sales and bookout claims and sponsor Seattle's transaction reporting templates).

[842] *See* Tr. 1897:18-20 (Hanser) (admitting that as an expert witness, he is not providing facts).

[843] *See* Order on Rehearing at P 30 ("the Commission must evaluate each seller's conduct in relation to specific contract negotiations and/or whether the contract imposes an excessive burden on consumers").

covering the Section 206 Period, and there is no indication in the record that Ms. Green ever did so either.[844] Without evidence identifying individual contracts or transactions, it is impossible to evaluate whether a particular contract or contracts between a Respondent and Seattle imposed an excessive burden or seriously harmed the public interest, or to determine any "down the line" effect of the contract.

945. Mr. Hanser also adopted Ms. Green's reference to rate increases totaling fifty-eight percent that Seattle instituted at or about this time, alleging that these rate increases were the result of "increased costs for wholesale power that Seattle was forced to pay."[845] However, these rate increases were not tied to any specific wholesale energy costs, much less any costs that resulted from Respondents' contracts or behavior. Not only does Seattle fail to associate any purported burden with a particular Respondent's sale, but as Respondents point out, Seattle also disregards the impact of electricity prices in the Pacific Northwest on the customers of other load serving entities. For example, Mr. Hanser conceded that he performed no analysis of rate increases that other Pacific Northwest load serving entities experienced during the relevant period.[846] Similarly, Mr. Hanser also conceded that his testimony did not contain "any analysis of regional conditions and electric rate increases" that provide context for Seattle's rate increases.[847]

946. In point of fact, the evidence of record reflects that these rate increases were a result of a myriad of factors including many having nothing to do with wholesale energy costs at all. For example, nearly twenty percent of the increase (a percentage Mr. Hanser erroneously surmised at the hearing was only five to ten percent) came from increases in transmission costs having nothing to do with wholesale energy costs.[848] An additional portion of the increase, which Mr. Hanser was unable to quantify, came from the effect of capitalizing certain costs, and the effect of debt acquired before the period at issue.[849]

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[844] Tr. 1901:2-25 (Hanser).

[845] Ex. SCL-1 at 5:20, 34:5.

[846] Tr. 2200:14-18 (Hanser).

[847] Tr. 2200:19-23 (Hanser).

[848] Tr. 1981:3-1983:4 (Hanser).

[849] Ex. CCG-10 at 15 (independent consulting group's 2002 report on Seattle City Light finding that "SCL's current debt is primarily the result of a series of decisions made in the 1990's which when combined, created an enormous debt load for SCL … decision-makers decided to increase the debt load rather than increase rates or reduce operating costs").

Seattle's increased wholesale power costs also reflect the consequence of Seattle's business decisions to reduce its long-term purchases, sell its share of the Centralia coal plant, and increase reliance on the wholesale spot market,[850] which then coincided *with the lowest water year on record in 60 years* that limited hydroelectric generation output.[851] In fact, compelling and well supported expert testimony analysis of market fundamentals by Professor Hogan concluded that reduced hydro generation was the "single most important factor contributing directly and indirectly to the high power prices during the Western Power Crisis."[852]

947. None of these factors are consistent with the kind of excessive burden that courts and the Commission have held, in exceptional cases, might justify the reformation of contract rates. In fact, Seattle's average electric rates remained the lowest of the twenty-five largest cities in the United States in 2001.[853] For residential rates in particular, Seattle's average rate was 5.99 cents/kWh, well below the U.S. average of 8.48 cents/kWh.[854] These rate levels are inconsistent with any claim by Seattle of excessive burden.[855]

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[850] Tr. 1911:5-13 (Hanser) ("PRESIDING JUDGE: I'm sorry. I thought the thrust of the question was if the BPA contract had continued, would those contract rates have been lower at that point in 2000 and 2001 than the spot market rates that they were exposed to. THE WITNESS: Yes. They would have been for the period of time -- the period of time, the month basically from the summer of June of 2000 -- summer of 2000 through basically the beginning of the summer of 2001."); Ex. SCL-40 at 2 (Seattle City Light Issues Brief stating that for 2000 and 2001, Seattle is "more dependent on the market than we have been historically because of the sale of our share of the Centralia coal plant").

[851] Ex. SCL-10 at 10 ("Since late 2000, SCL's ability to use hydroelectric resources to restrict market purchases to off-peak periods has been greatly limited because of water conditions that are among the lowest in sixty years of record").

[852] Ex. PNR-1 at 83:4-7.

[853] Ex. PRX-260 at 3 (Seattle City Light 2001 Annual Report). *See also* Tr. 2208:6-14 (Hanser) (agreeing that Seattle's rates were the lowest out of the 25 largest cities).

[854] Ex. PRX-260 at 3.

[855] Additionally, for each year from 2002 to 2008, Seattle either had a rate decrease or no change to its rates, except in 2003 when there was a 1.4 percent increase.

(continued…)

948. Mr. Hanser also provided excerpts of bond offerings from 2001 and 2003 to support Seattle's claim that increased wholesale power costs incurred by Seattle led to an excessive burden.[856] Again, however, none of these documents analyze how any increased amounts for wholesale energy contracts translated into specific rate increases, much less how those amounts were connected to the Respondents or harmed the public interest. To the contrary, the documents showed that Seattle maintained its AAA credit rating during and after the period at issue.[857] Further, the undersigned concurs with the Respondents that the bond offering documents actually support their position that the higher wholesale power prices Seattle incurred were the result of market fundamentals of supply and demand and to a lesser degree, Seattle's own business decisions. For example, as Respondents point out, in the bond offering from 2001, Seattle explained to the investment community that its "financial results in 2000 were far below historical levels, due to a combination of subnormal water conditions and unusually high demand for power, which drove the cost of power supply to unprecedented levels."[858] Seattle also reported in the 2001 offering that its output from its "hydroelectric facilities is projected to be only 66 percent of the average output over the water conditions in the 49-year period from 1929 through 1978."[859] In the 2003 bond offering, Seattle reported to the investment community that it had increased rates in 2001 after it "was required to purchase large amounts of power in the wholesale market as a result of its 1996 decision to limit purchases from Bonneville, … the sale of Centralia Steam Plant in May 2000, and unusually poor water conditions in the water year beginning October 1, 2000."[860] Seattle's statements at the time thus confirm that any burden Seattle faced was the result of unanticipated market forces and its own decisions and do not support any claim of excessive burden or harm to the public interest as a result of the Respondents' sales to Seattle during the relevant period.

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Ex. CCG-17. Thus, there were no "down the line" effects of the Respondents' contracts.

[856] Ex. SCL-1 at 32:1-35. *See also* Ex. SCL-38; Ex. SCL-39.

[857] Ex. SCL-39 at 1. Mr. Hanser was unable at hearing to reconcile this AAA rating with the testimony he purported to adopt from Ms. Green that Seattle's credit rating was harmed. Tr. 2226:1-17 (Hanser).

[858] Ex. SCL-38 at 2.

[859] *Id.* at 3. *See* Tr. 1928:10-1929:21 (Hanser).

[860] Ex. SCL-39 at 2.

949. Seattle asserts that its prior business decisions are irrelevant to the inquiry in this proceeding because the prudence of those decisions is not at issue. Although Seattle's business decisions may have been prudent at the time they were made, those decisions led to unforeseen consequences that are relevant to whether Respondents caused an excessive burden on consumers or seriously harmed the public interest. Any rate increase associated with Seattle's wholesale energy costs was clearly impacted by Seattle's decision, prudent or otherwise, to rely more heavily on the spot market.

950. Further, while supply and demand market fundamentals are critical components in establishing market-based prices for wholesale sales of energy, Seattle failed to account for those market forces during the relevant period. Mr. Hanser acknowledged on cross-examination that he "never tried to analyze the Pacific Northwest demand" or overall supply during the relevant period,[861] and that he failed to analyze the effects of supply and demand fundamentals on price.[862]

951. Mr. Hanser's lack of any such analysis stands in stark contrast to Professor Hogan's careful and detailed analysis of the supply and demand fundamentals. While the record is replete with probative evidence regarding the complex confluence of market forces in the Pacific Northwest that caused significant increases in energy prices during the relevant period, Professor Hogan's testimony is particularly compelling. Professor Hogan explained that on the supply side, the large reduction in hydro generation (coinciding with the lowest water year on record in 60 years) was particularly critical because Pacific Northwest purchasers rely heavily on hydro generation.[863] The reduction in hydro generation output led to an increased demand for already expensive natural gas-fired generation.[864] As demand for costly natural gas was increasing, supply of natural gas in the West was reduced, thereby further increasing the cost of natural gas. In addition to the El Paso pipeline rupture,[865] an inventory policy established by the California Public Utilities Commission directed utilities to reduce inventories of natural gas, resulting in further reductions of natural gas supplies in the region.[866] Likewise, the

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[861] Tr. 1949:10-23 (Hanser).

[862] Tr. 1960:13-1969:24 (Hanser).

[863] Ex. PNR-1 at 83-100.

[864] *Id.* at 115:1-120:14.

[865] Tr. 4113:3-4 (Hogan).

[866] Tr. 4114:3-11 (Hogan).

cost of NOx emission allowances required for burning natural gas in California increased to record levels.[867] Combined with hourly operating limits, the record level NOx emission allowance costs impeded the supply of low-cost natural gas-fired generation.[868] Numerous other supply constraints created a "perfect storm,"[869] including the reduced electricity output of qualifying facilities (QF) in California, reduced nuclear output in California, and maintenance outages for coal generation.[870] On the demand side, energy consumption was higher in each month of 2000 as compared to the corresponding month of any previous year (with one exception), and this pattern continued into 2001, with consumption in January and February exceeding the previous year's record.[871]

952. While these complex and variable market fundamentals of supply and demand are inextricably intertwined, Professor Hogan concluded that reduced hydro generation was the "single most important factor contributing directly and indirectly to the high power prices during the Western Power Crisis."[872] Mr. Hanser did not disagree with evidence presented to him during his cross-examination of historically low water conditions in the Pacific Northwest nor did he challenge Professor Hogan's factual findings with respect to other supply and demand market fundamentals impacting energy prices in the Pacific Northwest during the relevant period.[873]

953. Accordingly, Seattle has failed to demonstrate that a particular Respondent's contracts imposed an excessive burden on consumers or seriously harmed the public interest.

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[867] Ex. PNR-1 at 60:3-61:22.

[868] *Id. at* 122:4-134:23.

[869] *Id.* at 64:9.

[870] *Id.* at 101:7-105:20.

[871] *Id.* at 67:8-13.

[872] *Id.* at 83:4-7.

[873] Tr. 1988:7-1989:10 (Hanser).

### 4. Seattle's Claims Pursuant to Section 309 of the FPA

#### (a) Seattle Failed to Demonstrate That Any Respondent Engaged in a Specific Violation of a Substantive Provision of the FPA or Its Filed Tariff or Rate Schedule

954. In its April 5, 2013 Order on Rehearing, the Commission determined that it may order refunds, if appropriate, for transactions between January 1, 2000 and December 24, 2000 (Section 309 Period), under its FPA section 309 authority.[874] While Seattle initially conceded that its testimony pertaining to the Section 309 Period does not pertain to the Section 206 Period,[875] Seattle is apparently renewing its argument in its post-hearing briefs that the Order on Rehearing permits Seattle to submit claims for refunds under section 309 for the entire period of January 1, 2000 through June 20, 2001. However, this argument is moot given that Seattle has not demonstrated a basis for abrogating the subject contracts or for refunds for any period.

955. The Commission's Order explained that "refund claimants may attain the relief under FPA section 309 (if at all) by demonstrating a seller's specific violation of a substantive provision of the FPA or tariff, compliance with which the Commission can enforce by taking actions 'necessary and appropriate.'" [876] The *Mobile-Sierra* requirements established by the Commission for the Section 206 contracts apply with equal force for the Section 309 claims. The Commission reiterated in the Order on Rehearing that the focus of the inquiry to determine "whether a buyer can avoid application of the *Mobile-Sierra* public interest presumption, is individual contracts and the conduct of the seller as it relates to the formation of each contract."[877] The Commission noted that in attempting to overcome the *Mobile-Sierra* presumption,

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[874] Order on Rehearing at P 32.

[875] City of Seattle, Washington June 14, 2013 Answer in Opposition to the Indicated Respondents' Expedited Motion to Strike at 6 ("Mr. Hanser's [June 3, 2013] testimony asserts Section 309 claims only for the period January 1, 2000 through December 24, 2000"); *see also* Tr. 1901:23-25 (Hanser) ("Q. You did not do a benchmark analysis in your 206 testimony, either direct or rebuttal; is that correct? A. [Mr. Hanser]: No, I did not.").

[876] Order on Rehearing at P 32.

[877] *Id.* P 26.

"evidence that *specific contract rates* imposed an excessive burden on consumers" may be considered.[878]

956. Reliance on evidence consisting of high prices alone was firmly rejected.[879] Seattle acknowledges that in order to receive refunds under section 309 of the FPA, Seattle must demonstrate that Respondents violated either a substantive provision of the FPA or a filed tariff or rate schedule.[880] Nevertheless, Seattle does not address individual contracts and the conduct of the seller as it relates to the formation of each contract,[881] but rather focuses on allegations that prices charged in excess of its proffered Mitigated Market Clearing Price (MMCP) benchmark and Pivotal Unit Benchmark demonstrate that each Respondent acquired market power and then used that market power to charge Seattle rates that greatly exceeded the rates the Respondent could have charged if the market had been competitive. Seattle argues that by doing so, each Respondent violated its market-based tariff and section 205 of the FPA, which requires all prices for wholesale power to be "just and reasonable."[882] While not including itself in these "benchmark" analyses, Seattle acknowledges that it was also a market participant in the Pacific Northwest, charging similar market rates.[883]

957. Mr. Hanser asserts that each Respondent repeatedly violated its market-based tariff and section 205 of the FPA, which requires all prices for wholesale power to be "just and reasonable," by charging Seattle prices that were outside of a "zone of reasonableness determined by the seller's marginal cost of producing power."[884]

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[878] *Id.* P 27 (emphasis added) (quoting Order Granting Interlocutory Appeal at P 15).

[879] Order on Rehearing at P 30.

[880] *Id.* P 32.

[881] In fact, as with the data submitted for the Section 206 Period, Seattle's transaction spreadsheets lack the information necessary for identifying specific contracts and are based on an overly broad definition of "spot market." Ex. SCL-97 through SCL-105.

[882] 16 U.S.C. § 824d(a) (2012).

[883] Seattle states that it has agreed to voluntarily reduce any refund claims it makes against a Respondent by the amount of refunds Seattle would owe that Respondent if it were subject to the Commission's jurisdiction.

[884] Ex. SCL-110 at 34:22-24, 44:19-23.

Mr. Hanser uses two benchmarks to support his conclusions: (1) the Mitigated Market Clearing Price (MMCP) that the Commission used to calculate refunds in the California Refund Case and (2) the Pivotal Unit Benchmark, a surrogate for the marginal cost of a pivotal unit in the Pacific Northwest. According to Mr. Hanser, the MMCP Benchmark is a "price cap, calculated for each hour or ten-minute time interval, that approximates the marginal cost of the highest-cost generating unit that the [California] ISO dispatched to balance the market in real-time."[885] Mr. Hanser stated that the Pivotal Unit Benchmark "is designed to act as a surrogate for the marginal cost of the pivotal unit online across several balancing areas in the [Pacific Northwest] market."[886]

958. While there are deficiencies in using the MMCP or Pivotal Unit Benchmark as a basis to abrogate the subject contracts or to support refunds in this proceeding, Seattle's general argument that prices in the Pacific Northwest were "too high" is the same one that was rejected by the Commission in the Order on Rehearing: "Cal Parties' claims of uniformly higher prices amount to little more than a variation on claims of general market dysfunction, which have been previously rejected by the Supreme Court as a basis for overcoming *Mobile-Sierra*."[887]

**(b) The MMCP Benchmark is Specific to the Organized California Energy Markets and Not Appropriate for Use in the Pacific Northwest**

959. Seattle argues that the ability to charge prices in excess of the MMCP is clear evidence that Respondents acquired, possessed, and exercised market power. Seattle asserts that by acquiring market power and charging prices in excess of the MMCP, each Respondent engaged in unlawful activity by violating its market-based tariff, because that tariff was conditioned on the seller's lack of market power, and the "just and reasonable" requirement of section 205 of the FPA. Seattle's MMCP benchmark argument is fundamentally flawed however because the MMCP is a remedial relief construct specific to the organized California energy markets and is not an appropriate benchmark to address whether prices in the Pacific Northwest were just and reasonable.[888]

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[885] *Id.* at 38:3-6.

[886] *Id.* at 41:2-3.

[887] Order on Rehearing at P 30.

[888] As Respondents noted, the Commission's application of the MMCP to the CAISO's OOM purchases in the Pacific Northwest was based on a finding that the OOM purchases were inextricably tied to the purchases made in the organized California

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960. First, the context in which the MMCP was developed illustrates its inappropriateness as a measure of individual violations or unlawful actions even in the California market for which it was constructed, much less in the Pacific Northwest. In its December 15, 2000 Order Directing Remedies for California Wholesale Electric Markets, the Commission specifically stated that it had not made:

> … findings about whether particular rates charged by specific sellers during the summer of 2000 were unjust or unreasonable or that any individual sellers exercised or abused market power. Further, although the record has now been supplemented with additional information and evidence, nothing has been presented that would cause us to change the findings … There is not sufficient evidence on this record to find that particular sellers have exercised market power or that they have violated Commission-approved market rules.[889]

The Commission made clear that the primary focus of its analyses and remedies was on market design flaws and other negative events:

> … in the circumstances here, independent of any showing of a specific abuse of market power, a variety of factors have converged to drastically skew wholesale prices under certain conditions: significant over-reliance on spot markets which by their very nature can produce dramatic price increases when supply is tight; significant increases in load combined with lack of new facilities as well as reduced availability of supply from out of state; chronic underscheduling; and lack of demand responsiveness to price.[890]

961. Second, the MMCP is calculated for each hour using the marginal costs of the last unit dispatched to meet load in the CAISO's real-time market, as adjusted to reflect various inputs.[891] Seattle states that the MMCP represents prices that would have been

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markets. *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515-16 (2001) (CAISO's OOM purchases "are no different than purchases through its markets").

[889] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,294, at 61,998 (2001).

[890] *Id.*

[891] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120 (2001).

charged for wholesale energy had the market been competitive and not subject to manipulation. However, the MMCP does not include fixed costs, profit margin, marketer costs, or transmission costs.[892] In response to assertions by the sellers that using the MMCP as a benchmark with these deficiencies would often result in selling at a loss, Seattle simply responds that it is using the MMCP benchmark solely for the purpose of addressing the liability issue, and that Respondents can be given the opportunity to "true up" estimated data with actual data in the same way they were permitted to do in the California Refund Case.[893] This response ignores Seattle's own theory of liability, that each Respondent acquired market power and then used that market power to charge Seattle rates that greatly exceeded the rates the Respondent could have charged if the market had been competitive, and ignores Seattle's burden of proof to demonstrate seller specific violations of a substantive provision of the FPA or tariff.[894]

962. Finally, and most importantly, the Commission has rejected the use of the MMCP market-wide remedy adopted for the organized California markets as inappropriate for the bilateral Pacific Northwest spot market where "each seller receives only what a specific buyer agrees to pay for a given transaction and each buyer has the opportunity to negotiate a lower price."[895] The Commission's determination that the California and Pacific Northwest markets are fundamentally different for purposes of its consideration of the use of the MMCP as a remedial construct is fully explained in and supported by the record in the 2001 proceeding in which the Commission created the MMCP proxy. For example, that the MMCP was calculated for each hour using the marginal costs of the last unit dispatched to meet load in the CAISO's real-time market, as adjusted to reflect various inputs,[896] reflects the fact that the MMCP was based on marginal units in California, a state reliant on gas-fired resources, whereas the Pacific Northwest is much

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[892] Tr. 2091:9-2092:5 (Hanser). While Mr. Hanser later states that the MMCP's ten percent adder for risk premiums amounts to including a "reasonable profit," that was not its purpose, and there is insufficient evidence that ten percent is the appropriate value for what constitutes a reasonable profit in the subject market, particularly in the absence of seller specific marginal cost information.

[893] Tr. 2237:15-2238:1, 2243:23-2244:2, 2261:3-14 (Hanser).

[894] Order on Rehearing at P 32.

[895] Order on Remand at P 24.

[896] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120 (2001).

more reliant on hydroelectric resources, an important difference discussed more fully below.

963. Yet, Mr. Hanser acknowledged that he adopted the MMCP from that prior Commission proceeding for use in this proceeding without any independent analysis,[897] and apparently did so despite that fact that he was fully aware of fundamental differences in the subject markets. For example, Mr. Hanser acknowledged that "MMCPs were constructed based on what was considered to be a marginal unit in the California market" and were "not constructed based on the universe of units that were serving or could serve the Pacific Northwest."[898] In justifying different definitions of spot sale, Seattle also acknowledges fundamental differences between the bilateral market in the Pacific Northwest and the California organized markets, including: (1) different market structures; (2) the Pacific Northwest's reliance on hydroelectric generation;[899] and (3) the behavior of Load Serving Entities (LSEs) in the Pacific Northwest. Seattle explains that LSEs in the Pacific Northwest generally engage in a process of buying and selling power in transactions up to one month in duration in order to triangulate toward a precise balance of loads and resources when the hour of actual delivery occurs.[900] Seattle notes that the effects of changed water conditions can last up to one year, and therefore, the need for energy to balance load is not limited to a single hour or a single day. Thus, compared to market participants in California, participants in the Pacific Northwest "trade energy across much longer timeframes, with the standard products specifying delivery for multiple hours in each day, and products traded for a day, a month, a quarter, or a year (or longer) at a time."[901] Accordingly, the fact that MMCP was formulated as proxy for use in the organized California energy markets based on marginal units in California, a state reliant on gas-fired resources, whereas the Pacific Northwest is much more reliant on hydro resources, is a fundamental difference that informs the market behavior of participants in those markets in very different ways.[902]

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[897] Tr. 2015:16-18 (Hanser). *See also* Ex. SCL-115 at 6-7.

[898] Tr. 2019:15-2020:2 (Hanser).

[899] Ex. SCL-37 at 9:11-13.

[900] Ex. SCL-95 at 6:16-19; Ex. SCL-83. *See also* Ex. SCL-96.

[901] Ex. SCL-117 at 13:3-6.

[902] This analysis also demonstrates that Seattle's claim of undue discrimination based on a comparison of the prices Seattle paid with the MMCP price paid by the CAISO must fail because (1) Seattle and the CAISO are not similarly situated and (2) the

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964. Despite these fundamental market differences, Seattle points to Mr. Hanser's cointegration analysis to demand that the Commission treat the hydro intensive bilateral wholesale market in the Pacific Northwest and the natural gas-fired generation dependent California organized markets the same for purposes of energy pricing. However, Mr. Hanser has acknowledged that his cointegration analysis does not establish any *causal* link between the two markets.[903] Neither did he establish any clear relationship between these two fundamentally different markets other than to observe that prices often moved in the same direction at the same time. Thus, Mr. Hanser's cointegration analysis does nothing to address these fundamental market differences or to rebut the testimony of other experts in this proceeding, such as Mr. Cavicchi, that "MMCPs are applicable to the California organized wholesale markets for the purposes of the Commission California refund proceeding and have no relationship to the Pacific Northwest bilateral spot market."[904]

#### (c) The Pivotal Unit Benchmark Analysis is Fundamentally and Fatally Flawed

965. Seattle also argues that the ability to charge prices in excess of the Pivotal Unit Benchmark is clear evidence that Respondents acquired, possessed, and exercised market power. Seattle asserts that by acquiring market power and charging prices in excess of the Pivotal Unit Benchmark, each Respondent engaged in unlawful activity by violating its market-based tariff, because that tariff was conditioned on Respondent's lack of market power, as well as the "just and reasonable" requirement of section 205 of the FPA. Seattle's Pivotal Unit Benchmark argument is fundamentally flawed however because the analysis is deficient for the purpose of supporting such a finding.

966. Seattle's Pivotal Unit Benchmark analysis is fatally flawed from the outset because it ignores *individual* sellers' actual marginal costs.[905] The benchmark

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Respondents did not directly charge the CAISO the MMCP price. To rule otherwise would effectively establish a market-wide remedy for the Pacific Northwest, a remedy the Commission has continually rejected. Order on Remand at P 24 & n.56; Order on Rehearing at P 30.

[903] Tr. 2178:21-2179:16 (Hanser).

[904] Ex. JDG-1 at 17:5-10.

[905] Tr. 2016:1-7 (Hanser) (admitting that the benchmarks are "based on estimates of seller costs"); Tr. 2086:15-18 (Hanser) (admitting that he did not calculate Respondent's specific marginal cost).

calculations do not even take into consideration whether the cost of energy incurred by a Respondent exceeds the benchmark even before the Respondent may have resold it to Seattle.[906] The failure to confront individual marginal costs is a fatal error for every Respondent given the Respondent-specific nature of this case as, perhaps most dramatically, illustrated by reference to the power marketer Respondents, whose marginal costs were tied to the prices available in the market, not generation costs. Further, the marginal cost estimates utilized in the Pivotal Unit Benchmark do not include the recovery of fixed costs, a reasonable profit, opportunity costs, or transmission costs.[907] Nor does the Pivotal Unit Benchmark account for scarcity rents, which are the "additional increment above marginal running cost" by which competitive prices will rise in times of limited supply.[908]

967. In addition, the Pivotal Unit Benchmark suffers from other deficiencies that render it of limited usefulness in support of Seattle's attempt to abrogate the subject contracts or to obtain refunds. Under the Pivotal Unit Benchmark analysis, a maximum cost unit is identified in each and every hour.[909] Unlike the MMCP, the Pivotal Unit Benchmark

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[906] Tr. 2083:20-2084:7 ("PRESIDING JUDGE: Let me just ask a follow-up question about that. So I'm struggling with trying to understand the record with respect to the costs associated with this energy that was being sold by the City of Seattle and the Respondents. Is it possible that the cost of the energy to the City of Seattle exceeded the MMCP benchmark even before they resold it? THE WITNESS: Well, I mean, if it was -- I don't know. PRESIDING JUDGE: You didn't look at that, did you? THE WITNESS: No.").

[907] Mr. Hanser's Pivotal Unit Benchmark for units actually in the Pacific Northwest does not contain any adders and is determined solely by multiplying hourly plant heat rates by gas prices. Ex. SCL-110 at 41:1-9; Ex. SCL-115 at 21:18-23. Tr. 2125:18-20, 2031:13-15 (Hanser) (opportunity cost is not a component of marginal cost; the Pivotal Unit Benchmark does not account for seller's opportunity costs).

[908] Ex. SCL-111 at 95 ("This is not to say that competitive prices should never rise above the marginal running cost of generation. When supply is scarce relative to demand, competitive prices will rise to a level that reflects the value that the marginal consumer places on additional consumption. This additional increment above marginal running cost is referred to as the 'scarcity rent.'").

[909] As indicated in his Section 309 Rebuttal Testimony, Mr. Hanser changes to hourly transactional data as the basis for both the MMCP Benchmark barrier and his Pivotal Unit Benchmark barrier. Ex. SCL-115 at 18-21.

appears to be based on units that served the Pacific Northwest.[910] However, because the Pivotal Unit Benchmark is calculated by multiplying the hourly pivotal heat rate by the associated daily gas prices, it is limited to only one element−the value of fuel burned to produce a megawatt of electricity−of one type of generating facility−natural gas-fired generation.[911]

968. Moreover, the revised Pivotal Unit Benchmark analysis that Mr. Hanser submitted in his rebuttal testimony does not include *actual* natural gas costs. Instead, Mr. Hanser constructed his own natural gas cost to control for assumed price distortions.[912] In light of the fact that the transactions between buyers and sellers in the Pacific Northwest reflected *actual* natural gas costs, it is difficult to understand why Mr. Hanser used "reconstructed" natural gas costs in his analysis.[913]

969. In addition to using reconstructed natural gas costs in his revised Pivotal Unit Benchmark analysis, Mr. Hanser's Section 309 rebuttal testimony made another inexplicable change, excluding sales *below* the benchmarks from consideration while retaining sales *above* the benchmarks.[914] Including prices both above and below the benchmark is particularly important given that the contracts at issue may have spanned multiple hours with hourly pricing within a contract that may have been both above and below the benchmark. Examining *all* hours provides the most comprehensive analysis of individual contracts when examining if there is an "excessive burden." Furthermore, Seattle's own invoicing demonstrates that billing occurred on a monthly basis, not hour to hour. Thus, for the purpose of examining the burden on Seattle's consumers, netting

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[910] Tr. 2028:21-25 (Hanser).

[911] Ex. SCL-115 at 8:8-9 ("the Pivotal Unit benchmark is calculated by multiplying the hourly pivotal heat rate by the associated daily gas prices").

[912] Ex. SCL-115 at 7:12-22.

[913] Tr. 3349:1-12 (Cavicchi) ("PRESIDING JUDGE: All right. Why is that a more useful natural gas price to be used as the variable, in your opinion? THE WITNESS: Because it represents the actual gas market supply/demand conditions in California at the time. Whereas, if you take the gas price in Louisiana at the Henry Hub and you add a measure of historical transportation costs from a year where supply/demand conditions were different, so this would be 1999, you don't capture any of the variation in prices that existed due to transportation constraints between the Gulf region and California.").

[914] Tr. 2033:1-7 (Hanser).

prices above and below a benchmark is consistent with standard industry practice at the time.

970. The fact that Seattle waited until the rebuttal phase of its Section 309 filing to make these two significant unilateral changes to its Pivotal Unit Benchmark analysis is particularly suspect given the fact that when the Pivotal Unit Benchmark is calculated using the *actua*l natural gas costs, as presented in the initial Pivotal Unit Benchmark Mr. Hanser proposed, and is measured against Respondent sale prices both above and below the benchmarks, many of the "premiums" Mr. Hanser identifies in his analysis turn negative.[915] This result is graphically demonstrated by Exhibit JDG-11, which reflects that the total alleged "premiums" turn negative for Avista Energy, Constellation, El Paso, PPL, and PSCo, and are dramatically reduced as to the remaining Respondents. These findings are inconsistent with any claim of "excessive burden" and are inconsistent with Seattle's basic theory of liability that these sellers charged Seattle rates that greatly exceeded the rates they could have charged if the market had been competitive.

971. Further, even following Mr. Hanser's method and using reconstructed natural gas costs, the Respondents' sales to Seattle were priced below the Pivotal Unit Benchmark more than sixty percent of the time,[916] meaning that "more frequently than not the [Respondents'] charge was below the benchmark."[917] Again, these findings are inconsistent with any claim of "excessive burden" and are inconsistent with Seattle's basic theory of liability – "… that each Respondent acquired market power and then used that market power to charge Seattle rates that greatly exceeded the rates the Respondent could have charged if the market had been competitive in violation of each Respondent's market-based tariff and section 205 of the FPA, which requires all prices for wholesale power to be "just and reasonable."[918] As the Commission has observed, "just because market-based rates exceed cost-based rates during conditions of scarcity does not mean that such market-based rates become unjust or unreasonable during these periods"[919] and does not establish "… an absolute upper bound on anything that could look like a competitive market," as Mr. Hanser contends.[920]

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[915] *See* Ex. JDG-11

[916] Ex. SCL-115 at 8:19-20.

[917] Tr. 2066:19-21 (Hanser).

[918] 16 U.S.C. § 824d(a) (2012).

[919] *See Blumenthal*, 118 FERC ¶ 61,205, at P 32 (2007) (citing *Edison Mission Energy v. FERC*, 394 F.3d 964, 968–69 (D.C. Cir. 2005)) ("just because market-based

(continued…)

972. For the reasons discussed above, Seattle benchmark analyses, the sole basis for its claims, are inconsistent with any claim of excessive burden on consumers and are inconsistent with Seattle's basic theory of liability – that these sellers charged Seattle rates that greatly exceeded the rates they could have charged if the market had been competitive.

## VI. The California Parties Issue 1(A) Claims

973. Issue 1(A) addresses claims that an individual seller engaged in unlawful market activity, without a legitimate business reason, that directly affected the particular contract or contracts to which that seller was a party such that the presumption of just and reasonable rates applicable to bilateral contracts under the *Mobile-Sierra* standard would not apply. The California Parties have asserted Issue 1(A) claims against Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral) and TransCanada Energy Ltd. (TransCanada). The California Parties' claims concern transactions entered into by CERS between January 17, 2001 and June 20, 2001 (CERS Period). Initial briefs were filed by the parties on December 16, 2013,[921] and reply briefs were filed on January 28, 2014.[922]

### A. Summary of the Position of the Parties

#### 1. The California Parties Initial Brief

974. As described more fully below, the California Parties assert that they have demonstrated that Coral and TransCanada engaged in unlawful market activity that included fraud, duress, and bad faith; undue price discrimination; False Exports; and the exercise of market power. The California Parties contend that they have also shown that

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rates exceed cost-based rates during conditions of scarcity does not mean that such market-based rates become unjust or unreasonable during these periods). *See also New York Indep. Sys. Operator, Inc.*, 131 FERC ¶ 61,169, at P 81 (2010) (finding that in market-based regime in times of scarcity generators have the opportunity "to receive compensation above their marginal costs").

[920] Tr. 2186:5-7 (Hanser) (testifying that "the Pivotal Unit benchmark is, in some sense, an absolute upper bound on anything that could look like a competitive market").

[921] The California Parties filed errata to their initial brief.

[922] In their post-hearing briefs, Respondents provide substantially similar arguments on numerous issues. Those arguments are not repeated in each summary.

the extent of identified unlawful market activity altered the playing field for contract negotiations, directly affected the negotiation of specific bilateral contracts, and resulted in unjust and unreasonable rates.

### (a) Standard of Proof and Relevant Law

975. The California Parties state that section 206 of the FPA requires complainants to show, by a preponderance of the evidence,[923] that the existing rate is unjust and unreasonable.[924] The California Parties state that once the complainant has put forward a *prima facie* case, the burden shifts to the respondent to make an affirmative defense.[925] The California Parties assert that the "test for *prima facie* evidence is whether there are facts in evidence which if unanswered would justify men of ordinary reason and fairness in affirming the question which the plaintiff is bound to maintain."[926]

976. Next, the California Parties state that the spot market contracts at issue in this proceeding are subject to the *Mobile-Sierra* Doctrine.[927] Under the *Mobile-Sierra* Doctrine, the Commission presumes that the rate set out in a wholesale energy contract "meets the 'just and reasonable' requirement" imposed by the FPA unless the contract "seriously harms the public interest."[928] The California Parties state that the Supreme Court has clarified that this presumption applies only to "valid" contracts that were "freely negotiated."[929]

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[923] *Steadman v. SEC*, 450 U.S. 91, 102 (1981) (noting that Congress intended "expressly [to adopt] a preponderance-of-the-evidence standard").

[924] 16 U.S.C. § 824e(a) (2012).

[925] *Nantahala Power and Light Co.*, 19 FERC ¶ 61,152, at 61,276, *reh'g denied*, 20 FERC ¶ 61,430 (1982), *aff'd sub nom., Nantahala Power and Light Co. v. FERC*, 727 F.2d 1342 (4th Cir. 1984).

[926] *Id.*

[927] Order on Remand at P 20.

[928] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[929] *Id.* at 530, 548.

977. The California Parties state that in *Morgan Stanley*, the Supreme Court emphasized that the Commission "has ample authority to set aside a contract where there is unfair dealing at the contract formation stage."[930] Additionally, the California Parties assert that the Court held that "if the 'dysfunctional' market conditions under which the contract was formed were caused by illegal action of one of the parties, [the Commission] should not apply the *Mobile-Sierra* presumption."[931] The California Parties state that the Court concluded that "if it is clear that one party to a contract engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations, the Commission should not presume that the contract is just and reasonable."[932] Thus, where a causal connection is established between unlawful activity and the contract rate, the *Mobile-Sierra* presumption should not apply.[933]

**(b) Allegations of Fraud, Duress, and Bad Faith**

978. The California Parties assert that the *Mobile-Sierra* presumption does not apply where "there is … evidence of unfairness, bad faith, or duress in the original negotiation."[934] The California Parties argue that Respondents' sales to CERS were routinely tainted by duress, fraud, and bad faith because CERS was in a weak bargaining position and lacked reasonable alternatives in its purchasing. The California Parties contend that each Respondent was aware of this weak bargaining position and took advantage of it to obtain a disproportionate exchange of value.[935] The California Parties state that Mr. Taylor found fraud, duress, and bad faith in 119 of Coral's 156 contracts and 91 of TransCanada's 161 contracts with CERS.[936]

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[930] *Id.* at 547 (citing *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at 62,399-400 (2003)).

[931] *Id.*

[932] *Id.* at 554.

[933] *Id.* at 555.

[934] *Pub. Utils. Comm'n of Cal. v. Sellers of Long-Term Contracts to the Cal. Dep't of Water Res.*, 103 FERC ¶ 61,354, at P 62 (2003). *See also Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 410 (D.C. Cir. 2000).

[935] *See, e.g., CrossTalk Prods., Inc. v. Jacobson*, 76 Cal. Rptr. 2d 615, 623-24 (Cal. App. 1998).

[936] *See* Ex. CAT-408; Ex. CAT-412.

979. The California Parties note that duress, fraud, and bad faith have distinct legal meanings, but all involve exploitative behavior by the seller that negates any presumption that a contract was "freely negotiated."[937] The California Parties contend that Mr. Taylor correctly defined economic duress as an improper threat or other action that leaves a party with no reasonable alternative but to consent to a deal;[938] fraud as a practice that relies on deception or misrepresentation to cause a party to do something that it might otherwise not be willing to do;[939] and bad faith as a practice in which one party acts dishonestly, unfairly, or opportunistically to take advantage of another party.[940] The California Parties argue that the applicable legal definitions, based on Utah law,[941] for duress, fraud, and bad faith are substantially similar to those used by Mr. Taylor. The California Parties state that Mr. Taylor did not distinguish among the three practices, and there was no reason to do so.[942]

980. The California Parties assert that each Respondent understood that CERS needed to purchase its energy or face blackouts, and nonetheless, each Respondent collected a price that was far above the already distorted prevailing market price. The California Parties state that Respondents obtained margins from CERS that could never be obtained or sustained in a competitive market, and that Respondents did not obtain these excessive margins from other buyers in the market. The California Parties assert that contracts in which a Respondent engaged in duress, fraud, or bad faith had an immediate and harmful effect because these practices altered the playing field for contract negotiations and resulted in unjust and unreasonable rates.

981. Next, the California Parties contend that they presented unrefuted evidence that CERS was dealing from a position of weakness. The California Parties note that both Mr. Hart and Ms. Lee provided evidence that CERS operated under the continuing threat

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[937] *Morgan Stanley*, 554 U.S. at 530.

[938] Ex. CAT-041 at 39.

[939] *Id.*

[940] *Id.*

[941] All contracts at issue in this proceeding were entered into pursuant to the WSPP Agreement, which applies Utah law to the contracts. Ex. CAT-012 at 16; Ex. CAT-124 at 48.

[942] *See, e.g.*, Tr. 2660:6-2661:1 (Taylor).

of blackouts and that sellers took advantage of it.[943] The California Parties state that blackouts and ISO emergencies occurred throughout the CERS Period.[944] The California Parties assert that even Respondents' own witness, Mr. Tranen, conceded that blackouts had to be avoided at all costs.[945] The California Parties further contend that Respondents understood that the prospect of blackouts required CERS to pay whatever it took to acquire the last needed megawatt.[946]

982. The California Parties further note that in real-time, CERS was often required to purchase energy at COB due to congestion. The California Parties state that this drastically narrowed the field of potential sellers to an oligopolistic group, who could then extract higher prices.[947] The California Parties also argue that Respondents knew they had additional pricing leverage over CERS because other potential sellers refused to sell to CERS based on credit concerns.[948]

983. The California Parties contend that Respondents wrongly rely on selected trader tapes in which the CERS trader suggested the price, offered a higher price than demanded, or agreed to the price offered.[949] The California Parties aver that these tapes demonstrate that CERS was in a "must buy" situation, lacked reasonable alternatives, and that its traders had become resigned to paying very high prices to avoid blackouts. The California Parties state that Mr. Taylor explained that the trader tapes can only be correctly understood in the context of evolving market conditions in which CERS traders had become inured to paying very high prices in order to acquire necessary supplies.[950]

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[943] Ex. CAT-012 at 9-13; Ex. CAT-022 at 7-8.

[944] *See* Ex. CAT-041 at 30 n.49; Ex. CAT-289 at 110 n.223; Ex. CAT-134.

[945] Tr. 3980:8-23 (Tranen).

[946] *See, e.g.*, Ex. CAT-713 at 7:24-8:4; Tr. 4056:3-5 (Bowman); Ex.CAT-703 at 39.

[947] Tr. 2441:9-13, 2613:5-11 (Taylor).

[948] Ex. CAT-012 at 14.

[949] *See, e.g.*, Tr. 2394:23-2415:20 (Taylor); Ex. TRC-171 through TRC-177.

[950] Tr. 2932:4-25 (Taylor).

984. With respect to Mr. Taylor's analysis, the California Parties aver that Mr. Taylor took a very conservative approach and considered only those transactions in which objective evidence showed that the Respondent charged CERS a price that was far above the prevailing market price. Specifically, to be considered as a transaction that evidenced duress, fraud, or bad faith, the price charged to CERS had to be greater than the highest price recorded in *Power Markets Week* for COB or Mid-C, plus $75/MWh.[951] Mr. Taylor further narrowed the claim to exclude instances in which the Respondent was charging other purchasers even higher prices during the same hours and transactions in which some evidence suggested that the seller may not have been attempting to exploit CERS.[952]

985. Next, the California Parties assert that there is compelling evidence specific to each Respondent that demonstrates the contracts were the product of duress, fraud, or bad faith. The California Parties first note that Coral witness Ms. Bowman, who supervised traders during the CERS Period, stated that she had no ethical problem with being the cause of rolling blackouts.[953] The California Parties also argue that Coral's traders were managed by a former Enron trader who brought Enron's gaming strategies with him to Coral.[954] The California Parties allege that Coral's traders worked in an environment in which, as a matter of corporate policy, they were required to exploit CERS's weakened position in order to extract the highest possible margins.

986. The California Parties contend that Coral failed to justify the high prices that they charged CERS on the basis of calculated risk premiums.[955] The California Parties argue that Coral saw no ceiling on the price it should charge CERS, and Coral consistently tried to obtain the highest price that CERS was desperate enough to pay. Moreover, the California Parties state that Coral's minimum margin requirement virtually ensured that Coral's traders would insist on excessive prices.[956] The California Parties further argue

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[951] Ex. CAT-289 at 157. The California Parties note that the evidence that sellers were charging higher prices to CERS than other buyers confirms the accuracy of Mr. Taylor's assumption that the actual price in the Pacific Northwest was in the range reflected in the *Power Markets Week* index for Mid-C and COB.

[952] *See* Ex. CAT-161 at 70-71; Ex. CAT-289 at 98; Tr. 2474:5-2475:10 (Taylor).

[953] Ex. CAT-713 at 7:24-8:4; Tr. 4056:3-5 (Bowman).

[954] *See* Tr. 4022:9-18 (Bowman).

[955] Ex. SNA-1 at 14:20-23; Ex. SNA-9 at 32.

[956] Tr. 3981:4-3984:5 (Tranen).

that Mr. Taylor's False Export analysis demonstrates that Coral's sales to CERS were the result of fraud because Coral went out of its way to disguise the origin of power that it purchased in California and resold to CERS at COB.

987. The California Parties also state that there is specific documentary evidence of Coral's attempts to exploit CERS. This evidence includes (1) January 26, 2001 emails, which indicate that Coral sold CERS energy for $625/MWh that was purchased from the City of Glendale for $125/MWh;[957] (2) a February 2001 email from a Coral trader bragging that he was able to achieve margins in excess of $200/MWh at a time when the ISO was experiencing Stage 3 Emergency conditions;[958] (3) an April 22, 2001 email that states that Coral was raising its premiums at the same time that it was raising its credit limits to CERS;[959] (4) trader conversations demonstrating that Coral lined up potential energy purchases from third parties and then offered the energy to CERS at a mark-up of $200/MWh or more;[960] and (5) an April 2001 email which states that Coral traders should "be patient when dealing with CERS" and only execute sales that met the margin targets.[961] The California Parties argue that this evidence demonstrates that Coral was extracting high prices and margins by waiting until CERS could not meet its load.[962]

988. Next, the California Parties describe the evidence that relates specifically to TransCanada. The California Parties allege that TransCanada used its existing 50 MW long-term, firm transmission contract with BC Hydro to purchase low cost power out of the Power Pool of Alberta (PPoA), and then resold that energy to CERS at excessive margins.[963] The California Parties assert that during the CERS Period, power prices in PPoA averaged approximately $80/MWh, whereas TransCanada's average price to CERS was $322/MWh.[964] The California Parties further note that on one occasion,

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[957] Ex. CAT-104.

[958] Ex. CAT-041 at 81-82.

[959] Ex. CAT-104; Ex. CAT-137.

[960] *See, e.g.*, Ex. CAT-356 through CAT-367.

[961] Ex. CAT-137.

[962] Ex. CAT-289 at 94.

[963] Ex. TRC-77 at 22; Tr. 3585:1-3588:8 (Kunz).

[964] Tr. 2922:1-8 (Taylor); Ex. CAT-662; Ex. CAT-697; Ex. CAT-698. The California Parties note that power purchase costs were by far the largest costs that

(continued…)

TransCanada purchased energy from the PPoA for $66/MWh and resold it to CERS for $575/MWh, after refusing to lower the price to $550/MWh or even $570/MWh.[965] The California Parties argue that given the unconscionable margins that TransCanada was earning in its sales to CERS, it would be unreasonable to classify TransCanada's behavior as anything short of bad faith.

989. The California Parties further argue that TransCanada understood that as CERS became more desperate for energy, it would pay more for it. The California Parties assert that this is evidenced by the fact that all of TransCanada's sales to CERS were in the day-of market.[966] The California Parties state that Mr. Taylor demonstrated that TransCanada parked day-ahead energy with Pacific Northwest parties and resold that energy to CERS in real-time.[967]

990. With respect to TransCanada's claim that the PPoA was an extremely volatile market and that TransCanada committed to sell to CERS before it knew the PPoA price,[968] the California Parties contend that this defense is a "litigation-inspired" afterthought that has no basis in fact.

991. Lastly, the California Parties contend that TransCanada's argument that the profits merely reflect the high Pacific Northwest prices is already accounted for by Mr. Taylor's conservative screen, which uses actual market prices in the Pacific Northwest. The California Parties state that TransCanada obtained a profit margin that never could have been sustained in a truly competitive market, but Mr. Taylor's screen captured only those transactions that were priced at levels so far above the market that it was clear that TransCanada was engaging in bad faith.

### (c) Allegations of Undue Price Discrimination

992. The California Parties state that sections 205 and 206 of the FPA prohibit undue price discrimination.[969] The California Parties assert that undue price discrimination also

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TransCanada incurred in selling energy to CERS. *See* Tr. 2929:15-2931:12 (Taylor).

[965] *See* Tr. 2915:7-2925:25 (Taylor); Ex. CAT-659; Ex. TRC-196; Ex. TRC-197.

[966] Ex. CAT-030.

[967] Ex. CAT-041 at 84-85; Ex. CAT-117.

[968] Tr. 3542:23-3548:7 (Kunz).

[969] *See* 16 U.S.C. §§ 824d(b), 824e(a) (2012).

constitutes an independent basis for overcoming the *Mobile-Sierra* presumption.[970] The California Parties state TransCanada and Coral unduly discriminated against CERS. The California Parties argue that undue price discrimination was possible during the CERS Period because a limited set of sellers knew that CERS had to buy large amounts of energy in real-time.[971]

993. The California Parties contend that the defenses that undue price discrimination was (1) economically rational or (2) impossible because the market would discipline a seller that tried to discriminate ignore the market dysfunction during the CERS Period, the limited number of sellers to CERS, and the reality that time only moves in one direction. The California Parties note that in real-time, CERS was often purchasing less than an hour, and sometimes only minutes, before it needed the energy to flow. The California Parties state that the highest premiums generally occurred early in the CERS Period when CERS was the most vulnerable and markets were especially dysfunctional.[972]

994. The California Parties state that Dr. Fox-Penner employed a conservative methodology that examined the transactions on an hour-by-hour basis and found that approximately thirty percent of the hourly sales by Respondents to CERS were at prices: (1) significantly higher than directly comparable sales to other purchasers during the same period or (2) significantly outside, by three or six standard deviations, the average distribution of prices to other purchasers. Moreover, the California Parties state that Dr. Fox-Penner conducted an econometric regression analysis that validated his conclusions.[973]

995. The California Parties note that Dr. Fox-Penner described the price discrimination by Respondents as "a systematic and substantial pattern that's not explained by cost differences."[974] The California Parties state that Dr. Fox-Penner's analysis is compelling proof of undue price discrimination because it established that CERS was treated differently from other purchasers in Pacific Northwest markets without a reasonable or supportable cost justification.

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[970] *Town of Norwood v. FERC*, 587 F.2d 1306, 1311 (D.C. Cir. 1978).

[971] Tr. 3700:19-21 (Kunz). *See also* Ex. TRC-234.

[972] Ex. CAT-161 at 13, Table II-1.

[973] Ex. CAT-413 at 35-41.

[974] Tr. 1399:5-22 (Fox-Penner).

996. Furthermore, the California Parties contend that the excessive prices that resulted from Respondents' undue price discrimination directly harmed California consumers. The California Parties state that as a result of this discrimination, consumers paid more in energy costs. The California Parties also argue that the undue price discrimination further contributed to the overall market dysfunction and excessive prices experienced during the CERS Period.

997. Next, the California Parties discuss Dr. Fox-Penner's methodology in more detail. The California Parties state that to evaluate price discrimination, Dr. Fox-Penner compared the prices that Respondents charged CERS to the prices that Respondents charged other buyers for power delivered at the same time and location.[975] Although in some instances exact matching transactions were available, other times, Dr. Fox-Penner had to adjust the price because of locational differences.[976] Dr. Fox-Penner then compared the weighted average CERS price to the weighted average price that Respondents charged to non-CERS buyers, and referred to this difference as the "CERS Premium."[977] In comparing the specific hourly deliveries, the California Parties state that Dr. Fox-Penner used a $50/MWh threshold in order to account for hourly price dispersion and potential cost differences, such differences in transaction size and credit premiums. The California Parties argue that the $50/MWh threshold is extremely conservative.

998. For hours in which a Respondent sold only to CERS, the California Parties state that Dr. Fox-Penner compared these prices with the other transactions at the same location.[978] Dr. Fox-Penner computed the mean and standard deviation of the transaction prices in that day and used statistical tests to determine the probability that the CERS price was within the expected range of prices. Dr. Fox-Penner used a threshold of three to six standard deviations above the mean and determined that many of the prices that Respondents charged to CERS were well outside the boundaries of normal market price dispersion and therefore, reflected undue price discrimination.[979]

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[975] Ex. CAT-161 at 5.

[976] In these cases, Dr. Fox-Penner added the published tariff cost of firm transmission and line losses between the two delivery points. Ex. CAT-413 at 20.

[977] Tr. 1328:13-1329:3 (Fox-Penner).

[978] To conduct this analysis, Dr. Fox-Penner used the transaction data from Docket No. PA02-2.

[979] Ex. CAT-161 at 75.

999. Additionally, Dr. Fox-Penner reviewed each hour of Respondents' transactions with CERS to determine if there were additional hours that reflected an extended pattern of price discrimination that did not meet the benchmarks described above.[980] The California Parties state that this additional examination revealed that Respondents' sales to CERS were often consistent across peak or off-peak periods,[981] and that Dr. Fox-Penner concluded that these transactions were unduly discriminatory when a similar transaction in a nearby hour met the price discrimination screens.[982]

1000. Next, the California Parties review the evidence of price discrimination related to each individual Respondent. With respect to Coral, Dr. Fox-Penner concluded that Coral's prices to CERS were unduly discriminatory in 595 hours during the CERS Period, with an average premium of $211/MWh.[983] The California Parties contend that Mr. Tranen failed to demonstrate that Coral's prices were justified because the sales to CERS were "back-to-back" transactions, where each sale to CERS could be tied to a particular Coral purchase. The California Parties argue that Mr. Tranen's analysis demonstrates that Coral consistently singled out CERS with an average mark-up that was nearly $100/MWh more than the mark-ups to other buyers in similar "back-to-back" transactions. Additionally, the California Parties assert that Mr. Tranen's "back-to-back" analysis fails to account for upstream transactions that involved the same energy that was ultimately sold to CERS.[984] The California Parties state that when all the mark-ups in the upstream transactions are taken into account, the actual total mark-up to Coral was revealed to be well in excess of the mark-up for the final transactions that had been shown in Mr. Tranen's analysis.[985]

1001. Lastly, the California Parties state that Dr. Fox-Penner found twenty-six hours where TransCanada unduly discriminated in its sales to CERS. The California Parties state that there were relatively few hours in which there were comparable transactions to non-CERS purchasers because virtually all of TransCanada's sales during the CERS

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[980] *See* Tr. 1311:16-1312:6, 1347:19-1348:6, 1453:23-1455:1, 1466:21-1467:5 (Fox-Penner).

[981] Tr. 1470:8-23 (Fox-Penner).

[982] Ex. CAT-413 at 29.

[983] Ex. CAT-163 at 19.

[984] Tr. 2969:11-2995:16 (Taylor); Ex. CAT-668 through CAT-675.

[985] *See* Ex. CAT-670; Ex. CAT-675.

Period were to CERS.[986] The California Parties state that in the two months in which Dr. Fox-Penner was able to quantify instances of TransCanada's undue discrimination, its average premium was $210/MWh in February 2001 and $14/MWh in May 2001.[987]

**(d) Allegations of False Export**

1002. The California Parties contend that Coral engaged in False Export sales to CERS. A False Export consists of a supplier purchasing power generated within the ISO, filing a day-ahead or day-of schedule showing a fictitious "export" of power, and then selling that energy to CERS in real-time, falsely representing that the energy was coming from outside the ISO.[988] The California Parties argue that False Exports allowed sellers to divert power generated within the ISO away from the day-ahead market and take advantage of CERS's weak bargaining position during real-time.[989]

1003. The California Parties argue that a False Export transaction consists of two instances of fraudulent conduct: (1) a false indication to the ISO that energy generated in California was being exported outside of the ISO and (2) a false indication to CERS that the energy that it was purchasing came from the Pacific Northwest. The California Parties contend that False Export transactions, like the similar Enron False Import scheme that the Commission previously condemned,[990] violated the ISO Tariff's Market Monitoring and Information Protocol (MMIP).[991] The California Parties further argue that False Export transactions violated the ISO Tariff provisions concerning operating requirements, scheduling, and bidding. The California Parties assert that there is an implicit requirement that schedules filed with the ISO would not be intentionally inaccurate or misleading.[992] Lastly, the California Parties assert that False Exports

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[986] *See, e.g.*, Ex. CAT-702.

[987] Ex. CAT-161 at 13, Table II-1.

[988] Ex. CAT-041 at 88.

[989] *Id.* at 87-88.

[990] *See Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at P 25 (2003).

[991] *See* Ex. CAT-147 at 152-70.

[992] Ex. CAT-041 at 93.

violated the seller's market-based rate tariff because the sale to CERS was based on a fraudulent representation.[993]

1004. The California Parties contend that False Exports were harmful. The California Parties argue that prior to the CERS Period, False Exports helped lead to the financial collapse of the California IOUs. During the CERS Period, the California Parties assert that by shifting supply from the day-ahead to real-time, Respondents were able to strengthen their bargaining power over CERS. Additionally, the California Parties assert that the False Export transactions created misleading shortage signals within the day-ahead energy market.

1005. Next, the California Parties describe Mr. Taylor's False Export analysis. The California Parties state that Mr. Taylor employed a single-party False Export screen that examined whether in a given hour a supplier: (1) submitted a day-ahead or day-of export schedule to the ISO that was not a wheel-through or circulation transaction and (2) made a real-time sale to CERS in the same hour.

1006. The California Parties assert that Mr. Taylor found that Coral engaged in False Exports in over 139 hours for a total of 2,798 MWh. The California Parties state that Coral described the False Export transactions as innocent statistical "noise."[994] However, the California Parties aver that Mr. Taylor explained that in a competitive market, you would expect the economics to favor either export out or import in, not both in the same hour.[995] Therefore, the California Parties argue that one would expect the overlap between a party's exports and imports to be far less than the expected overlap between sets of random, unrelated transactions.

1007. The California Parties also contend that Coral improperly alleged that it did not supply CERS from a portfolio of energy, but rather from specific "back-to-back" transactions.[996] As discussed more fully below, the California Parties argue that many of the alleged "back-to-back" transactions actually involved upstream transactions that were not considered by Coral.

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[993] *Enron Power Mktg., Inc.*, 103 FERC ¶ 61,343, at P 52 (2003); Ex. CAT-041 at 93.

[994] Tr. 2582:11 (Coral Counsel). Coral argued that there will be random overlap between the export and import transactions.

[995] Tr. 2580:6-2582:3 (Taylor).

[996] Ex. SNA-9 at 11-12.

### (e) Allegations of Selling Non-Firm Energy as Firm

1008. In their post-hearing briefs, the California Parties only alleged that TransAlta engaged in selling non-firm energy as firm. Because the California Parties and TransAlta subsequently settled their claims, there are no allegations against any of the remaining Respondents.

### (f) Allegations that Respondents Exercised Market Power

1009. The California Parties assert that the exercise of market power undermined the effective functioning of the ISO markets and violated the MMIP.[997] The California Parties state that Respondents exercised market power during the CERS Period or took advantage of market power circumstances that existed by engaging in price discrimination. The California Parties contend that the exercise of market power had both reliability and price impacts.

1010. The California Parties state that Dr. Reynolds' econometric and statistical tests demonstrated that market power existed and that larger sellers exercised market power and charged higher prices to CERS.[998] The California Parties note that Dr. Reynolds' CERS Regression analysis shows that Respondents' day-of prices increased significantly with the quantity sold.[999] Additionally, Dr. Reynolds demonstrated that the prices that Respondents charged CERS for day-of power were higher when there were fewer sellers.[1000] The California Parties note that the regressions supported Dr. Reynolds' prediction that large suppliers could have obtained and exercised market power during the CERS Period by accumulating supplies in both the day-ahead and day-of markets and selling the accumulated supplies to CERS in the day-of market.

1011. The California Parties assert that Mr. Taylor and Dr. Fox-Penner supported Dr. Reynolds' conclusions. Mr. Taylor found that there was "voluminous evidence that market power played a role in the prices paid by CERS" and that the potential for

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[997] Ex. CAT-147 at 158. *See also* Ex. CAT-041 at 92.

[998] Ex. CAT-264 at 6-20; Ex. CAT-266; Ex. CAT-631 at 5-25, 33-42.

[999] Ex. CAT-264 at 10-12; Ex. CAT-631 at 5-25, 35-36.

[1000] Ex. CAT-264 at 9-12; Ex. CAT-266; Ex. CAT-631 at 5-7. *See also* Ex. CAT-413 at 52-53.

blackouts gave Respondents market power with respect to CERS.[1001] Dr. Fox-Penner testified that "[t]he conditions for price discrimination to occur – market power and impediments to resale – were present during the CERS Period,"[1002] and that Respondents "exercised a particular form of market power, which is called price discrimination."[1003] Further, Dr. Fox-Penner explained how the overall credit situation constrained supply and enhanced seller market power,[1004] and that Respondents themselves acknowledged that larger single purchases could make them vulnerable to the exercise of market power by other sellers in the Pacific Northwest.[1005]

1012. Next, the California Parties state that Respondents failed to refute the evidence of market power. The California Parties contend that Dr. Reynolds' rebuttal testimony demonstrated that Trial Staff's critiques of his analysis were misguided or inconsequential.[1006] With respect to the criticism that Dr. Reynolds' CERS Regressions overlooked causal links between price and quantity,[1007] the California Parties contend that no witness substantively addressed this issue. Moreover, the California Parties argue that the criticism is incorrect because (1) to the extent that any causation issue existed, it would actually result in the exercise of market power being understated;[1008] (2) the criticism overlooks that, even if price influenced each firm's quantity, the effect would have been to depress the measured effect of quantity in Dr. Reynolds' CERS

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[1001] Ex. CAT-289 at 20, 109-10. *See also* Ex. CAT-041 at 12; Ex. CAT-289 at 6, 90-91.

[1002] Ex. CAT-413 at 5.

[1003] Tr. 1308:25-1309:1 (Fox-Penner); *see also* Ex. CAT-413 at 7-8.

[1004] Ex. CAT-413 at 8-10.

[1005] *Id.* at 53-54.

[1006] Ex. CAT-264 at 6-13, 15-20; Ex. CAT-266; Ex. CAT-631 at 3-7, 10-15, 21-29, 31-36, 38-42; Ex. CAT-632 at 3-4.

[1007] Ex. S-13 at 37-38.

[1008] Ex. CAT-631 at 10-11.

Regressions;[1009] and (3) no witness actually tried to demonstrate that this variable issue affected any indication of market power by larger sellers.[1010]

1013. Next, the California Parties address Dr. Savitski's critiques regarding emergency stage variables, hourly observations, and product market definition. The California Parties first note that Dr. Savitski failed to analyze the content of Dr. Reynolds' market power analyses and made no attempt to produce any of his own empirical analyses to examine or challenge Dr. Reynolds' market power findings.[1011] The California Parties state that Dr. Savitski admitted that he never reviewed Dr. Reynolds' workpapers, did not recall reviewing any of the memos underlying Dr. Reynolds' analyses, and did not try to rerun or validate any of Dr. Reynolds' regressions.[1012] Moreover, the California Parties note that Dr. Savitski admitted that he has never performed a market power analysis in the electric sector and has not performed a regression analysis during his tenure at the Commission.[1013]

1014. With respect to Dr. Savitski's criticism regarding emergency stage variables, the California Parties state that Dr. Reynolds testified that he included variables in his regression analysis to control for the independent effects of ISO Emergencies, and that Dr. Savitski was simply incorrect that emergency stage results were inconsistent with the exercise of market power.[1014] The California Parties argue that Dr. Savitski's criticism of using hourly observations is unclear because Dr. Savitski did not propose an alternative unit of observation and the statistical techniques that Dr. Reynolds used in his analyses are well accepted.[1015] Lastly, the California Parties note that Dr. Reynolds testified that Dr. Savitski's product market criticisms were inaccurate, and that the "most relevant evidence of the scope of the relevant product and geographic markets lies in the direct evidence of competitive effects."[1016] The California Parties state that if "direct evidence

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[1009] *Id.* at 4, 5, 10-11.

[1010] *Id.* at 12-14.

[1011] *Id.* at 6.

[1012] Tr. 4265:1-4266:23 (Savitski).

[1013] Tr. 4263:15-4264:9 (Savitski).

[1014] Ex. CAT-631 at 23-24.

[1015] *Id.* at 24-25.

[1016] *Id.* at 26-27.

of harm to competition" is present, then determining market shares and defining the market is unnecessary.[1017]

1015. The California Parties also contend that Coral's claim that its higher prices were not related to market power is unsupported.[1018] The California Parties state that Dr. Reynolds performed additional statistical tests that controlled for peak and off-peak differences and confirmed that Coral realized higher prices for larger quantities sold.

1016. Additionally, the California Parties state that Professor Hogan's claim that the California Parties did not analyze market power is false. The California Parties assert that Dr. Reynolds demonstrated that day-of prices charged to CERS increased due to the exercise of market power.[1019] The California Parties further note that Professor Hogan admitted that he did not focus on Dr. Reynolds' testimony.[1020]

1017. The California Parties also contend that criticisms that Dr. Reynolds did not use certain Commission market power screens are irrelevant. The California Parties assert that courts and antitrust agencies have agreed that "direct evidence is sufficient – on its own – to show market power."[1021] Further, the California Parties state that the Commission stopped using the hub-and-spoke test in November 2001, noting that it "no longer adequately protects customers against generation market power."[1022] Lastly, the California Parties aver that the tests that Dr. Reynolds advocated to measure market power are "sound and robust" and are "based on the actual transactions during the CERS Period."[1023]

1018. Lastly, the California Parties address claims that CERS exercised monopsony power or had a competitive advantage. The California Parties assert that Dr. Reynolds and Mr. Taylor demonstrated that CERS could not have exercised monopsony power in

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[1017] *Id.* at 27.

[1018] Ex. SNA-9 at 36.

[1019] Ex. CAT-264 at 17-18; Ex. CAT-631 at 38.

[1020] Ex. CAT-632 at 8. *See also* Ex. CAT-631 at 38 n.80.

[1021] Ex. CAT-631 at 40.

[1022] *Id.*

[1023] *Id.* at 41.

the circumstances it faced.[1024] Mr. Taylor noted that, beyond pointing out that CERS was the largest buyer in the market, Respondents made no attempt whatsoever to show that CERS exercised any monopsony power.[1025] Mr. Taylor also described how "[w]hen CERS did try to hold the line on prices, it could not do so without threatening the reliability of the California power system."[1026]

1019. With respect to claims that CERS had a competitive advantage because of access to non-public information through CERS employees that were stationed on the ISO control room floor, the California Parties assert that this claim is unfounded. The California Parties note that Mr. McIntosh, the Director of Grid Operations for the ISO, testified that having CERS personnel on the ISO control room floor was an operational necessity.[1027] Moreover, Mr. McIntosh and Mr. Alaywan testified that CERS personnel only had information about how much energy the ISO needed to buy in any given hour to balance the market.[1028] Mr. Alaywan testified that CERS received "highly aggregated information concerning the ISO's planned purchases in advance of the hour, and only during the period April 7 - June 25, [2001]."[1029] The California Parties state that access to confidential information regarding grid operations and market information was highly restricted and the ISO took steps to insulate CERS personnel from confidential information.[1030] The California Parties note that neither Mr. McIntosh nor Mr. Alaywan were aware of any instance in which CERS personnel gained access to proprietary information during the CERS Period.[1031]

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[1024] Ex. CAT-264 at 18-20; Ex. CAT-631 at 3-7, 10-15, 21-29, 31-36, 38- 42; Ex. CAT-289 at 107-08, 121; Tr. 2531:18-2532:5 (Taylor). *See also* Ex. CAT-285 at 10-11; Ex. CAT-272 at 1.

[1025] Ex. CAT-289 at 107.

[1026] *Id.* at 109-10. *See also* Ex. CAT-384 through CAT-389; Ex. CAT-161 at 8.

[1027] Ex. CAT-641 at 4-8.

[1028] *Id.* at 8; Ex. CAT-643 at 6-7, 9.

[1029] Ex. CAT-643 at 11.

[1030] Ex. CAT-641 at 8-11; Ex. CAT-643 at 4-5.

[1031] Ex. CAT-641 at 10-11; Ex. CAT-643 at 2, 6-9; Tr. 2304:8-12 (Alaywan); Tr. 2349:4-11 (McIntosh).

### (g) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1020. The California Parties state that in *Morgan Stanley*, the Supreme Court made clear that the *Mobile-Sierra* presumption applies only to valid contracts that were freely negotiated.[1032] The Court emphasized that the Commission "has ample authority to set aside a contract where there is unfair dealing at the contract formation stage" [1033] and concluded that "if it is clear that one party to a contract engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations, the Commission should not presume that the contract is just and reasonable."[1034] The California Parties state that where a causal connection is established "between unlawful activity and the contract rate … the *Mobile-Sierra* presumption should not apply."[1035]

1021. As stated above, the California Parties assert that they demonstrated that each Respondent engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations. The California Parties state that this directly affected the negotiation of specific bilateral contracts between Respondents and CERS, resulting in unjust and unreasonable rates.

1022. The following table summarizes the allegations of unlawful activity made by the California Parties against Coral[1036] and TransCanada:[1037]

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[1032] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530, 548 (2008).

[1033] *Id.* at 547.

[1034] *Id.* at 554.

[1035] *Id.* at 555.

[1036] The California Parties and Coral reached a stipulation concerning the vast majority of the transactional details for Coral's sales to CERS during the CERS Period. Shell Energy North America (US), L.P. and the California Parties August 12, 2013 Joint Stipulation Concerning Transaction Information.

[1037] The California Parties and TransCanada have not reached a stipulation concerning transactional details for TransCanada's sales to CERS during the CERS Period. The California Parties' data regarding TransCanada's sales to CERS were submitted in Ex. CAT-030.

| | **Coral**[1038] | **TransCanada**[1039] |
|---|---|---|
| **Total Number of Contracts with CERS** | 156 | 161 |
| **Total Number of Contracts Challenged** | 133 | 96 |
| **Duress, Fraud, Bad Faith** | 119 | 91 |
| **Undue Price Discrimination** | 101 | 4 |
| **False Export** | 36 | 0 |

### (h) Legitimate Business Behavior by Respondents

1023. The California Parties state that none of the Respondents' proffered justifications explain the extraordinarily high prices charged to CERS. The California Parties assert that Respondents' actions were not "consistent with appropriate behavior in a competitive market."[1040]

1024. First, the California Parties address Respondents' claim that market fundamentals explain the high prices in the Pacific Northwest.[1041] The California Parties assert that fundamentals could not explain the high prices. The California Parties aver that Professor Hogan failed to incorporate into his discussion years of evidence – and Commission findings – showing that the market was not workably competitive and sellers engaged in "withholding, gas price manipulation, Enron-style gaming, and … tens of thousands of tariff violations."[1042] The California Parties note that Professor Hogan's

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[1038] California Parties Initial Br. at 89-90. However, Appendix B to the California Parties' Initial Brief contains slightly different figures for both Coral and TransCanada.

[1039] *Id.*

[1040] Order on Remand at P 22 n.52.

[1041] Ex. PNR-1 at 64.

[1042] Ex. CAT-536 at 8-11. *See also* Ex. CAT-041 at 109; Ex. CAT-045 at 57-59; Ex. CAT-289 at 10-13; Ex. CAT-537 through CAT-540; Ex. CAT-542 through CAT-547.

testimony on the market fundamentals has remained static for the past decade[1043] and Professor Hogan admitted that he did not take into account the specific facts of this proceeding, review any documents from TransCanada or Coral, or listen to any trader tapes.[1044]

1025. Moreover, the California Parties contend that Professor Hogan ignored key facts. For example, the limited hydro resources did not occur until the fall of 2000, after the price spikes in May and June 2000 when the crisis began.[1045] The California Parties also argue that Professor Hogan failed to incorporate into his analysis the discretionary nature of hydro availability and that reductions in hydro supply were the result of strategic decision-making.[1046]

1026. The California Parties also state that Professor Hogan analyzed events beyond the time period at issue and events that occurred outside the United States.[1047] Moreover, the California Parties note that Professor Hogan failed to justify his attempt to conflate the international credit risks of Argentina's economy with sales to CERS.[1048]

1027. Lastly, the California Parties argue that even if market fundamentals did impact prices, that would not negate the California Parties' evidence of widespread fraud and energy market manipulation. The California Parties note that Mr. Taylor and Dr. Fox-Penner acknowledged that scarcity was a factor in the prices paid in the Pacific Northwest,[1049] but that this scarcity actually "set the stage for the exercise of market power," and played "a supporting role, not the leading role," in high CERS prices.[1050] Moreover, the California Parties assert that market fundamentals are irrelevant to the

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[1043] Ex. CAT-289 at 9-10 & n.3; Tr. 4104:14-4108:20 (Hogan).

[1044] Tr. 4083:2-4084:18 (Hogan).

[1045] Ex. CAT-289 at 14-15.

[1046] *Id.* at 14-18.

[1047] *See* Tr. 4113:22-23, 4118:19-25 (Hogan).

[1048] Ex. PNR-1 at 19, 150-52; Tr. 4087:16-4088:17 (Hogan).

[1049] Ex. CAT-289 at 21-22; Ex. CAT-413 at 12-14.

[1050] Ex. CAT-289 at 21-22. *See also* Tr. 2543:12-2544:1 (Taylor).

extent that CERS paid unduly discriminatory prices because adverse fundamentals would have applied to all purchasers at the time.[1051]

1028. Second, the California Parties address the Respondents' claims that they lacked market power. The California Parties note that this defense is "neither consistent with available evidence, nor [] dispositive because market power is not required for profitable manipulative schemes."[1052] Moreover, the California Parties aver that the undue price discrimination that occurred during the CERS Period is indicative of the existence of market power.

1029. Third, the California Parties respond to defenses that the prices were justified due to credit and litigation risks. The California Parties note that Dr. Fox-Penner was the only witness to perform an assessment of Respondents' prices and to make a determination of the appropriate adder for any risks in dealing with CERS.[1053] The California Parties state that Respondents performed no quantitative analysis, provided no documents supporting the premiums they charged, and could not substantiate what would have constituted appropriate risk premiums.[1054]

1030. The California Parties state that Dr. Fox-Penner concluded that even under the most conservative of assumptions, the calculated premium for a $500/MWh sale would be $0.46/MWh, or about 1.06 percent.[1055] Dr. Fox-Penner further noted that, even if he assumed that CERS was as risky as a "junk bond," it would "not justify more than a few cents of risk premium."[1056] The California Parties state that Dr. Fox-Penner's calculated credit premium was well below the ten percent credit adder to the MMCP.[1057] The

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[1051] Ex. CAT-413 at 12-14.

[1052] Ex. CAT-289 at 6, 19-21 (citing, *e.g.*, *Deutsche Bank Energy Trading, LLC*, 142 FERC ¶ 61,056 (2013); *Barclays Bank PLC*, 141 FERC ¶ 61,084 (2012); *Brian Hunter*, 135 FERC ¶ 61,054 (2011)).

[1053] Ex. CAT-161 at 15-58.

[1054] Ex. CAT-413 at 42; Tr. 4086:15-4090:8 (Hogan); Tr. 4034:20-4037:18 (Bowman).

[1055] Ex. CAT-161 at 26. *See also* Tr. 1551:22-1552:18 (Fox-Penner).

[1056] Ex. CAT-161 at 24-29.

[1057] Ex. CAT-413 at 43 (citing *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418 ,at 62,564 (2001)).

California Parties state that because CERS never defaulted on payment and had a shorter time period of outstanding credit risk, Dr. Fox-Penner concluded that the appropriate risk premium for CERS would be substantially less than ten percent.[1058]

1031. Additionally, the California Parties argue that Respondents managed credit risk by imposing credit limits and in some cases raised those credit limits during the CERS Period in order to take advantage of high margins.[1059] The California Parties note that this is "precisely the opposite relationship one would expect if high mark-ups reflected an increased default risk premium."[1060]

1032. The California Parties also state that Mr. Taylor found that the evidence did not support arguments that perceived risk justified the prices that CERS paid.[1061] Mr. Taylor found that claims of credit risk were unfounded, squarely at odds with Respondents' "fundamentals" arguments, and unsupported by record evidence.[1062] The California Parties note that contemporaneous documents and trader tapes demonstrate that Respondents sought the highest prices possible, regardless of CERS's credit risk.[1063]

1033. With respect to litigation risk, the California Parties contend that this argument should be summarily rejected. The California Parties note that the subject sales were in Commission-jurisdictional markets, which require rates to be just and reasonable.[1064] The California Parties state that if a rate was excessive, and therefore not just and reasonable, then the Commission is required to determine the just and reasonable rate to be charged.[1065] Thus, sellers will be assured a just and reasonable rate.[1066]

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[1058] Ex. CAT-413 at 44.

[1059] *See, e.g.*, *id.* at 47-48.

[1060] *Id.* at 47.

[1061] Ex. CAT-041 at 103-08.

[1062] Ex. CAT-289 at 5-6, 20-21, 33-34, 89-96, 115-16.

[1063] *Id.* at 89-96.

[1064] *See* 16 U.S.C. § 824d(a) (2012).

[1065] *See* 16 U.S.C. § 824e(a) (2012).

[1066] *See, e.g.*, *Ariz. Pub. Serv. Co.*, 144 FERC ¶ 61,200, at P 16 (2013). *See also* Ex. CAT-413 at 50-51; Ex. CAT-289 at 95.

1034. Fourth, Respondents and Trial Staff argued that Respondents had no obligation to sell to CERS and that any sales that Respondents did make to CERS helped California.[1067] The California Parties argue that Respondents harmed California consumers, businesses, and government by charging excessive, unjust, and unreasonable rates. Further, the California Parties state that Respondents followed a pattern of waiting to sell energy to CERS until CERS was "desperate" in order to reap the highest possible profits.[1068] The California Parties argue that this behavior, and the resulting prices, compromised "[t]he ability of the entire system to provide electricity reliably."[1069]

1035. Fifth, the California Parties respond to claims that Respondents behavior was legitimate market arbitrage. The California Parties assert that Respondent should not be allowed to reap high profits because the flawed markets allowed Respondents to take advantage of the situation.[1070]

1036. Next, the California Parties address Coral's proffered justifications. Specifically, Coral argued that (1) the high prices charged were legitimate risk premiums; (2) Coral's sales to CERS did not constitute undue price discrimination because they constituted back-to-back transactions; and (3) Coral's behavior helped CERS.[1071]

1037. The California Parties contend that Coral failed to provide any empirical measures or contemporaneous documents that demonstrated that a specific risk premium was added to sales to CERS.[1072] The California Parties assert that Coral's own witnesses showed that the "risk premium" amounted to nothing more than profit maximization. The California Parties further state that Dr. Fox-Penner found that any appropriate risk

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[1067] *See* Ex. SNA-1 at 8-15, 21; Ex. SNA-9 at 26, 34-35; Ex. S-13 at 15-20; Ex. TRC-1 at 5-10, 16-23, 26-50, 87-99, 104-29, 155-56.

[1068] Ex. CAT-041 at 30, 79-86, 106-08.

[1069] *Id.* at 134, 140.

[1070] *See, e.g.*, *In re Make-Whole Payments and Related Bidding Strategies*, 144 FERC ¶ 61,068 (2013); *Barclays Bank PLC*, 144 FERC ¶ 61,041 (2013); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 142 FERC ¶ 63,011, at P 157 (2013).

[1071] *See* Ex. SNA-1 at 5-23; Ex. SNA-9 at 4-33.

[1072] Ex. CAT-413 at 44-50.

premium for sales to CERS would have fallen well below the twenty-five percent average margin charged by Coral.[1073]

1038. The California Parties also assert that Mr. Taylor found that the prices that Coral charged were not connected with risk[1074] and Coral maximized profits by waiting to sell to CERS until blackouts were imminent. The California Parties cite an internal Coral email encouraging traders to "be patient" and wait until CERS was desperate for energy, such as when the "weather … heat[ed] up," in order to push margins as high as possible.[1075] The email also instructed traders to push the margin as high as possible as long as Coral could still "pass[] the red-faced test" if confronted by a regulator.[1076]

1039. The California Parties also aver that Ms. Bowman admitted to numerous inconsistencies in Coral's risk premium defense and that the purported risk premium was just a profit maximizer. The California Parties state that Ms. Bowman acknowledged that the risk premium did not change depending on credit limits.[1077] Moreover, the California Parties note that if risk premiums had been connected to credit limits, the risk premiums would have lowered in connection with raised credit limits;[1078] however, Coral's "risk premiums" increased as prices increased.[1079] The California Parties further state that Ms. Bowman acknowledged that the risk premium fluctuated throughout the day – and even throughout each hour – despite previous testimony that the risk premium remained constant over the day.[1080] Ms. Bowman further stated that she had "no knowledge" of whether the term "risk premium" was used in contemporaneous Coral documents,[1081] and

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[1073] *See* Ex. SNA-14.

[1074] Ex. CAT-289 at 89-96. *See also* Ex. CAT-041 at 79-83, 106, 125-26; Ex. CAT-104; Ex. CAT-113; Ex. CAT-114; Ex. CAT-123; Ex. CAT-137; Ex. CAT-346 through CAT-351; Ex. CAT-360; Ex.CAT-361; Ex. CAT-378; Ex. CAT-379.

[1075] Ex. CAT-137.

[1076] *Id*.

[1077] Tr. 4052:10-20 (Bowman).

[1078] Ex. SNA-1 at 15; Ex. CAT-289 at 90-91.

[1079] *See* Ex. CAT-041 at 107; Ex. CAT-137; Ex. CAT-289 at 95.

[1080] *Compare* Tr. 4043:6-4044:5 (Bowman) *with* Tr. 4044:16-4051:21 (Bowman).

[1081] Tr. 4052:21-4053:7 (Bowman).

that there were no documents supporting any calculations of risk premiums or financial risk assessments.[1082] The California Parties argue that this indicates that the concept of the risk premium was created solely for litigation purposes. Furthermore, the California Parties state that Ms. Bowman acknowledged that there was no way to tell how much of Coral's risk premium constituted actual risk, and that the risk premium "wasn't really calculated on [the] basis" of assessing the "actual risk of selling."[1083] Lastly, the California Parties note that Ms. Bowman admitted that Coral's traders, not the credit department, were the ones responsible for determining the risk premium, that the risk premium was nothing more than profit maximization, and that "there was no limit" to the risk premium that Coral traders could get.[1084]

1040. Next, the California Parties respond to Coral's assertion that it sold to CERS through "back-to-back" transactions rather than through a portfolio or resources. The California Parties contend that even if Coral's characterization of its transactions as "back-to-back" is accepted, it would not disprove price discrimination. Rather, Dr. Fox-Penner asserted that the "back-to-back" analysis does "a better job of proving price discrimination than disproving it."[1085]

1041. The California Parties argue that Coral failed to substantiate its "back-to-back" transactions defense. The California Parties state many of the supposed "back-to-back" transactions involved upstream transactions in which Coral sold power out of California to a third party and then bought it back at COB.[1086] The California Parties assert that Mr. Tranen's "back-to-back" analysis merely represents the last transaction of a series of transactions that took energy out of California and sold it back to CERS.[1087]

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[1082] Tr. 4032:15-4037:18 (Bowman). *See also* Ex. CAT-710 through CAT-712.

[1083] Tr. 4040:3-13 (Bowman).

[1084] Tr. 4039:3-21 (Bowman).

[1085] Ex. CAT-413 at 68.

[1086] *See* Tr. 2969:20-2995:16, 3010:11-3011:2 (Taylor); Ex. CAT-668a; Ex. CAT-669 through CAT-675; Ex. CAT-705; Ex. CAT-706; Tr. 3924:6-3928:19, 3948:19-3952:15 (Tranen). *See also* Ex. CAT-041 at 80; Ex. CAT-104.

[1087] Tr. 2993:10-21 (Taylor).

1042. The California Parties state that Mr. Tranen even admitted that these multi-party transactions could constitute False Exports.[1088] The California Parties further note that Mr. Tranen admitted that he examined only 19 of 1,703 transactions to determine the origin of the energy that was later sold to CERS.[1089] Moreover, Mr. Tranen admitted that he only reviewed a selected few documents and a "handful" of trader tapes.[1090] Lastly, the California Parties state that the analysis done by Mr. Tranen in response to Mr. Taylor's redirect-examination testimony showed that there were potentially more than 300 hours in which Coral was exporting power for later resale to CERS.[1091]

1043. Next, the California Parties respond to Coral's assertion that Coral's long-term contract with CERS constitutes a legitimate business justification for Coral's high prices.[1092] The California Parties assert that Exhibit SNA-43 demonstrates that Coral was intent on entering into the long-term contract whether or not that long-term contract was backed by bonds. The California Parties note that the "Proposal Summary" in Exhibit SNA-43 states that CERS "refused to grant most of the credit provisions sought by sellers," that any bond issuance would come too late for the long-term contract, and that CDWR might or might not be able to issue rated bonds.[1093] Despite this situation, Coral resolved to move forward with the contract anyway, deciding to wait and see whether bonds were issued in late October, at which point it could walk away from the transaction "<u>with no termination payment</u>."[1094] The California Parties further note that Exhibit SNA-43 is substantially different from the publicly-available final long-term contract.[1095]

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[1088] *See* Tr. 3955:24-3956:14 (Tranen). The California Parties assert that regardless of whether Coral's multi-party transactions were technically False Exports within Mr. Taylor's definition, they clearly were fraudulent.

[1089] Tr. 3957:6-20 (Tranen).

[1090] Tr. 3912:11-3915:6 (Tranen).

[1091] Tr. 3973:6-13 (Tranen). Mr. Tranen did not introduce a copy of his new analysis into the record. Tr. 3974:25-3975:1, 3992:6-11 (Tranen).

[1092] Ex. SNA-43; Tr. 4001:24-4005:23 (Bowman).

[1093] Ex. SNA-43 at 26.

[1094] Ex. SNA-43 at 26 (emphasis in original).

[1095] California Department of Water Resources, Master Power Purchase and Sale Agreement of May 24, 2001, *available at*

(continued…)

1044. Lastly, the California Parties argue that Coral wrongly claims that its actions benefited California. The California Parties assert that Coral attempted to maximize its profits and was not inhibited by the potential harm to CERS or California. The California Parties note that Ms. Bowman, the manager of Coral's entire West Region,[1096] stated at the time that she had no "ethical problem" with blackouts[1097] and that her main focus was on the millions of dollars that Coral was making in a matter of hours.[1098] The California Parties state that this is further supported by the fact that Coral's margins were largest during Stage 3 emergency periods and real-time.

1045. Moreover, the California Parties contend that Ms. Bowman's attempts to paint Coral's entrance into a long-term contract with CERS and its investments in generators as helping CERS are diametrically opposed to the filed testimony of Coral's witness Mr. Brown in the long-term contract case.[1099] Specifically, Mr. Brown stated that the purpose of the long-term contract was to benefit Coral because Coral had chosen to invest in some generators.[1100] Mr. Brown further stated that Coral needed to hedge against the investments that it had chosen to make, and thus needed to enter into the long-term contract.[1101]

1046. Next, the California Parties respond to assertions made by TransCanada. TransCanada argued that: (1) its pricing was not excessive and reflected TransCanada's acquisition costs; (2) parking did not reflect withholding; (3) TransCanada's preference for sales in real-time was a legitimate response to CERS failing to show its true demand

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http://www.cers.water.ca.gov/pdf_files/power_contracts/coral/052401_coral_final_ppa.pdf.

[1096] Tr. 4014:7-18 (Bowman).

[1097] Ex. CAT-708; Tr. 4055:20-4056:17 (Bowman); Ex. CAT-713 at 7:24-8:3.

[1098] Ex. CAT-713 at 7:13-24.

[1099] Coral Power, LLC, Brown Direct Testimony, Docket No. EL02-60-003, (filed Oct. 17, 2002).

[1100] *Id.* at 43.

[1101] December 12, 2002 Hearing Transcript, Docket No. EL02-60-003, at 2349:11-18 (Brown).

in the day-ahead market; (4) TransCanada's negotiations with CERS did not involve duress; and (5) that the volatility of the PPoA justified high prices to CERS.[1102]

1047. First, the California Parties argue that neither TransCanada's acquisition costs nor the duration and timing of transactions justify TransCanada's high prices. The California Parties aver that both Mr. Taylor and Dr. Fox-Penner showed that TransCanada's high prices were the result of high mark-ups not acquisition costs.[1103] The California Parties state that TransCanada's margins ranged from $115/MWh to $165/MWh.[1104] Additionally, the California Parties note that Dr. Fox-Penner did not find higher acquisition costs associated with sales to CERS.[1105] Moreover, the California Parties state that Dr. Fox-Penner found that criticisms of failing to "match" transactions in terms of the duration of the delivery period were flawed, and that the profit margins calculated for TransCanada's sales to CERS were appropriate.[1106]

1048. Second, the California Parties contend that TransCanada had no valid reason to enter into its parking transactions. The California Parties aver that Mr. Taylor demonstrated that TransCanada undertook its parking transactions not for legitimate business reasons, but for the purpose of withholding energy so that it could be sold in real-time.[1107] Moreover, the California Parties state that contemporaneous trader notes clearly indicate that withholding was the purpose.[1108] The California Parties further state that there is evidence that demonstrates that TransCanada's traders were attempting to conceal where energy was going.[1109] The California Parties conclude that concealment and withholding are not legitimate business justifications for the parking transactions.

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[1102] Ex. TRC-1 at 124-29; Ex. TRC-77 at 41-45.

[1103] Ex. CAT-289 at 101-02; Ex. CAT-041 at 84-86; Ex. CAT-413 at 5-6, 38-41, 51-54.

[1104] Ex. CAT-289 at 101-02.

[1105] Ex. CAT-161 at 29-68.

[1106] Ex. CAT-413 at 16-20.

[1107] Ex. CAT-289 at 102-04.

[1108] Ex. CAT-041 at 85; Ex. CAT-118 at 5.

[1109] Ex. CAT-699 at 12, 26; *see also* Tr. 3666:5-3674:5 (Kunz).

1049. Third, the California Parties contend that TransCanada wrongly claims that CERS failed to show its true demand in the day-ahead market. The California Parties state that Mr. Taylor refuted this argument, noting that it was a "recapitulation of the 'underscheduling' argument made by sellers with regard to the pre-CERS period."[1110] The California Parties aver that Mr. Taylor showed that the price data did not support this argument and that any CERS-related price distortion was not in the day-ahead market, but rather in real-time.[1111]

1050. Fourth, the California Parties argue that TransCanada cherry-picked certain transactions and the corresponding trader tapes to demonstrate that CERS was not under duress. The California Parties note that Mr. Taylor had not even alleged duress in all but one instance, and appropriately adjusted that conclusion.[1112]

1051. Fifth, the California Parties assert that volatility in PPoA does not justify the prices TransCanada charged CERS. The California Parties state that TransCanada regularly traded in the PPoA market and understood its dynamics.[1113] The California Parties note that TransCanada provided one example where its traders did not purchase in PPoA because of higher potential risk.[1114]

1052. With respect to the pricing data described by Mr. Kunz as a "typical day,"[1115] the California Parties assert that Mr. Kunz chose the one day during the CERS Period that represented a price that far exceeded typical prices.[1116] The California Parties state that Mr. Kunz later admitted that he chose the day to demonstrate the volatility in the market.[1117] The California Parties assert that the price that TransCanada received from

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[1110] Ex. CAT-289 at 102.

[1111] *Id.* at 103.

[1112] *Id.* at 103-04.

[1113] Tr. 3578:13-17 (Kunz).

[1114] Tr. 3693:19-3695:4 (Kunz).

[1115] Tr. 3544:19-24, 3642:22-3643:99 (Kunz).

[1116] Ex. CAT-697; Tr. 3643:19-3648:19 (Kunz).

[1117] Tr. 3650:1-18 (Kunz).

CERS was far greater than the price that TransCanada paid in PPoA in almost every instance.[1118]

1053. The California Parties further state that Mr. Kunz admitted that there was no real risk of PPoA volatility because, if TransCanada were to notice a period of extreme volatility, it could simply choose to stop selling until that volatility stopped.[1119] Moreover, the California Parties note that TransCanada's internal reports acknowledged that TransCanada was able "to capitalize on volatility" in the market.[1120]

1054. Sixth, the California Parties contend that TransCanada's credit and litigation risk arguments are unsupported. The California Parties note that TransCanada carefully considered its credit exposure, sought to expedite the approval of credit to CERS in late January 2001, and, by early March 2001, had set that limit at an amount that permitted it to make sales of 50 MWh in each hour to CERS without exceeding the limit.[1121] The California Parties assert that the credit file that TransCanada maintained on CERS does not reveal the concerns that Dr. Morris suggests, and Dr. Morris did not even use it in his analysis.[1122] The California Parties aver that contemporaneous records fully supported Dr. Fox-Penner's conclusion that credit risk was not the basis for the premiums that TransCanada charged to CERS.

### 2. <u>TransCanada Initial Brief</u>

#### (a) Allegations of Fraud, Duress, and Bad Faith

1055. TransCanada states that in *Morgan Stanley* the Supreme Court explained that the Commission can set aside a contract where there is unfair dealing at the contract formation stage, for instance, if it finds traditional grounds for the abrogation of the contract such as fraud or duress.[1123] Thus, TransCanada concludes that claims of duress,

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[1118] Ex. CAT-698; Tr. 3656:1-3657:4 (Kunz).

[1119] Tr. 3653:13-19, 3657:13-17 (Kunz).

[1120] Tr. 3660:2-3, 3662:2-10 (Kunz).

[1121] Ex. TRC-1 at 44. *See also* Ex. CAT-699 at 26; Ex. CAT-703.

[1122] Tr. 3784:4-8 (Morris).

[1123] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008) (quoting *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at P 110 (2003)).

fraud, and bad faith present questions regarding behavior at the contract formation stage to determine whether the parties formed a "valid" contract.[1124]

1056. TransCanada states that duress refers to "improper pressure applied during the bargaining process" and takes two forms – physical and non-physical.[1125] Non-physical duress, occurs when "a party's manifestation of assent is induced by an improper threat by another party that leaves the victim no reasonable alternative."[1126] TransCanada notes that the California Parties' claims of duress are non-physical, and more specifically, "economic duress."

1057. TransCanada states that non-physical duress requires three elements be shown: (1) one side involuntarily accepted the terms of another; (2) circumstances permitted no other alternative; and (3) such circumstances were the result of coercive acts of the opposite party.[1127] TransCanada asserts that the duress must be proven to have been the result of the opposite party's conduct and not of the necessity of the party claiming duress.[1128] Thus, "the mere stress of business conditions … where the defendant was not responsible for those circumstances"[1129] and economic pressure, "even the threat of considerable financial loss," does not constitute duress.[1130]

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[1124] *See A&S Council Oil Co., Inc. v. Lader*, 56 F.3d 234, 240 (D.C. Cir. 1995); *PacifiCorp v. Reliant Energy Servs., Inc.*, 105 FERC ¶ 61,184, at P 55 (2003).

[1125] *Utah Power & Light Co.*, 33 FERC ¶ 63,001, at 65,003-04 (1985), *aff'd*, 41 FERC ¶ 61,308, at 61,807 (1987).

[1126] *Boud v. SDNCO, Inc.*, 54 P.3d 1131, 1137 (Utah 2002) (quoting RESTATEMENT (SECOND) OF CONTRACTS § 175(1) (1979)).

[1127] *Fruhauf Sw. Garment Co. v. United States*, 111 F. Supp. 945, 951 (Ct. Cl. 1953) (citing *United States v. Bethlehem Steel Corp.*, 315 U.S. 289, 301 (1942) and *French v. Shoemaker*, 81 U.S. 314, 332 (1872)); *see also Utah Power & Light Co.*, 33 FERC at 65,004.

[1128] *La Crosse Garment Mfg. Co. v. United States*, 432 F.2d 1377, 1382 (Ct. Cl. 1970).

[1129] *Fruhauf*, 111 F. Supp. at 951.

[1130] *Int'l Tel. & Tel. Corp. v. United States*, 509 F.2d 541, 549 & n.11 (Ct. Cl. 1975).

1058. Moreover, TransCanada states that "[e]conomic duress may not be implied merely from the making of a hard bargain."[1131] TransCanada avers that the pressures of the negotiation process "do not constitute duress if there were reasonable alternatives available to the party claiming duress."[1132] Moreover, the mere loss of a potential bargain or the fact that all other alternatives were more expensive does not leave the party with "no reasonable alternative."[1133]

1059. Lastly, TransCanada contends that "[d]uress involves a step beyond mere illegality and implies that a person has been unlawfully constrained or compelled by another to perform an act under circumstances which prevent the exercise of free will."[1134] Thus, "a threat to do what one has a legal right to do cannot constitute duress."[1135]

1060. With respect to fraud, TransCanada defines fraud as "an intentional perversion or concealment of the truth for the purpose of inducing another in reliance upon it to part with some valuable thing or to surrender a legal right."[1136] TransCanada states that fraud consists of five elements: (1) the respondent made a false material representation; (2) the respondent knew the representation was false when it was made or made the representation recklessly without any knowledge of its truth; (3) the respondent made the misrepresentation with the intent to induce the claimant to enter into an agreement; (4) the claimant justifiably relied upon the misrepresentation; and (5) the claimant thereby suffered injury.[1137]

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[1131] *Aircraft Assocs. & Mfg. Co., Inc. v. United States*, 357 F.2d 373, 378 (Ct. Cl. 1966).

[1132] *See Utah Power & Light Co.*, 33 FERC ¶ 63,001, at 65,004 (1985) (citing *La. Pac. Corp. v. United States*, 656 F.2d 650, 653 (Ct. Cl. 1981)).

[1133] *See Ne. Utils. Serv. Co.*, 52 FERC ¶ 61,336, at 62,314 n.7 (1990); *Boud v. SDNCO, Inc.*, 54 P.3d 1131, 1138 (Utah 2002).

[1134] *Fruhauf*, 111 F. Supp. at 952.

[1135] *Swam v. Philpott*, 1968 U.S. Dist. LEXIS 11638, at *3 (S.D. Ill. 1968).

[1136] *In re Allied Supermarkets, Inc.*, 1988 U.S. Dist. LEXIS 18194, at *11 (E.D. Mich. 1988) (quoting *Barkau v. Ruggirello*, 113 Mich. App. 642, 647 (1982)); *see also Office of Consumers' Counsel v. FERC*, 783 F.2d 206, 215 (D.C. Cir. 1986).

[1137] *Eason Corp. v. Easton Assocs., Inc.*, 728 F.2d 285, 292 (6th Cir. 1984); *see also Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 115 FERC ¶ 61,375, at PP 77-78 (2006).

1061. Next, TransCanada states that bad faith is defined as [t]he opposite of 'good faith,' generally implying or involving actual or constructive fraud, or a design to mislead or deceive another, or a neglect or refusal to fulfill some duty or some contractual obligation, not prompted by an honest mistake as to one's rights or duties, but by some interested or sinister motive."[1138] TransCanada notes that in applying claims of bad faith, the Commission has held that mere evidence of hard bargaining does not amount to bad faith.[1139]

1062. Thus, TransCanada asserts that the California Parties must demonstrate an illicit and intentional act in the contract negotiations in order to show fraud, duress or bad faith. TransCanada contends that the California Parties have not demonstrated that the contracts entered into between CERS and TransCanada are invalid on the basis of duress, fraud, or bad faith.

1063. First, TransCanada argues that the parameters used by Mr. Taylor to identify a "contract" do not accord with the principles of contract law. TransCanada states that under the WSPP Agreement, a contract consists of the WSPP Agreement plus a Confirmation Agreement.[1140] The Confirmation Agreements were memorialized in taped telephone calls between the CERS and TransCanada traders.[1141] TransCanada asserts that rather than identifying contracts based on the trader conversations, Mr. Taylor identified a contract based on the CERS database that grouped transactions using CERS deal tickets.[1142] TransCanada contends that these deal tickets are inaccurate and inconsistent with the actual confirmations.[1143] Moreover, TransCanada avers that the trader tapes are the best evidence of the course of negotiations between CERS and a

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[1138] *MCI Commc'ns Corp. v. Am. Tel. & Tel. Co.*, 708 F.2d 1081, 1159 & n.116 (7th Cir. 1983).

[1139] *Pac. Gas & Elec. Co.*, 111 FERC ¶ 61,312, at P 9 (2005); *see also Pub. Util. Comm'n of Cal. v. Sellers of Long Term Contracts to the Cal. Dept. of Water Res.*, 105 FERC ¶ 61,182, at P 86 (2003).

[1140] Ex. CAT-289 at 142:18-19; *see also* Tr. 2410:21-24 (Taylor); Ex.TRC-83 at 8.

[1141] Tr. 2410:21-24 (Taylor).

[1142] *See* Tr. 870:6-24 (Lee); Tr. 2377:22-2378:2, 2481:2-23, 2433:4-17 (Taylor); Ex. CAT-031.

[1143] *See* Ex. TRC-77 at 25:4-26:19; Tr. 878:21-900:11, 936:14-938:8 (Lee); Ex. TRC-1 at 149:9-16; Ex.TRC-93 at 6-23.

seller of energy. TransCanada notes that the California Parties have had ample opportunity to perform their own review of the trader tapes, but failed to do so prior to submitting their direct testimony in this case.[1144] TransCanada further notes that it has submitted transcripts of each trader tape for all the contracts entered into between TransCanada and CERS.[1145]

1064. Next, TransCanada argues that the California Parties' analysis to determine if contracts exhibited duress, fraud, or bad faith is flawed. Specifically, TransCanada notes that Mr. Taylor made a determination of duress, fraud, or bad faith if the price charged to CERS exceeded the *Power Markets Week* price plus $75.00 or if Dr. Fox-Penner found undue price discrimination.[1146] TransCanada states that Mr. Taylor did not distinguish between duress, fraud, or bad faith, but rather combined each of these three separate and distinct legal concepts into a single category. TransCanada contends that failing to price in conformity with an index is wholly irrelevant to establishing duress, fraud or bad faith.

1065. TransCanada avers that Mr. Taylor did not present any evidence pertaining to the negotiations between CERS and TransCanada, and admitted that he has no personal first-hand knowledge of duress, fraud, or bad faith affecting the formation of any agreement.[1147] TransCanada further notes that Mr. Taylor never spoke to a single CERS trader who traded with TransCanada and prior to submitting his direct testimony, never reviewed any of the recorded trader tapes.[1148] Moreover, TransCanada states that when preparing his rebuttal testimony, Mr. Taylor only reviewed those trader tapes submitted by TransCanada in their answering testimony.[1149] TransCanada contends that the California Parties failed to systematically review the best evidence of negotiations between CERS and TransCanada, the taped Confirmation Agreements.

1066. Next, TransCanada asserts Mr. Taylor testified that consideration of duress, fraud, and bad faith cannot be reduced to a formula.[1150] TransCanada states that Mr. Taylor

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[1144] Tr. 2433:10-17 (Taylor).

[1145] Ex. TRC-221; Ex. TRC-222.

[1146] Tr. 2385:8-2386:18 (Taylor).

[1147] Tr. 2431:9-14 (Taylor).

[1148] Tr. 2431:15-2432:24, 2455:5-15 (Taylor).

[1149] Tr. 2434:20-2436:2, 2455:5-15 (Taylor).

[1150] Tr. 2375:6-9 (Taylor); Ex. CAT-289 at 150:7-24.

admitted that his inference of duress, fraud, or bad faith based on the *Power Markets Week* price could be refuted by reviewing the recorded trader tapes.[1151] TransCanada argues that simply examining pricing data cannot show what transpired in the negotiations between CERS and TransCanada, which is necessary to establish the elements of duress, fraud, and bad faith.[1152]

1067. Furthermore, TransCanada avers that the *Power Markets Week* data do not provide appropriate benchmarks related to TransCanada's sales. TransCanada states that *Power Markets Week* reported after the fact, day-ahead peak and off-peak pricing,[1153] while all of TransCanada's sales to CERS were in the day-of market.[1154] TransCanada notes that Mr. Taylor recognized that many factors can cause day-ahead prices to diverge from day-of prices.[1155] TransCanada also states that day-ahead energy is typically sold in multi-hour blocks, whereas day-of energy is typically sold in smaller increments of time.[1156]

1068. TransCanada also contends that the *Power Markets Week* data may not reasonably reflect the prices in the marketplace because the data are assembled by phone calls to energy companies that voluntarily reported their sales.[1157] TransCanada states that this is exemplified by the total amount of sales reported in *Power Markets Week*.[1158] For example, only a single 25-megawatt, off-peak sale at COB was reported to *Power*

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[1151] Tr. 2443:14-17 (Taylor). TransCanada notes that Mr. Taylor did adjust one of his findings based on the trader tapes submitted with TransCanada's answering testimony because the tape indicated that CERS set the price without any offer from TransCanada. Ex. CAT-289 at 104:5-12.

[1152] Tr. 2443:4-5 (Taylor).

[1153] Tr. 2482:23-2483:13, 2757:15-17 (Taylor).

[1154] Tr. 2758:2-5 (Taylor).

[1155] Tr. 2779:7-16. (Taylor). *See also* Ex. CAT-041 at 36, Table II-3; Ex. CAT-289 at 103:4-8

[1156] *See* Tr. 875:1-4 (Lee).

[1157] Tr. 2488:23-2489:14 (Taylor).

[1158] Ex. TRC-193. *See* Tr. 2482:10-17 (Taylor).

*Markets Week* for February 6, 2001, even though CERS's own data show that over 25,000 MWh were transacted that day at COB.[1159]

1069. TransCanada next states that there was a lag in time between the time that prices were charged and the time that prices were reported in *Power Markets Week*.[1160] TransCanada notes that as a weekly publication, *Power Markets Week* day-ahead pricing cannot logically serve as a basis for inferring trader knowledge of market pricing when negotiating day-of transactions.

1070. Next, TransCanada asserts that the "evidentiary support" identified by Mr. Taylor also does not establish duress, fraud or bad faith. TransCanada states that a detailed review of the documents and materials provided by Mr. Taylor reveals that none of the documents listed for TransCanada's contracts demonstrate that the contracts were the product of duress, fraud, or bad faith.

1071. First, TransCanada states that Mr. Taylor provided the WSPP Agreement.[1161] TransCanada notes that if the WSPP Agreement itself was sufficient to show duress, fraud or bad faith, every single transaction conducted thereunder would not be entitled to *Mobile-Sierra* protection. Second, Mr. Taylor provided a February 25, 2001internal CERS memorandum that does not mention TransCanada.[1162] The third and fourth documents relied on by Mr. Taylor are the direct testimonies of Mr. Hart and Ms. Lee, which also do not make specific allegations against TransCanada.[1163] Fifth, Mr. Taylor provides a series of internal CERS emails regarding credit limits imposed by some seller, but not TransCanada.[1164] TransCanada states that Mr. Taylor alleges that the emails involve showing "sellers' pivotality," but Mr. Taylor agreed that he did not perform a pivotal supplier analysis with respect to TransCanada.[1165] Sixth, TransCanada states that

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[1159] *See* Tr. 2486:18-2487:3 (Taylor); Ex. TRC-82 at 17-24.

[1160] Tr. 2483:1-4 (Taylor).

[1161] Ex. CAT-124.

[1162] Ex. CAT-060; Tr. 2462:16-2463:1 (Taylor).

[1163] Tr. 2463:2-18 (Taylor).

[1164] Ex. CAT-138; Tr. 2463:19-2464:5 (Taylor).

[1165] Tr. 2464:23-25 (Taylor); *see also* Ex. TRC-1 at 129:1-9; Ex. TRC-72 at 3; Ex. TRC-4 at 81.

Mr. Taylor listed three additional documents pertaining to March 20, 2001, but none involve TransCanada.[1166] Lastly, Mr. Taylor cites a trader conversation between CERS and APB, a CERS broker, for evidentiary support related to transactions on April 11, 2001.[1167] TransCanada notes that the trader tape does not mention TransCanada.[1168]

1072. TransCanada avers that at best, these documents support Mr. Taylor's claim that California experienced stress during the CERS Period. However, TransCanada asserts that to the extent that stress existed, it was due to market fundamentals and California's flawed regulatory structure. TransCanada notes that it did not sell to California or CERS before January 31, 2001, and there is no evidence that TransCanada had any role in creating that stress. TransCanada contends that the California Parties fail to distinguish between stress experienced in the State of California and duress caused by TransCanada.

1073. TransCanada notes that Mr. Taylor also provides TransCanada's deal tickets as evidence of parking energy for transactions on March 21 and 22, 2001.[1169] TransCanada argues that Mr. Taylor wrongly alleges that TransCanada parked and withheld energy day-ahead in order to extract higher prices by selling the energy to CERS day-of. TransCanada states that these documents only show TransCanada parked power on two separate occasions. TransCanada asserts that, as Mr. Taylor acknowledged, there are legitimate reasons why parties enter into parking arrangements and parking by itself does not demonstrate any wrongful activity.[1170]

1074. TransCanada also avers that Mr. Taylor ignored information that demonstrates that the two parking transactions were undertaken for valid reasons. First, TransCanada states that the timing of the transactions with CERS was consistent with the typical trading practices of TransCanada and CERS.[1171] Second, TransCanada notes that the parking transactions involved Portland General Electric (PGE), an entity that would not extend

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[1166] Ex. CAT-384, Ex. CAT-386, Ex. CAT-388. Tr. 2466:7-2467:11 (Taylor).

[1167] Ex. CAT-403.

[1168] Tr. 2470:12-19 (Taylor).

[1169] Ex. CAT-117; Ex. CAT-118; Tr. 2467:19-2468:12 (Taylor).

[1170] Ex. TRC-1 at 115:15-16. Tr. 2527:17-24 (Taylor).

[1171] Ex. TRC-77 at 45:1-5.

credit to CERS. Thus, the parking transactions served as a means to provide CERS with energy that otherwise was unavailable to CERS when CERS sought it.[1172]

1075. Moreover, TransCanada notes that Mr. Taylor admitted that TransCanada did not have an affirmative obligation to sell energy day-ahead to CERS or to buy energy day-ahead in order to provide that energy to CERS.[1173] TransCanada also states that Mr. Taylor did not analyze the price TransCanada could have received had it sold power in the day-ahead market, and therefore, could not compare any alternative price to the price TransCanada actually received from CERS.[1174] Thus, TransCanada asserts that the California Parties failed to demonstrate that TransCanada engaged in withholding activity for the purpose of extracting a higher price.

1076. Lastly, TransCanada notes that the California Parties have previously asserted claims that TransCanada's two parking transactions are a basis for refunds and have not been successful.[1175]

1077. Next, TransCanada asserts that a review of the actual contract negotiations contained in the recorded trader tapes directly refutes Mr. Taylor's conclusions that TransCanada improperly threatened CERS (duress), knowingly or recklessly misrepresented a material fact to CERS (fraud), or acted fraudulently or deceptively when negotiating with CERS based on a sinister motive (bad faith).

1078. TransCanada states that at most, the trader tapes reflect only a few instances of "hard bargaining," which is not evidence of duress or bad faith.[1176] TransCanada avers that the trader tapes reveal that negotiations between CERS and TransCanada were conducted in a friendly and jovial manner,[1177] and at times, TransCanada tried to help

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[1172] Ex. TRC-122; Ex. TRC-121; Ex. TRC-77 at 44:18-46:13; Ex. TRC-118; Ex. TRC-135 at 2.

[1173] Tr. 2525:8-15 (Taylor).

[1174] Tr. 2529:8-2530:10 (Taylor).

[1175] *See California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 130 FERC ¶ 63,017, at P 238 (2010); *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 135 FERC ¶ 61,113 (2011); *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178 (2011), *reh'g denied*, 139 FERC ¶ 61,210 (2012).

[1176] *See, e.g.*, Ex. TRC-196; Ex. TRC-208; Ex.TRC-212; Ex. CAT-659.

[1177] *See, e.g.*, Ex. TRC-146; Ex. TRC-151.

CERS by offering a sales price that was below the price CERS offered.[1178] TransCanada states that the trader tapes demonstrate that in an overwhelming number of instances, TransCanada displayed a strong desire to work with CERS traders to achieve a mutually acceptable price that both parties felt was fair and reasonable.[1179]

1079. TransCanada notes that at hearing, Ms. Lee and Mr. Taylor heard a number of tapes, none of which evidenced fraud, duress, or bad faith. For example, Ms. Lee admitted that for the transaction occurring on February 8, 2001 for hour ending 11, she did not hear anything that constituted a TransCanada trader exercising duress,[1180] notwithstanding Mr. Taylor's contrary conclusion.[1181] Additionally, TransCanada states that at hearing, Mr. Taylor admitted that the trader tape for hour ending 23 on February 21, 2001 conflicted with his prior conclusion regarding duress, fraud, and bad faith.[1182] TransCanada notes that on another occasion, TransCanada offered to drop the sales price to "an off-peak price," but that CERS declined the offer, stating that the peak price TransCanada was asking for was "good enough."[1183] TransCanada contends that this exemplifies the arbitrary nature of Mr. Taylor's formulaic test and its failure to demonstrate duress, fraud, or bad faith.

1080. TransCanada further argues that Mr. Taylor misinterpreted or mischaracterized exchanges between TransCanada and CERS that he ultimately did review. For example, TransCanada notes that Mr. Taylor referenced certain calls that he believed illustrated the excessiveness of TransCanada's sales prices to CERS.[1184] TransCanada asserts that the actual tapes demonstrate that Mr. Taylor's recollection of these calls was fundamentally

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[1178] *See, e.g.*, Ex. TRC-89 at 22-23; Ex. TRC-119 at 1-2, 6-7; Ex. TRC-176.

[1179] *See generally* Ex. TRC-222; Ex. TRC-222A.

[1180] Tr. 975:17-21 (Lee); Ex. TRC-151.

[1181] *See* Ex. CAT-412 at 18.

[1182] Tr. 2414:13-17 (Taylor); Ex. CAT-412 at 4. *See also* Tr. 2451:14-2452:5 (Taylor) (admitting that the negotiations between CERS and TransCanada regarding the sale on April 6, 2001 for hours ending 1 through 7 did not reflect anything outside the ordinary norms of negotiations).

[1183] Ex. TRC-177; Tr. 2413:12-2414:8 (Taylor).

[1184] Tr. 2456:3-11 (Taylor).

distorted.[1185] TransCanada notes that Mr. Taylor admitted that there was no evidence of duress after listening to the tapes at hearing.[1186]

1081. Next, TransCanada states that the California Parties attempted to use the settled price of energy in the PPoA in order to support Mr. Taylor's conclusions of fraud and bad faith.[1187] TransCanada first notes that Mr. Taylor admitted that he was not familiar with the rules of the PPoA and never assessed the various risks associated with purchasing energy from the PPoA.[1188] TransCanada states that the PPoA is a highly volatile energy market where a purchaser, such as TransCanada, would not know the settled power pool price until after the hour that the energy was delivered.[1189] Therefore, the pool prices shown in Exhibits CAT-661 and CAT-662 would not have been known by TransCanada's traders at the time that they negotiated and entered into the contracts with CERS.[1190]

1082. TransCanada notes that Mr. Kunz explained that in the PPoA, very minimal fluctuations in supply or demand can lead to dramatic changes in the price.[1191] TransCanada also states that the PPoA was served predominantly by coal plants, including several that were "quite old," and which raised reliability concerns.[1192] TransCanada asserts that the PPoA hourly forecast data demonstrate a considerable level of volatility.[1193]

1083. Lastly, TransCanada states that to the extent the California Parties allege that TransCanada gained excessive profits, Mr. Taylor admitted that a seller attempting to

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[1185] Ex. TRC-196; Ex. TRC-197; Tr. 2516:6-9 (Taylor).

[1186] Tr. 2955:1-5 (Taylor). *See also* Ex. TRC-201 through TRC-219; Tr. 2951:16-2952:25 (Taylor); Ex. CAT-659; Ex. TRC-196; Ex. TRC-197.

[1187] Ex. CAT-661; Ex. CAT-662.

[1188] Tr. 2371:13-2372:3, 2948:17-2949:17 (Taylor).

[1189] Ex. TRC-77 at 7:1-6; Tr. 3547:7-12, 3653:10-12 (Kunz).

[1190] *See* Tr. 3692:6-24 (Kunz).

[1191] Tr. 3550:23-3551:5, 3553:5-13; 3555:2-18 (Kunz); Ex. TRC-225.

[1192] Tr. 3556:2-16 (Kunz).

[1193] Ex. TRC-225; Ex. TRC-231.

maximize profits, in and of itself, is insufficient to show that the seller engaged in duress, fraud, or bad faith.[1194] However, TransCanada asserts that Mr. Taylor's accusations of duress, fraud, and bad faith are tied to his belief that a seller may not make any sales that, in his opinion, have excessive gross margins.[1195] TransCanada contends that it is also clear that Mr. Taylor's accusations of excessive margins are tied to high prices without consideration of the margins that may be associated with those prices, even though Mr. Taylor admitted that there is no price per megawatt hour that is *per se* excessive.[1196]

### (b) Allegations of Undue Price Discrimination

1084. TransCanada states that discrimination is "undue" when there is a difference of rates, terms or conditions among similarly situated customers.[1197] Thus, TransCanada asserts that "factual differences between customers" that "arise from differing costs of service or otherwise" can justify different rates.[1198]

1085. TransCanada avers that the California Parties base their claims of undue discrimination on Dr. Fox-Penner's (1) a hourly sales analysis, (2) a multi-transactional analysis, and (3) regression computations. TransCanada asserts that Dr. Fox-Penner has no experience trading commodities, advising clients regarding commodity risk exposure, performing a case-by-case evaluation of undue price discrimination similar to that done in this proceeding, or authoring any peer-reviewed publications on the topic of undue price discrimination.[1199] TransCanada contends that none of the analyses demonstrate that TransCanada engaged in undue price discrimination against CERS.

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[1194] Tr. 2536:8-12 (Taylor).

[1195] *See, e.g.*, Tr. 2406:15-22, 2441:14-18, 2444:5-15, 2445:25-2446:14, 2496:22-2497:7, 2659:25-2660:5 (Taylor).

[1196] Tr. 2492:23-2493:5 (Taylor).

[1197] *Cal. Indep. Sys. Operator Corp.*, 119 FERC ¶ 61,076, at P 369 (2007) (citing 16 U.S.C. §§ 824d, 824e (2000); *Calpine Oneta Power, L.P.*, 116 FERC ¶ 61,282 (2006)).

[1198] *Cities of Newark, New Castle & Seaford v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985).

[1199] Tr. 1248:3-14, 1308:7-15 (Fox-Penner).

1086. TransCanada notes that Dr. Fox-Penner alleged price discrimination against TransCanada in just twenty-six hours.[1200] Of these twenty-six hours, four hours were found to be unduly discriminatory because the price charged to CERS exceeded the price charged to the non-CERS buyer by $50/MWh or more.[1201] TransCanada notes that Dr. Fox-Penner refers to these pairs of transactions as "identical matching transactions" even though there are critical differences. TransCanada states that the remaining twenty-two hours that were found to be unduly discriminatory were based on Dr. Fox-Penner's standard deviation test.[1202] TransCanada notes that all twenty-two of these hours occurred on the same day, February 22, 2001.[1203]

1087. With respect to the four hours that included "identical matches," TransCanada contends that the transactions were not similarly situated. First, TransCanada states that Dr. Fox-Penner's analysis failed to account for the duration of TransCanada's sales, noting that the non-CERS sales were for a single hour while the CERS sales were part of multi-hour blocks.[1204] Thus, TransCanada contends that the CERS transactions involved greater risk than the non-CERS transactions.[1205] TransCanada further notes that Dr. Fox-Penner did not present an analysis of "whether the durations of matched transactions are comparable" with respect to TransCanada even though he did do such an analysis for other Respondents.[1206] Moreover, TransCanada asserts Dr. Fox-Penner's own definition of "comparable duration" would have excluded the four transactions.[1207]

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[1200] Ex. CAT-163 at 121.

[1201] Ex.CAT-161 at 7:1-3, 71:4-11. Specifically, the California Parties allege undue discrimination on this basis in hour ending 15 on February 4, 2001; hours ending 1 and 23 on February 5, 2001; and hour ending 16 on May 11, 2001. *See* Ex. CAT-163.

[1202] *See* Ex. CAT-163 at 91.

[1203] *See id*.

[1204] Tr. 1149:7-13 (Fox-Penner); Ex. TRC-221 at 2, 3, and 48.

[1205] Ex. TRC-1 at 47:15-16.

[1206] Ex. CAT-413 at 17:14-18.

[1207] Ex. CAT-413 at 18:17-19 ("I consider transactions comparable in duration if transactions … have no greater than two hours difference in durations").

1088. Second, TransCanada contends that Dr. Fox-Penner failed to account for the time of day when the respective CERS and non-CERS sales were agreed to.[1208] TransCanada notes that the price of energy in a given hour moved with the passage of time.[1209] TransCanada asserts that this temporal factor was particularly important to TransCanada because ninety percent of its sales to CERS were made from energy purchased in the PPoA[1210] and TransCanada would not know its acquisition costs until after it agreed to a price to sell that energy to CERS.[1211] TransCanada avers that the longer the period of time between the entry into the agreement and its performance, the greater the chance for adverse price developments in the PPoA. TransCanada asserts that Dr. Fox-Penner admitted that did not consider these risks when formulating his analysis.[1212]

1089. Third, TransCanada contends that Dr. Fox-Penner failed to adequately account for the risks associated with selling to CERS.[1213] TransCanada asserts that Dr. Fox-Penner's conclusion that "CERS was a highly creditworthy entity" is not realistic. TransCanada notes that Dr. Morris testified that selling to CERS was riskier than selling to other buyers because CERS lacked of revenue sources, funding, and financial backing.[1214] TransCanada notes that CERS's own consultant concluded that CERS's credit, administrative, and market risk ranged from medium to very high in February 2001 and from high to very high in the future.[1215] Moreover, TransCanada avers that Ms. Lee and Mr. Hart recognized at the time that the "main factor … limiting CERS' ability in the market … is credit"[1216] and that "[c]redit issues still remain the single largest obstacle to

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[1208] *See* Ex. TRC-1 at 93:12-14.

[1209] Ex. CAT-660 at 37 (showing the price for energy with same counterparty for the same delivery hour moved from $285/MWh at 11:09 pm to $485/MWh at 2:11 am). *See also* Ex. CAT-660 at 55.

[1210] Ex. TRC-77 at 5:4-6:2.

[1211] Ex. TRC-1 at 47:1-5; Ex. TRC-161 at 3.

[1212] Ex. TRC-77 at 7:7-8:17; Ex.TRC-79 at 2-3, 5-8.

[1213] Ex. TRC-1 at 96:2-6.

[1214] Ex. TRC-1 at 32:11-15.

[1215] Ex. TRC-161 at 4.

[1216] Ex. TRC-26 at 1.

purchasing energy out-of-state."[1217] TransCanada further notes that the CPUC denied the utilities' request to recover the costs they paid to CERS at the outset of 2001.[1218]

1090. TransCanada contends that Dr. Fox-Penner's *post hoc* assessment of the credit risk associated with sales to CERS is in conflict with the market reality at the time, noting that many merchants refused to make any transactions with CERS. TransCanada states that Dr. Fox-Penner had no previous experience evaluating credit risk in electric markets[1219] and was unaware of certain facts that affected CERS's credit risk.[1220] With respect to litigation risk, TransCanada avers that Dr. Fox-Penner admitted that measuring litigation risk was "outside the realm of my expertise."[1221] TransCanada states that when the credit, political, regulatory, and litigation risks are considered, CERS paid no more than other TransCanada counterparties.[1222]

1091. Fourth, TransCanada asserts that Dr. Fox-Penner ignores additional variables that would explain the differences in price. For example, TransCanada states that throughout the CERS Period, CERS's net short requirements changed by nearly 10,000 megawatts, including daily swings in the thousands of megawatts.[1223] TransCanada notes that Dr. Fox-Penner admitted that significant changes in CERS's demand would have some impact on the prices at COB, but failed to test for the impact.[1224] Moreover, TransCanada avers that the California Parties did not provide a supply curve during the CERS Period in the Pacific Northwest or calculate a price elasticity of demand for any of the non-CERS buyers.[1225]

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[1217] Ex. TRC-25 at 1.

[1218] Ex. TRC-21 at 15.

[1219] Tr. 1300:24-1301:14 (Fox-Penner).

[1220] *See* Tr. 1246:6-1251:17 (Fox-Penner).

[1221] Tr. 1258:11-18 (Fox-Penner).

[1222] Ex. TRC-1 at 99:1-4.

[1223] Ex. TRC-233 at 1; Ex. TRC-234 at 1.

[1224] Tr. 1222:22-1223:4 (Fox-Penner). *See* Ex. CAT-161; Ex. CAT-413.

[1225] Tr. 1228:4-8, 1401:21-25 (Fox-Penner).

1092. Fifth, TransCanada argues that Dr. Fox-Penner failed to properly account for the fact that TransCanada's sales to non-CERS buyers occurred on the BPA system, approximately 500 miles from COB.[1226] TransCanada states that Dr. Fox-Penner attempted to account for this difference by adding the BPA tariff rate to the price.[1227] However, TransCanada asserts that Dr. Fox-Penner assumed that congestion did not exist during the four "matching hours" and that deliveries could be made by TransCanada at both locations.[1228] TransCanada notes that Dr. Broehm demonstrated that TransCanada's reservation of firm capacity on those lines ranged between zero and one percent, and for much of the time, TransCanada had no firm transmission capacity to COB.[1229] Moreover, TransCanada states that Dr. Broehm testified that the AC Line (north-to-south) was partially curtailed for 26 of the 155 days in the CERS Period.[1230]

1093. TransCanada states that its purchases of energy from the PPoA often occurred when the markets were tight or transmission was constrained and that it did not have firm transmission across the entire Alberta-COB path.[1231] TransCanada asserts that the California Parties have acknowledged that these challenges occasionally prevented energy from being scheduled for export from Alberta to the Pacific Northwest.[1232]

1094. TransCanada also notes that Dr. Fox-Penner suggested that transmission constraints could "fragment the market into smaller sub-markets."[1233] However, TransCanada argues that Dr. Fox-Penner treated sales at different locations, connected by transmission capacity subject to interruption and curtailment during the CERS Period, as the same market and did not test whether distinct pricing between different locations signaled the existence of different markets or sub-markets.

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[1226] Ex. TRC-1 at 87:13-15.

[1227] *Id.* at 88:5-10.

[1228] *Id.* at 90:8-91:2.

[1229] Ex. CAT-237 at 11-17.

[1230] Ex. CAT-237 at 19:9-20:1.

[1231] *See* Ex. TRC-77 at 21:18-22:4; Ex. S-5 at 5:18-6:7.

[1232] Ex. TRC-4 at 83-85; Ex. TRC-141.

[1233] *See* Ex. TRC-1 at 28:13-16; Ex. TRC-11 at 9-10.

1095. TransCanada contends that rather than relying on the tariff rate, which may or may not be applicable to the path and the circumstances in effect at the time of the sale, a more accurate assessment of the value of transmission would account for the difference in price between the two locations, as explained by Dr. Fox-Penner in his own textbook.[1234] TransCanada also asserts that Dr. Fox-Penner failed to properly account for differences in line loss charges on different transmission paths.[1235] TransCanada states that by accounting for the locational difference in price, Dr. Morris demonstrated that for the four "matching hours," the prices are not significantly different and do not indicate undue discrimination.[1236]

1096. Sixth, TransCanada asserts that even using Dr. Fox-Penner's threshold, the evidence of undue discrimination is lacking. TransCanada notes that although there were four hours (out of 14 hours with "matching" non-CERS transactions) where CERS did pay at least $50/MWh more than other TransCanada customers, there were also four hours when CERS paid $50/MWh *less* than other TransCanada customers.[1237] For the remaining six hours, CERS paid essentially the same price ($0.47 less) in five of the hours.[1238] TransCanada states that Dr. Fox-Penner never attempted to reconcile these contrary results.

1097. TransCanada also avers that Dr. Morris' statistical test demonstrates that TransCanada did not price discriminate. Specifically, Dr. Morris tested whether there was a statistically significant difference between TransCanada's average prices to CERS and to non-CERS buyers in the "identical sales."[1239] Dr. Morris concluded that "[t]here is no statistically significant difference" between those prices.[1240]

1098. Next, TransCanada addresses Dr. Fox-Penner's standard deviation test. TransCanada contends that the standard deviation test also fails to demonstrate that

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[1234] Ex. TRC-1 at 88:11-15; Ex. TRC-11 at 4.

[1235] Tr. 3763:18-3764:1 (Morris).

[1236] Ex. TRC-1 at 91:6-92:16; Ex. TRC-55.

[1237] Ex. CAT-163 at 110.

[1238] *Id*.

[1239] Ex. TRC-1 at 84:3-5.

[1240] *Id.* at 84-88; Ex. TRC-53.

TransCanada engaged in undue price discrimination against CERS because the methodology is flawed and premised on an irrational foundation.

1099. First, TransCanada argues that it is impossible to show price discrimination during these hours because TransCanada did not make any sales to non-CERS customers.[1241] TransCanada notes that Dr. Fox-Penner admitted that price discrimination occurs when "you sell the same thing to two different buyers for two different prices."[1242] Additionally, TransCanada states that Dr. Fox-Penner's own definition of price discrimination relies on two transactions involving the same seller.[1243] However, because TransCanada made no non-CERS sales during the subject hours, the PA02-2 database used by Dr. Fox-Penner provides no information on what prices TransCanada would have charged a non-CERS buyer.[1244] TransCanada further avers that it is impossible to determine whether the sellers included in the PA02-2 database are similarly situated to TransCanada.

1100. Second, TransCanada contends that Dr. Fox-Penner improperly compared the sales price charged by TransCanada to CERS in a single hour to the weighted average daily price charged by other sellers to non-CERS buyers. TransCanada states that the prices could vary widely in a single day and an average non-CERS price across an entire day does not account for the specific conditions of TransCanada's sales to CERS in a single hour.[1245] Furthermore, as discussed above, TransCanada notes that the time in which transactions are entered into affects the prices charged.

1101. Third, TransCanada states that the durations of the sales or even if the sales were in peak or off-peak hours are also not identified in the PA02-2 data.[1246] TransCanada notes that its transactions with CERS varied in duration between one and ten hours.[1247] TransCanada also states that Dr. Fox-Penner acknowledged that the PA02-2 data did not

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[1241] Ex. TRC-1 at 60:20-61:3.

[1242] Ex. TRC-5.

[1243] Tr. 1303:7-25 (Fox-Penner).

[1244] Ex. TRC-1 at 83:1-3.

[1245] *See* Ex. TRC-153 at 1-4.

[1246] Ex. TRC-1 at 75:15-19; Tr. 1163:2-6 (Fox-Penner).

[1247] Ex. TRC-87 at 10-11.

include data to test the standard deviation of prices and price dispersions within individual hours.[1248]

1102. Fourth, TransCanada notes that all of the hours identified by the standard deviation test occurred in a single day, February 22, 2001. However, TransCanada states that its pricing behavior with CERS was the same on February 21st, 22nd, and 23rd.[1249] TransCanada asserts that Dr. Fox-Penner admitted that "the reason for the allegation of undue price discrimination on February 22nd is due to the lower prices and a smaller range of prices in trades not involving TransCanada as opposed to any difference in TransCanada's behavior toward CERS."[1250]

1103. Fifth, TransCanada states that Dr. Fox-Penner's standard deviation test produced false positives. TransCanada states that in "at least three cases where the price to CERS is more than six standard deviations above the mean price," Dr. Fox-Penner declined to allege price discrimination where he found that Respondents' actual sales to other buyers did not demonstrate undue discrimination.[1251]

1104. Next, TransCanada states that the California Parties attempted to prove undue price discrimination by comparing the average price from TransCanada's sales to non-CERS buyers to TransCanada's prices to CERS.[1252] TransCanada asserts that Dr. Fox-Penner's calculations are based on flawed data that were inaccurately transcribed, fail to properly distinguish between long-term sales and monthly sales, and create a distinction between day-of sales and hourly sales that is meaningless.[1253] TransCanada states that Dr. Morris found that the actual price difference between sales to CERS and non-CERS buyers was only $41/MWh, without accounting for differences between the buyers.[1254] TransCanada states that when location and risk are accounted

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[1248] Tr. 1265:13-25 (Fox-Penner).

[1249] Ex. TRC-1 at 76:6-8; Ex. TRC-51.

[1250] Ex. TRC-1 at 76-78. February 22nd presents the lowest price difference of any day and contains only twenty-three non-CERS transactions. Ex. TRC-1 at 78-79.

[1251] *Id.* at 75:4-13.

[1252] Ex. CAT-161 at 51:8-14.

[1253] *Id.* at 61:12-62:2, 66:7-18.

[1254] *Id.* at 67:1-12.

for, TransCanada sold energy to CERS on average for $33/MWh less than it sold energy to non-CERS buyers.[1255]

1105. Moreover, TransCanada states that each entity that bought energy from TransCanada paid a different average price during the CERS Period based upon the characteristics of each individual trade.[1256] TransCanada notes that of the twenty entities that bought energy from TransCanada during the CERS Period, CERS paid only the fifth highest average price.[1257] TransCanada asserts that the fact that different buyers paid different prices over a five month period "is to be expected and would occur in any normally functioning market."[1258]

1106. Lastly, TransCanada contends that Dr. Fox-Penner's econometric regression analysis fails to demonstrate undue price discrimination. TransCanada first notes that the regression analysis fails to examine individual contracts, but rather considers contracts in the aggregate. TransCanada also asserts that the analysis did not measure the impact of (1) the duration of transactions, (2) the time at which the transactions were entered into, (3) the location of the transactions, or (4) the credit risks of the buyers.[1259] TransCanada further states that the analysis is not based upon a comparison of the prices charged by a single seller, but upon comparisons of the prices a seller charged to CERS to the prices other sellers charged other non-CERS buyers.

1107. TransCanada states that Dr. Fox-Penner admitted that his regression analysis was done to "get around the fact that matching transactions may not be common or even present."[1260] However, TransCanada argues that, consistent with Dr. Fox-Penner's own definition, price discrimination involves the same seller selling to two different buyers.[1261] TransCanada contends that at most, the regression analysis demonstrates that different sellers charged different prices to different buyers.

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[1255] *Id.* at 68:14-69:5.

[1256] *Id.* at 62:16-63:1.

[1257] *Id.* at 63:1-6.

[1258] *Id.* at 63:6-9.

[1259] Tr. 1275:6-1276:24 (Fox-Penner).

[1260] Ex. CAT-413 at 37:3-4.

[1261] Tr. 1302:17-1303:25 (Fox-Penner).

#### (c) Allegations that Respondents Exercised Market Power

1108. TransCanada states that the California Parties did not allege that TransCanada exercised market power during the CERS Period. TransCanada notes that Dr. Reynolds confirmed that he made "no specific allegation of exercise of market power by TransCanada" and did not undertake a detailed market power analysis with regard to TransCanada.[1262] Additionally, TransCanada states that the record contains no allegation that TransCanada acted as a pivotal supplier or otherwise exercised market power.[1263]

#### (d) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1109. TransCanada argues that the California Parties' claims against TransCanada are unsubstantiated, and the California Parties' testimonies and exhibits do not demonstrate that the price charged under each specific contract was unjust and unreasonable.

#### (e) Legitimate Business Behavior by TransCanada

1110. TransCanada states that its market activities have all been shown to be legitimate business behavior. TransCanada argues that it has demonstrated that that its actions did not involve fraud, duress, unlawful withholding, or undue price discrimination, and that TransCanada lacked market power and was unable to exploit CERS or charge excessive prices. TransCanada argues that even if the California Parties had made a *prima facie* case on their allegations, the various circumstances surrounding each transaction demonstrate that TransCanada engaged in legitimate business behavior, such as accounting for the risks associated with trading with CERS.

### 3. <u>Coral Initial Brief</u>

#### (a) Standard of Proof and Relevant Law

1111. Coral states that in order to avoid the *Mobile-Sierra* presumption, the California Parties must "submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by [Coral] and unjust and unreasonable rates under a specific contract."[1264] Coral notes that complainants bear

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[1262] Tr. 1843:25-1844:5, 1851:14-19 (Reynolds); Ex. CAT-264 at 4:9-10.

[1263] Ex. TRC-72 at 3. *See also* Ex. TRC-1 at 129:5-9; Ex. TRC-4.

[1264] Order on Remand at P 21.

the burden to prove all elements of their allegations by a preponderance of the evidence.[1265]

### (b) Allegations of Fraud, Duress, and Bad Faith

1112. Coral first contends that the California Parties' claims of duress, fraud, or bad faith are outside the scope of this proceeding. Coral argues that the Commission excluded claims of duress, fraud or bad faith in its order setting this proceeding for hearing, noting that the Commission does not typically decide contract claims when they are governed by state law. Coral states that the Order on Remand instructed that permissible evidence must be about "unlawful manipulation" or "unlawful market activity."[1266] Coral notes that the California Parties sought rehearing on this issue, but the Commission denied rehearing, stating that it "stand[s] by the categories of evidence specified in the Remand Order, and continue to find that the categories of permissible evidence have been appropriately tailored …."[1267]

1113. Coral states that the Commission also found that the Complainants' "due process rights are not violated by the exclusion of evidence of violations of state[-law] good faith obligations because … permitting such evidence would require [the Commission] to interpret and apply state contract law."[1268] The Commission further stated that it "expects parties to continue to resolve most contract disputes, including those based on fraud in the inducement, without the involvement of the Commission, relying [instead] on state and federal courts to apply contract law as appropriate."[1269]

1114. Coral further notes that in 2005, the California Parties brought suit against a non-Respondent seller to CERS in state and federal courts seeking abrogation of CERS's purchases based on duress, fraud, and bad faith,[1270] and that the California Parties have

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[1265] *Nantahala Power & Light Co.*, 19 FERC ¶ 61,152 (1982) (citing *Steadman v. SEC*, 450 U.S. 91, 101 (1981)).

[1266] Order on Remand at PP 16-23, 26, 28, 29.

[1267] Order on Rehearing at PP 19, 23, 25.

[1268] *Id.* P 25.

[1269] *Id.* P 25 & n.49 (citing *Prohibition of Energy Market Manipulation*, 114 FERC ¶ 61,047, at P 37 (2006)).

[1270] Tr. 2429:12-22 (Taylor).

had ample opportunity to bring such claims against Respondents in the appropriate forum.

1115. Coral contends that the Commission has "long held that disputes over a contract for the sale of electric energy at negotiated, market-based rates are more appropriately resolved in state courts or arbitration."[1271] Coral states that in another proceeding related to the Western Energy Crisis, the Commission recognized that "there is no federal common law of contracts;" and therefore, allegations of fraud "must be based on the application of state substantive law."[1272] Coral notes that the Commission also has no standard for duress or bad faith and could only apply state law.

1116. Coral states that the Commission applies the three-factor *Arkla* test when determining whether to assert jurisdiction over contractual issues otherwise actionable in state court. That test considers (1) whether the Commission possesses some special expertise which makes the case peculiarly appropriate for Commission decision; (2) whether there is a need for uniformity of interpretation of the type of question raised by the dispute; and (3) whether the case is important in relation to the regulatory responsibilities of the Commission.[1273] Coral contends that the California Parties' claims do not satisfy the test. First, Coral asserts that the Commission has recently reiterated that it "has no special expertise in straight-forward contractual matters."[1274] Moreover, the Commission has specifically declined to assert jurisdiction over claims of fraud[1275] and bad faith.[1276] Second, Coral argues that there is no need for "uniformity of interpretation" regarding the state contract law claims in this proceeding. Lastly, Coral avers that claims of duress, fraud, and bad faith are not important in relation to the

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[1271] *Clarksdale Pub. Utils. Comm'n*, 93 FERC ¶ 61,002 (2000); *see also PPL Mont., LLC*, 96 FERC ¶ 61,313 (2001).

[1272] *Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 115 FERC ¶ 61,375, at P 70 (2006); *see also Town of Massena*, 18 FERC ¶ 61,068, at 61,116 (1982).

[1273] *Ark. La. Gas Co.*, 7 FERC ¶ 61,175 (1979); *PPL Mont., LLC*, 96 FERC ¶ 61,313 (2001). *See also Bd. of Pub. Works v. Wis. Power & Light Co.*, 613 F. Supp. 2d 1122, 1130-31 (D. Minn. 2009) (applying *Arkla* factors to determine FERC did not have primary jurisdiction).

[1274] *Essar Steel Minn., LLC*, 142 FERC ¶ 61,194 (2013); *see also Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 115 FERC ¶ 61,375, at P 2 (2006).

[1275] *City of Vernon*, 115 FERC ¶ 61,374, at PP 40-45 (2006).

[1276] *Cal. Dep't of Water Res.*, 121 FERC ¶ 61,191 (2007).

regulatory responsibility of the Commission because they involve no issue beyond the state law contract dispute. Thus, Coral contends that the California Parties' state contract law claims must be rejected as outside the scope of this proceeding.

1117. Next, Coral contends that the California Parties have not proven duress, fraud, or bad faith under any applicable legal standard. Coral notes that Mr. Taylor, the only witness to make these allegations, provides his own non-legal standards.[1277] However, Coral states that the WSPP Agreement contains a choice of law clause that identifies Utah as the relevant jurisdiction.[1278]

1118. Coral asserts that a contract is voidable for duress "if a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative."[1279] Coral contends that the California Parties have not presented any evidence that Coral threatened anyone. Coral avers that even if such evidence was present, the only plausible grounds in this case for claiming that a threat was improper would be if the threat were a breach of the duty of good faith and fair dealing under a contract with the threatened party.[1280] Coral states that under Utah law, "to find a breach of the duty of good faith and fair dealing, there must be some type of preexisting contractual relationship;"[1281] but here, Coral had no preexisting contractual relationship with CERS and was under no obligation to enter into any transaction with CERS.

1119. Coral also contends that the California Parties' argument that the Western Energy Crisis enabled duress is irrelevant. Coral notes that "[t]he mere fact that a contract is entered into under stress or pecuniary necessity is insufficient [to constitute duress]."[1282] Moreover, Coral states that the California Governor and Legislature were aware of

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[1277] Ex. CAT-041 at 39:1-9.

[1278] Ex. CAT-124 at § 24. *See California ex rel. Brown*, 135 FERC ¶ 61,178, at P 108 (2011) (applying Utah law pursuant to WSPP choice of law provision).

[1279] RESTATEMENT (SECOND) OF CONTRACTS § 175(1) (1979). *Andreini v. Hultgren*, 860 P.2d 916, 921 (Utah 1993) (adopting the legal standard of the Restatement (Second) of Contracts).

[1280] RESTATEMENT (SECOND) OF CONTRACTS § 176 (1979).

[1281] *Andreini*, 860 P.2d at 921.

[1282] *Gold Standard v. Getty Oil Co.*, 915 P.2d 1060, 1064 (Utah 1996) (citing *Horgan v. Industrial Design Corp.*, 657 P.2d 751, 753 (Utah 1982)).

market conditions when they created CERS. Coral argues that the *Mobile-Sierra* presumption should not be avoided on the basis of facts and consequences known by the State of California prior to the creation of CERS.[1283]

1120. Coral states that Mr. Taylor's *Power Markets Week* price test is irrelevant for showing duress because duress claims must be based on a threat. Coral avers that even if Mr. Taylor's price comparisons were probative of actual real-time market prices, "[t]he mere fact of an improvident or bad bargain" is not sufficient to avoid an otherwise valid contract.[1284]

1121. With respect to the California Parties' claims of fraud based on False Export transactions, Coral contends that the claims are redundant and irrelevant. Coral states that to meet the applicable standard for fraud, the California Parties must demonstrate by "clear and convincing evidence" that a Coral false statement injured or damaged CERS.[1285] Coral contends that the California Parties have not demonstrated that Coral made a false statement or that CERS was harmed by such a statement.

1122. Coral asserts that the evidence demonstrates that when CERS asked Coral to identify the source of Coral's power, Coral honestly and accurately informed CERS of the source.[1286] Moreover, Coral avers that there is no rule or market practice that would have required a Coral trader to inform CERS of the complete genealogy of the power, noting that the Commission has found that electricity in the Pacific Northwest was traded an average of six times between the point of generation and the final wholesale purchaser.[1287]

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[1283] *See United States v. Bethlehem Steel Corp.*, 315 U.S. 289, 304-05 (1942) (refusing to invalidate contracts on the sole ground of the coercive effect of circumstances which Congress clearly contemplated).

[1284] *Horgan*, 657 P.2d at 754. *See also Bethlehem Steel Corp.*, 315 U.S. at 312 (Murphy, J., Concurring).

[1285] *Andalex Res., Inc. v. Myers*, 871 P.2d 1041, 1046 (Utah Ct. App. 1994) (citing *Dugan v. Jones*, 615 P.2d 1239, 1246 (Utah 1980) & *Crookston v. Fire Ins. Exch.*, 817 P.2d 789, 800 (Utah 1991)).

[1286] Ex. SNA-1 at 17:3-10. *See, e.g.*, Ex. CAT-366 at 4:12-14.

[1287] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at P 47 (2003).

1123. In addition, Coral contends that the California Parties have provided no evidence that CERS was harmed by any Coral statement. Coral notes that Mr. McIntosh testified that CERS was responding to specific instructions from the ISO to purchase at COB.[1288] Coral states that the alleged "multi-party False Export" transactions were merely a response to CERS's demand in the Pacific Northwest by making additional power available to CERS precisely where it was needed. Thus, Coral avers that these transactions actually benefitted CERS and the State of California and were squarely in the public interest.

1124. Coral also argues that there is also no legal basis for aggregating allegations of duress, fraud, and bad faith into a single finding. Coral asserts that the California Parties must prove all elements of each claim independently.

1125. Next, Coral avers that the California Parties' claims fall short even under Mr. Taylor's "common sense" standards for duress, bad faith, and fraud.[1289] Coral states that Mr. Taylor finds this standard to have been met if Coral was offering power to CERS at a price more than seventy-five dollars higher than a published day-ahead index price. Coral argues that the California Parties fail to explain how an offer can constitute a threat or improper action. Coral states that it was one of many energy suppliers to CERS at COB,[1290] selling to CERS in only 928 of the approximately 3,700 hours of the CERS Period.[1291]

1126. With respect to bad faith, Coral avers that Ms. Lee testified that Mr. Taylor's index price comparison is irrelevant.[1292] Coral states that Ms. Lee explained that the relevant question is not whether a price charged by a Respondent approximates a day-ahead market index price, as Mr. Taylor assumes, but rather whether a price "is

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[1288] Ex. CAT-641 at 5:12-8:5. *See also* Ex. TRC-64 at 2; Tr. 826:15-23, 1002:15-17 (Lee).

[1289] Coral notes that Mr. Taylor testified that "economic duress exists when there has been an improper threat or other action that leaves a party with no reasonable alternative but to consent to a deal, even if that party would prefer to do something else. Ex. CAT-041 at 39:2-6.

[1290] *See* Ex. SNA-20; Ex. CAT-415.

[1291] Ex. CAT-161 at 76, Table II-6; *see also* Tr. 2672:3-11 (Taylor).

[1292] Tr. 1050:19-24 (Lee).

within the range that CERS was transacting on in this hour."[1293] Coral notes that the California Parties provided no evidence that CERS traders ever compared the real-time offers it received to a day-ahead index price.

1127. Coral further argues that Mr. Taylor's price screen has no connection to the facts from Coral's perspective. Coral states that its purchase costs for energy it later sold to CERS would trip Mr. Taylor's screen during many hours.[1294] Thus, in order to avoid tripping Mr. Taylor's screen, Coral would have had to sell to CERS at a loss or not sell to CERS at all. Moreover, Coral notes that its traders would not have known at the time that they were selling above Mr. Taylor's benchmark.

1128. With respect to Mr. Taylor's assertion that sellers to Coral raised prices because they knew Coral was selling to CERS, Coral contends that Mr. Taylor conceded that he had presented no evidence of this.[1295] Additionally, Coral argues that Mr. Taylor's claim that Coral's full profits aren't reflected in the "back-to-back" transaction margin is confined to only 18 of 1,703 "back-to-back" sales to CERS.[1296]

1129. Lastly, Coral avers that the California Parties' evidence of fraud also does not meet Mr. Taylor's definition. Coral first notes that Mr. Taylor does not claim that the withdrawn multi-party False Export allegations constitute fraud. Second, Coral states that there is no evidence that in these limited number of transactions, CERS would not have purchased the energy if it knew of Coral's upstream transactions. Third, Coral asserts that CERS requested additional energy from Coral at COB and Coral's upstream transactions enabled those additional sales.[1297] Fourth, Coral contends that its sales at COB benefited CERS because transactions made additional power available to CERS where it was needed.

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[1293] Tr. 1046:25, 1051:22-1052:23 (Lee). *See* Tr. 2446:15-25 (Taylor).

[1294] Tr. 2617:13-2629:13 (Taylor).

[1295] Tr. 2620:5-17 (Taylor).

[1296] Tr. 2623:16-2624:10, 3018:16-3019:13 (Taylor).

[1297] Ex. SNA-39; Ex. SNA-40. Coral states that on at least one occasion not involving Coral, the ISO specifically requested that CERS schedule power in a similar fashion. Tr. 916:16-917:14 (Lee).

### (c) Allegations of Undue Price Discrimination

1130. Coral argues that the California Parties' claims of undue price discrimination are flawed because CERS was not "similarly situated" to any other counterparty and Dr. Fox-Penner's analysis is insufficient to prove undue discrimination. Coral states that its offers to CERS were legitimate, consistent with market prices, and included a risk premium to account for the considerable uncertainty surrounding CERS's creditworthiness and the regulatory environment.

1131. Coral states that the Commission has determined that "discrimination is undue when there is a difference in rates or services among similarly situated customers that is not justified by some legitimate factor."[1298] Thus, "differences in rates are justified where they are predicated on differences in facts—costs of service or otherwise."[1299] Coral notes that the FPA does not prohibit discrimination; it only prohibits an "unreasonable difference in rates" or an "undue preference or advantage"[1300] and the Commission has held that "[d]issimilar treatment of dissimilar resources does not in and of itself constitute undue discrimination."[1301] Coral asserts if the complainant demonstrates both that the rates are different and that the two classes of customers are

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[1298] *Cal. Indep. Sys. Operator Corp.*, 132 FERC ¶ 61,148, at P 40 (2010); *see also W. Grid. Dev., LLC*, 133 FERC ¶ 61,029, at P 17 (2010).

[1299] *St. Michaels Utils. Comm'n v. FPC*, 377 F.2d 912, 915 (4th Cir. 1967). *See also Ark. Elec. Energy Consumers v. FERC*, 290 F.3d 362, 367 (D.C. Cir. 2002); *Cities of Newark, New Castle & Seaford v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985); *Frankfort v. FERC*, 678 F.2d 699, 706 (7th Cir. 1982).

[1300] *Elec. Consumers Res. Council v. FERC*, 747 F.2d 1511, 1515 (D.C. Cir. 1984); *"Complex" Consol. Edison Co. of N.Y. v. FERC*, 165 F.3d 992, 1012-13 (D.C. Cir. 1999).

[1301] *Sw. Power Pool Inc.*, 127 FERC ¶ 61,283, at P 29 (2009); *Cal. Indep. Sys. Operator Corp.*, 131 FERC ¶ 61,087, at P 43 (2010).

similarly situated,[1302] the respondent may still justify the different effects by "offering a valid reason for the disparity."[1303]

1132. Coral states that in determining whether there has been undue discrimination, "[i]f the costs of providing service to one group are different from the costs of serving the other, the two groups are in one important respect quite dissimilar."[1304] Coral further notes that the Commission has specifically found that market participants may be treated differently based on their "differing levels of risk."[1305] Coral states that the Commission has indicated that using a broad range of creditworthiness standards to evaluate a potential counterparty does not violate the section 206 prohibition of undue discrimination. Coral asserts that these standards include a broad range of qualitative and quantitative factors.[1306]

1133. Coral contends that CERS was an unknown buyer and not similarly situated to Coral's other purchasers. Coral notes that Dr. Fox-Penner admitted that "CERS was a uniquely situated entity in the whole WECC."[1307] Coral describes the unique circumstances surrounding the creation of CERS, including the default of the California IOUs, ongoing regulatory proceedings, and a proposal by the California Governor to

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[1302] *Transmission Agency of N. Cal. v. FERC*, 628 F.3d 538, 549 (D.C. Cir. 2010); *Sw. Elec. Coop., Inc. v. FERC*, 347 F.3d 975, 981 (D.C. Cir. 2003); *Wash. Water & Power Co. v. FERC*, 201 F.3d 497, 504 (D.C. Cir. 2000); *Buckeye Power, Inc. v. Am. Transmission Sys., Inc.*, 142 FERC ¶ 63,007, at P 583 (2013).

[1303] *Elec. Consumers Res. Council*, 747 F.2d at 1515.

[1304] *Ala. Elec. Coop., Inc. v. FERC*, 684 F.2d 20, 27-28 (D.C. Cir. 1982).

[1305] *PJM Interconnection, LLC*, 136 FERC ¶ 61,190, at P 120 (2011); *see also N. Natural Gas Co.*, 103 FERC ¶ 61,276, at P 29 (2003).

[1306] *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186, at PP 13-15 (2004).

[1307] Tr. 1245:18-1246:4 (Fox-Penner).

seize power plants using the state's eminent domain authority.[1308] Coral states that in this environment, CERS quickly became the largest buyer of power in the world.[1309]

1134. Coral asserts that in January 2001, when prices were the highest and Coral made forty percent of its challenged sales,[1310] CERS was a brand new entity with no balance sheets, no income statements, no transaction history, no credit ratings, and none of the information that a market participant would typically look to in order to evaluate a counterparty's creditworthiness.[1311] Coral notes that CERS had an initial appropriation of $400 million, but no guarantee that additional funds would be allocated,[1312] and CERS's purchases were explicitly denied the full faith and credit of the State of California.[1313]

1135. Coral avers that the record demonstrates that many market participants saw CERS as a unique credit risk and that CERS fully understood how it was perceived.[1314] Coral concludes that this preponderance of evidence demonstrates that market participants, including Coral, did not view CERS as "similarly situated" to any other purchaser they had ever dealt with, and CERS was aware of this perception. Coral argues that the perception of CERS as a uniquely risky counterparty justified charging a significant risk premium on sales to CERS, particularly early in CERS's purchasing history.[1315]

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[1308] CAT-012 at 8:3-5; *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 94 FERC ¶ 61,132, at 61,507-10 (2001); Tr. 682:2-5 (Hart).

[1309] Ex. CAT-012 at 7:4-5.

[1310] Ex. SNA-44; Ex. CAT-041 at 22, Figure II-3; Ex. CAT-040 at J-5.

[1311] Ex. SNA-1 at 6:1-11, 10:1-5.

[1312] *See* Ex. SNA-6.

[1313] Ex. CAT-014; Ex. CAT-015.

[1314] *See, e.g.*, Tr. 610:10-18, 712:17-715:5 (Hart); Tr. 829:24-830:11, 931:12-14 (Lee); Ex. CAT-016; Ex. CAT-170; Ex. CAT-272 at 15:14-20; Ex. CAT-279; Ex. CAT-280; Ex. CAT-415; Ex. SNA-6; Ex. SNA-8; Ex. SNA-12 at 1-3; Ex. SNA-25; Ex. TRC-25; Ex. TRC-26; Ex. TRC-29; Ex. TRC-36 at P 6; Ex. TRC-37; Ex. TRC-131 at 1-2; Ex. TRC-134; Ex. TRC-141; Ex. TRC-161.

[1315] *See* Ex. TRC-1 at 48:10-49:15.

1136. Coral contends that Dr. Fox-Penner ignored this evidence of the perceived risk in selling to CERS, estimating that the risk premium was less than one dollar per MWh.[1316] Coral argues that Dr. Fox-Penner's after-the-fact risk assessment is irrelevant and that the perception of CERS at the time is the only thing that matters.[1317] Coral further notes that Trial Staff witness Dr. Savitski stated that sellers' "decisions based on their estimates of CERS's risk *at the time* have to be given great weight" and that "[i]t is inappropriate to view risky decisions made at the time from today's riskless historical perspective, just as it is inappropriate to say insurance was a waste of money last year as there was no accident."[1318]

1137. Coral avers that accurately determining the "appropriate" risk premium that sellers should have applied to CERS must be done in the context of what sellers knew at the time. Coral contends that Dr. Fox-Penner's analysis includes information that sellers could not have known when they were making decisions.[1319] Coral notes that each seller had to independently estimate the degree of credit and litigation risk entailed in selling to CERS.[1320] Coral states that the uncertainty was driven by the lack of information about CERS, which was particularly opaque to market participants at the start of the CERS Period.

1138. Coral notes that Dr. Fox-Penner asserts that CERS was similarly situated to other buyers because the "essential aspect of being similarly situated is that the products and services obtained are similar … and that the differences in costs of supplying the two groups (if any) are insufficient to explain the differences in prices."[1321] Coral argues that Professor Hogan rebutted this assumption, stating "the economic content of the electricity can be quite different if the perceived counterparty risks differ among market participants."[1322] With respect to Coral's views at the time, Coral notes that Ms.

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[1316] Ex. CAT-161 at 6:1-3.

[1317] Ex. SNA-9 at 31:7-10; *see also* Tr. 3785:2-14 (Morris).

[1318] Ex. S-13 at 30:17-21.

[1319] *See, e.g.*, Ex. TRC-1 at 38:17-18.

[1320] Ex.PNR-1 at 22:4-13.

[1321] Ex. CAT-413 at 28:3-9.

[1322] Ex. PNR-1 at 16:4-17:2.

Bowman testified that "Coral viewed CERS as a counterparty, and California as a market, to be particularly high risk."[1323]

1139. Coral states that in addition to risk of non-payment, there were regulatory risks, including ongoing Commission proceedings, a requirement by the CPUC that the IOUs cooperate in pursuing refunds, a proposal at the California legislature to institute a windfall profits tax, and a concern that CDWR would exercise its authority to find prices unreasonable and decline to pay for CERS's purchases.[1324] Coral notes that some of these perceived risks, such as Commission proceedings, have in fact been realized.

1140. Coral argues that Dr. Fox-Penner wrongly relies on the ten percent credit adder the Commission approved for sales to the ISO made after June 19, 2001.[1325] Coral notes that the adder applied prospectively, after price caps were instituted and the crisis had subsided.[1326] Moreover, Coral states that Dr. Berry conceded that the ten percent adder was a result of settlement discussions and not a finding of fact.[1327] Coral asserts that the Commission's orders also demonstrate that its determination was specific to the circumstances of sales in the CalPX and ISO markets and has no relevance as to sellers' reasonable perceptions of CERS's creditworthiness.[1328] Furthermore, Coral notes that

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[1323] Ex. SNA-1 at 9:13-14.

[1324] Ex. SNA-1 at 11:18-13:12. In addition, Mr. Hart testified that during the relevant period the CEO of the largest Pacific Northwest seller to CERS expressed concern to him about CERS seeking refunds for its contemporaneous purchases. Tr. 720:10-721:3 (Hart).

[1325] Ex. CAT-413 at 43:1-44:5.

[1326] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,519 (2001); *see also San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,211 (2001).

[1327] Tr. 1661:23-1662:2 (Berry).

[1328] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,519 (2001); *see also San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,211 (2001).

unlike the bilateral market of the Pacific Northwest, in the ISO markets "credit is *collectively* extended" and risk is pooled among all market participants."[1329]

1141. Next, Coral argues that Dr. Fox-Penner's analysis is subjective and provides no basis for finding a violation under the Federal Power Act. Coral avers that Dr. Fox-Penner's $50/MWh benchmark is entirely subjective and has no support in Commission precedent or economic texts. Coral notes that the Commission has never found undue price discrimination in a competitive spot market.

1142. Coral states that even accepting Dr. Fox-Penner's matching analysis, nearly half of his undue discrimination findings directed against Coral are not based on matched transactions.[1330] Coral contends that Dr. Fox-Penner provides little explanation for finding undue discrimination in non-matching hours.[1331] Coral states that the likely reason for most of these findings is that Dr. Fox-Penner detected a "visible pattern" in Coral's pricing and discerned the "nature of that pattern."[1332] However, Coral asserts that Dr. Fox-Penner does not explain anything about this supposed pattern.

1143. Coral also avers that Dr. Fox-Penner's "matching analysis" improperly assumes "that each of the Respondents obtained their power from a portfolio of sources."[1333] Coral asserts that this assumption is critical to Dr. Fox-Penner's analysis because it allows Dr. Fox-Penner to assume that the only possible cost differences are related to credit risk and volume.[1334] However, Coral states that its transactions with CERS were not from a portfolio of resources, but through "back-to-back" transactions.[1335] Coral

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[1329] *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186, at P 17 (2004) (emphasis added); *accord Final Rule: Credit Reforms in Organized Wholesale Electric Markets*, 133 FERC ¶ 61,060, at P 32 (2010). *See also* Ex. PNR-1 at 16:15-19.

[1330] Dr. Fox-Penner finds matches in 311 hours but declares that Coral's sales to CERS were unduly discriminatory in 595 hours. Ex. CAT-163 at 19.

[1331] Ex. CAT-161 at 71:11-14.

[1332] *Id.* at 70:1-2.

[1333] Tr. 1277:8-16 (Fox-Penner).

[1334] Ex. CAT-161 at 5:18-20. Coral states that although Dr. Fox-Penner asserts that he abandoned his portfolio assumption in his Rebuttal Testimony, his analysis was virtually unchanged.

[1335] Ex. SNA-9 at 28:12-16.

states that the evidence confirms that Coral bought power from its back-to-back supplier at COB and then immediately resold that power to CERS.[1336]

1144. Coral asserts that Dr. Fox-Penner conceded that his portfolio assumption caused him to ignore Coral's costs of supplying CERS or non-CERS buyers.[1337] Coral states that because of this assumption, Coral would have had to sell energy at a loss in 177 of the 311 hours to avoid a finding of undue discrimination.[1338] Coral also contends that Dr. Fox-Penner's rationale at hearing, that Coral was selling its most costly power to CERS,[1339] contradicts his own methodology by basing his findings on Coral's costs and ignores the facts in evidence about how Coral did business.

1145. Moreover, Coral avers that power for sales to non-CERS buyers was different than the power that was sold to CERS. First, Coral states that it rarely sold to anyone at COB other than CERS, and that Dr. Fox-Penner used sales at NOB to match sales to CERS at COB.[1340] Second, Coral notes sales to CERS were significantly larger than sales to non-CERS counterparties.[1341] Coral states that the fact that the sales to CERS were larger also confirms that Coral did not "route" expensive purchases to CERS because such "routing" would have been at odds with the actual demand from buyers in the market.

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[1336] Ex. CAT-413 at 66:4-8 ("[Coral] assert[s] that all of the transactions with CERS were 'back-to-back' sales that involved a Day-of market purchase at a specific location (*e.g.*, COB, NOB) and a *near simultaneous* sale of the identical product to CERS at a higher price. *My examination of the trading data confirmed this description* …." (emphasis added)). *See also* Ex. SNA-1 at 5:18-19; Tr. 2644:7-8 (Taylor); Ex. CAT-356; Ex. CAT-358; Ex. CAT-360; Ex. CAT-362; Ex. CAT-366; Ex. CAT-462; Ex. CAT-464.

[1337] Tr. 1306:11-1307:1, 1328:8-12 (Fox-Penner).

[1338] *See* Ex. SNA-33; Ex. SNA-34; Ex. SNA-36; Ex. CAT-163 at 19; Tr. 1384:11-1399:22 (Fox-Penner).

[1339] Tr. 1399:10-18 (Fox-Penner).

[1340] Ex. SNA-33; Tr. 3979:6-10 (Tranen); Ex. CAT-669 at 7-11; Ex.CAT-674 at 6-9; Ex. SNA-32; Ex. SNA-30; Ex. SNA-31; CAT-237 at 5:19-22.

[1341] Tr. 1370:11-24, 1374:8-11 (Fox-Penner) (testifying that the average hourly volume Coral sold to CERS was approximately 300 MWh and the average volume sold to non-CERS buyers was 28 MWh).

1146. Next, Coral discusses Mr. Taylor's claim that many of Coral's "back-to-back" transactions were not "back-to-back."[1342] Coral states that Mr. Taylor conceded that he has provided evidence of only eighteen such transactions, each of which involved only a very small volume of energy.[1343] Coral states that these eighteen transactions account for less than 0.2 percent of the energy that Coral sold to CERS at COB and cannot meaningfully "affect the economics of what Coral was doing," as Mr. Taylor claims.[1344]

1147. Coral states that Mr. Tranen further studied Mr. Taylor's contention and determined that there were only thirty instances where Coral sold a quantity of power at NOB to a particular party, immediately purchased the same quantity of energy from the same party at COB, and then sold that same quantity of energy to CERS at COB.[1345] Coral states that Mr. Tranen also found approximately one hundred instances of the same pattern, but where the volumes did not match. Coral asserts that even assuming that each of these non-matched sets of transactions was coordinated (and there is no evidence that even one of these sets of transactions with unmatched volumes was coordinated), the transactions involved only 1.3 percent of the energy that Coral sold to CERS.[1346]

1148. Lastly, Coral states that a comparison of Coral's margins between sales to CERS and sales to non-CERS counterparties provides no basis for concluding that Coral engaged in undue price discrimination.[1347] Coral asserts that ninety percent of the 1,900 day-ahead back-to-back transactions with non-CERS parties involved the City of Glendale, which had a long-term marketing agreement with Coral.[1348] The remainder included the City of Colton, which also had an asset management agreement with Coral. Coral states that Colton and Glendale were business partners of Coral and were not

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[1342] Tr. 2637:8-14, 2993:22-2994:12 (Taylor).

[1343] Tr. 3019:8-13 (Taylor). However, Mr. Tranen identified nineteen transactions in exhibit SNA-13.

[1344] Ex. CAT-104 (totaling 313 MWh).

[1345] Tr. 3961:22-3962:13 (Tranen).

[1346] Tr. 3985:10-16, 3986:7-15 (Tranen).

[1347] Ex. CAT-413 at 67-68.

[1348] Coral received an average margin of 40 cents on these transactions. Ex. CAT-413 at 66 Table 4, 68. More than one-quarter of the transactions had no margins whatsoever. Ex. SNA-31.

"similarly situated" to CERS or any other market participant. Coral further notes that Dr. Fox-Penner conceded that he made no investigation of why the margins on these transactions were so small and suggested that they could have been sleeve transactions.[1349]

1149. Additionally, Coral that notes although forty percent of its sales to CERS occurred in the first two weeks of the CERS Period, Coral sold energy throughout the entire CERS Period.[1350] Coral asserts that Dr. Fox-Penner compares the margins associated with sales to CERS to the margins on transactions with non-CERS buyers over only a 46-day span, most of which occurred on just five days.[1351] Coral contends that the limited data set cannot prove that Coral "consistently singled out CERS."[1352] Moreover, Coral avers that this methodology—comparing *all* of Coral's margins on its sales to CERS to *all* of the margins Coral achieved in transactions with non-CERS buyers—falls short of Dr. Fox-Penner's standard of "reaching an individual conclusion regarding each transaction."[1353]

### (d) Allegations of False Export

1150. Coral states that the California Parties identify False Exports as hours in which the City of Glendale or Coral exported power from California in the same hour as a Coral sale to CERS at COB. Coral first notes that the California Parties wrongly attempt to analogize these transactions to the transactions that the Commission previously condemned as false imports.[1354] Coral states that unlike the transactions at issue in this proceeding, the Commission's false import violation was premised on a supplier evading a Commission-approved price cap.[1355] Coral further notes that the Commission

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[1349] Tr. 1345:4-8, 1359:1-11 (Fox-Penner).

[1350] Ex. SNA-44 (showing Coral made $35.6 million in sales to CERS in January out of its $84.7 million total sales, or 42 percent in January).

[1351] Ex. SNA-31.

[1352] Ex. CAT-413 at 67:19-20.

[1353] Ex. CAT-161 at 7:15.

[1354] Ex. CAT-041 at 87:15-21.

[1355] *Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at P 39 (2003). Tr. 2571:7-9 (Taylor).

specifically rejected the California Parties' argument that it should investigate transactions that did not exceed the price cap.[1356]

1151. Next, Coral states that even if Mr. Taylor's False Export allegations raised any issue of tariff compliance, they would not be relevant because they did not directly affect contract negotiations. Coral states that in the Order on Remand, the Commission instructed that complainants "must demonstrate that a particular seller engaged in unlawful market activity in the spot market and that such unlawful activity *directly affected* the particular contract or contracts to which the seller was a party."[1357] Coral avers that the only evidence that False Exports raised prices to CERS is a study, which is not in the record, concerning transactions in the California auction markets during the summer of 2000.[1358]

1152. Coral also argues that Mr. Taylor's False Export analysis relies on the following unsupported assumptions: (1) exports and real-time sales to CERS are related;[1359] (2) all exports by the City of Glendale were coordinated by Coral; (3) all exports were fictitious exports of energy that were then "parked" with Coral's eventual real-time "back-to-back" supplier;[1360] and (4) all parked energy was transferred in real-time back to Coral for a sale to CERS.[1361] Coral notes that Mr. Taylor relies on two Coral documents to support his assumptions:[1362] (1) an email that describes a transaction that Mr. Taylor conceded did not meet his definition of a False Export[1363] and (2) a "brainstorming" document written

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[1356] *Am. Elec. Power Serv. Corp.*, 106 FERC ¶ 61,020, at P 88 (2004).

[1357] Order on Remand at P 21 (emphasis added).

[1358] Tr. 2613:18-2615:6 (Taylor).

[1359] Tr. 2596:19-2597:6 (Taylor).

[1360] At hearing, Mr. Taylor suggested that instead of assuming that energy was parked day-ahead with Coral's supplier, he can instead assume both that the day-ahead export was parked with any counterparty in the Pacific Northwest and that the parked energy was later sold to Coral's eventual supplier. Coral states that Mr. Taylor's alternative requires an additional assumption.

[1361] Ex. SNA-38.

[1362] Tr. 2577:4-12 (Taylor).

[1363] Ex. CAT-104; Tr. 2573:9-25 (Taylor).

during the summer of 2000.[1364] Coral asserts that neither document has any relationship to the transactions that Mr. Taylor labels as False Exports.

1153. With respect to Mr. Taylor's first assumption, that exports and sales to CERS are related, Coral states that Mr. Taylor conceded that some overlap between the hours with an export and the hours with a Coral sale to CERS is inevitable because each happened so frequently during the relevant period.[1365] Coral argues that the overlap itself is therefore not indicative of any intent by Coral.

1154. Coral also notes that Mr. Taylor argued that "the idea that you would be able to buy out of a market and sell into the market in the same hour and consistently earn a profit does not make any sense economically in a competitive market."[1366] Coral contends that this statement ignores market forces that allowed a market participant to profitably export out of the ISO and sell to CERS at COB in the same hour. Specifically, Coral states that congestion, generator availability, local demand, and credit constraints are examples of factors that would affect prices at different locations and could drive movements of power between the ISO and the Pacific Northwest.[1367] Moreover, Coral states that because the City of Glendale is itself located outside of the ISO,[1368] an import from the ISO into Glendale's system could be used to serve Glendale's own retail load.

1155. Next, Coral addresses Mr. Taylor's assumption that Coral coordinated all of Glendale's exports. Coral notes that in ninety percent of Mr. Taylor's False Export claims against Coral, Glendale was the exporter.[1369] Coral states that it marketed and scheduled some of Glendale's generation that exceeded what Glendale needed to service its own retail load,[1370] but that Glendale independently initiated and scheduled other transactions.[1371] Coral asserts that Mr. Taylor's reliance on trader tapes to justify his

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[1364] Ex. CAT-113; Tr. 2574:17-21 (Taylor); Ex. SNA-1 at 17:17-24.

[1365] Tr. 2581:9-17, 2596:22-2597:6 (Taylor).

[1366] Tr. 2581:5-8 (Taylor).

[1367] *See* Tr. 3969:5-3970:2 (Tranen).

[1368] Tr. 3990:23-3991:1 (Tranen).

[1369] Ex. SNA-9 at 14:6-13; Tr. 3960:1-3 (Tranen).

[1370] Ex. CAT-123; Ex. SNA-1 at 17:21-22.

[1371] Ex. SNA-1 at 18:1-5; *see also* Tr. 2598:18-22 (Taylor).

assumption is misplaced because those tapes are evidence only of the undisputed fact that Coral marketed some, but not necessarily all, of Glendale's excess power. Coral further notes that none of the tapes are about a transaction that Mr. Taylor has labeled a False Export.

1156. With respect to Mr. Taylor's assumption that the exports were fictitious exports of energy that were then parked, Coral states that Mr. Taylor conceded at hearing that he has no evidence of even a single instance of Coral parking power.[1372] Mr. Taylor admitted that parking is not evident from the ISO data that he used to identify exports and that he did not present any trader book data to substantiate his assumption that Coral entered into parking transactions for each False Export allegation.[1373]

1157. Coral also addresses Mr. Taylor's assumption that the exported energy was either parked with or transferred to Coral's real time back-to-back supplier. Coral again states that Mr. Taylor has provided no evidence of the transactions and simply assumes that the transactions actually happened in each instance.

1158. Lastly, Coral argues that the withdrawn allegations of False Export are not evidence for the remaining allegations. Specifically, Coral notes that Mr. Taylor initially accused Coral of 256 instances of "single-party False Exports"[1374] and an additional 19 instances of "multi-party False Exports."[1375] However, in his Rebuttal Testimony, Mr. Taylor withdrew all of his multi-party allegations and adjusted his analysis of single-party False Exports, leaving only 139 allegations against Coral.[1376]

1159. With respect to the multi-party False Exports, Coral states that Mr. Taylor admitted that before filing his Direct Testimony he failed to look at data that demonstrated that these transactions did not meet his definition of a "False Export."[1377] However, at hearing, Mr. Taylor stated that these transactions "had the same character as a False Export and they certainly reflect kind of a rebranding of the energy sourced inside

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[1372] Tr. 2600:15-2601:21 (Taylor).

[1373] Tr. 2601:22-2602:6 (Taylor).

[1374] Ex. CAT-041 at 96, Table III-2.

[1375] *Id.* at 98:18-19; *see also* Ex. SNA-13.

[1376] Ex. CAT-289 at 129-133.

[1377] Tr. 3011:3-8 (Taylor).

the ISO as energy coming from outside the ISO, but the specific issue about day-ahead versus day-of, they're no longer a day-ahead/day-of comparison."[1378] Coral contends that it is unclear how these transactions can have "the same character" as a "False Export," noting that Mr. Taylor's own testimony reveals critical differences.

1160. Coral notes that the trader tapes and transaction data introduced during Mr. Taylor's redirect examination demonstrate that the traders were discussing moving power from Glendale to NOB, and then from NOB to COB.[1379] Similarly, another call that Mr. Taylor linked to a Coral email clearly refers to power that Coral purchased from Glendale and actually transmitted north on the DC transmission line to NOB.[1380] Coral asserts that Mr. Taylor admitted that these transactions moved real power and required real transmission,[1381] and thus are not "fictitious" exports that moved no power out of the ISO.[1382] Coral further avers that these multi-party False Export transactions do indicate that any parking was involved and that Mr. Tranen found that in most of the hours there was no export out of the ISO.[1383] As Mr. Tranen explained, the City of Glendale is outside the ISO control area, so energy generated by Glendale could not have been part of a False Export.[1384]

#### (e) Allegations that Respondents Exercised Market Power

1161. Coral states that the California Parties do not specifically allege that Coral possessed or exercised market power. However, Coral notes that Dr. Reynolds stated that Coral realized higher prices for larger quantities; a result he asserted "is consistent with the exercise of market power."[1385]

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[1378] Tr. 2574:12-17 (Taylor).

[1379] Ex. CAT-672; Ex. CAT-674. *See also* Tr. 3009:17-22 (Taylor).

[1380] Ex. CAT-671 at 2:9-2:24; Ex. CAT-104.

[1381] Tr. 2993:17-19, 3012:13-16, 3015:13-16, 3018:12-15 (Taylor).

[1382] Ex. CAT-041 at 87-88.

[1383] Ex. SNA-9 at 15:1-15.

[1384] Tr. 3989:22-24, 3990:23-3991:1 (Tranen); Ex. CAT-041 at 87:13-15.

[1385] Ex. CAT-631 at 2-6.

1162. Coral asserts that Dr. Reynolds does not present any analyses specific to Coral that are typically used by the antitrust enforcement agencies or the Commission to demonstrate market power.[1386] Coral states that the only analysis provided by Dr. Reynolds is an hour-by-hour market concentration calculation for sellers that actually sold to CERS in a given hour.[1387] Coral avers that calculating market share in this manner is not a commonly accepted analysis and does not demonstrate that Coral possessed market power in the Pacific Northwest spot market.[1388] Coral further notes that Dr. Reynolds did not use the analyses that the Commission employs to analyze horizontal market power: the wholesale market share screen and the pivotal supplier screen.[1389]

1163. Coral also asserts that Dr. Reynolds' econometric analysis did not account for Coral's business practices or costs. Thus, Coral concludes that Dr. Reynolds' claim that "Coral realized higher prices for larger quantities sold" to CERS is irrelevant to any claim that Coral possessed market power.

1164. Next, Coral addresses Dr. Reynolds' assertion that a proper market power analysis was unnecessary because he had "direct evidence of harm to competition."[1390] Coral contends that Dr. Reynolds' agglomeration theory is inapplicable to Coral since Coral

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[1386] Ex. TAE-54 (DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES (2010)); Tr. 1835:17-1836:19 (Reynolds); *Inquiry Concerning the Commission's Merger Policy under the Federal Power Act: Policy Statement*, Order 592, 77 FERC ¶ 61,263 (1996); *Analysis of Horizontal Market Power under the Federal Power Act*, 138 FERC ¶ 61,109, at PP 4, 36-39 (2012).

[1387] Tr. 1812:21-23 (Reynolds).

[1388] Tr. 1839:12-1840:2 (Reynolds).

[1389] Tr. 1838:8-13 (Reynolds); *see also Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Pub. Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252, at PP 34-35, *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 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), *aff'd sub nom. Mont. Consumer Counsel v. FERC*, 659 F.3d 910 (9th Cir. 2011); *see Analysis of Horizontal Market Power under the Federal Power Act*, 138 FERC ¶ 61,109, at PP 6, 57 (2012).

[1390] Ex. CAT-631 at 27:12-15.

sold to CERS in back-to-back transactions,[1391] noting that Dr. Reynolds conceded at hearing that Coral could not have used an "agglomeration" strategy.[1392]

1165. Lastly, Coral states that Dr. Reynolds ignored Coral's costs as a possible explanation for why there were higher prices associated with larger volumes. Coral notes that Dr. Reynolds conceded that he did not analyze Coral's costs of purchasing power, nor did he analyze whether Coral's profits were higher when it sold larger volumes to CERS.[1393]

#### (f) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1166. Coral argues that the California Parties' have not alleged that Coral engaged in "such extensive unlawful market manipulation as to alter the playing field for contract negotiations."[1394] Coral notes that the only allegation of market manipulation is Mr. Taylor's False Export allegations, which represent less than two percent of the volume of energy Coral sold to CERS and just fifteen percent of the total hours.[1395]

1167. Coral also contends that the California Parties failed to connect their allegations of wrongdoing to specific bilateral contracts. Coral asserts that Mr. Taylor's databases misidentify the contracts between Coral and CERS and misapply both the evidence and the California Parties' own allegations. Coral further notes that the documents cited in the databases are often not relevant to specific contracts.

1168. Coral avers that Mr. Taylor's databases adopt the delineation of hourly sales put forward by Ms. Lee in her transaction records.[1396] Coral notes that Ms. Lee admitted that the transaction records, most of which were made weeks after the contracts were formed

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[1391] Tr. 1841:13-16 (Reynolds).

[1392] Tr. 1842:21-1843:5 (Reynolds).

[1393] Tr. 1831:23-1834:2 (Reynolds).

[1394] Order on Remand at P 20.

[1395] Ex. CAT-289 at 131, Table V-2; Ex. CAT-415; Ex. CAT-161 at 76, Table II-6.

[1396] Tr. 2551:17-20 (Taylor).

and by someone other than the CERS trader who entered into the transaction,[1397] were never intended to identify contracts.[1398] Moreover, Coral contends that Mr. Taylor ignored Coral's contemporaneous records that were intended to track contracts[1399] and misunderstood the difference between Ms. Lee's records and Coral's records.[1400] Coral notes that Mr. Tranen found that in the vast majority of cases, Coral's deal numbers capture different hourly sales than Ms. Lee's records.[1401]

1169. Furthermore, Coral asserts that Mr. Taylor's database for Coral contains unreliable and inaccurate information. Coral notes that at hearing, Mr. Taylor testified that the column in his database labeled "Brief Summary," which on its face appears to contain a summary of each exhibit, is a "category"[1402] and in some cases reflects the content of other exhibits.[1403] Additionally, Coral states that Mr. Taylor's database includes allegations about another supplier,[1404] factual inaccuracies,[1405] and Mr. Taylor's own speculation, which is wholly disconnected from the actual content of the exhibit.[1406]

1170. Next, Coral argues that Mr. Taylor's database does not reflect "documentary evidence relating to that [specific] contract," as Mr. Taylor claims.[1407] For example, Coral states that Mr. Taylor cites internal Coral emails from January 26, 2001 and January 27, 2001 for every Coral sale to CERS from January 26 through April 21,

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[1397] Ex. CAT-028; Tr. 899:21-25, 1019:11-22 (Lee).

[1398] Tr. 1024:25-1035:13 (Lee) (describing why the transaction records may not represent individual contracts).

[1399] Ex. SNA-1 at 5:16-18.

[1400] Ex. CAT-289 at 138:14-16.

[1401] Ex. SNA-9 at 39:7-19.

[1402] Tr. 2271:17-2722:8 (Taylor).

[1403] Tr. 2724:20-2725:10 (Taylor).

[1404] Tr. 2726:5-14 (Taylor).

[1405] Tr. 2726:18-22 (Taylor).

[1406] *See* Ex. CAT-403.

[1407] Ex. CAT-041 at 8:4.

2001.[1408] Moreover, Coral notes that Mr. Taylor cited two documents for all Coral sales from January 17 through March 31, 2001 that do not even mention Coral.[1409]

1171. Coral further avers that Mr. Taylor's database misrepresents the California Parties' own allegations. For example, Mr. Taylor lists Exhibit CAT-362, a transcript of trader conversations relevant to Coral's "back-to-back" transaction with CERS on March 13 hour-ending 4. Coral states that Mr. Taylor claims that Exhibit CAT-362 is relevant to duress and price discrimination, but no California Parties witness directs any allegation of wrongdoing for this transaction.[1410]

1172. Lastly, Coral contends that Mr. Taylor's 1(A) and 1(B) conclusions about each set of Coral sales to CERS should be given no weight. First, Coral states that because Mr. Taylor does not accurately identify specific contracts, his findings are not probative for purposes of a contract-by-contract application of the *Mobile-Sierra* presumption. Second, Coral notes that Mr. Taylor's 1(A) and 1(B) conclusions are his own legal conclusions and entitled to no weight.[1411]

### (g) Legitimate Business Behavior by Coral

1173. Coral notes that in the Order on Remand, the Commission held that "[s]ellers accused of unlawful manipulation in this case may submit evidence that the activity in question was, in fact, legitimate business behavior."[1412] The Commission explained that legitimate business behavior includes "actions consistent with appropriate behavior in a

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[1408] Ex. CAT-104. Similarly, a single Coral email from February 2, is listed as relevant to every transaction from February 2 through April 21, 2001. Ex. CAT-114. Coral notes that in Mr. Taylor's direct testimony, these emails were cited only for the days in the emails; however, in his rebuttal database, Mr. Taylor associated the emails with a larger number of transactions without explanation. Ex. CAT-155; Ex. CAT-408.

[1409] Ex. CAT-060; Ex. CAT-138.

[1410] Ex. CAT-408 at 136. Similarly, Mr. Taylor cites Exhibits CAT-348 and CAT-350, two trader conversations that ultimately resulted in no sale to CERS, as evidence of price discrimination and duress. *Id.* at 1; Tr. 2564:17-23 (Taylor).

[1411] Ex. CAT-289 at 159:1-6; Tr. 2735:21-2736:4 (Taylor); *see also* Ex. S-15 at 17:12-18:4.

[1412] Order on Remand at P 22.

competitive market, i.e., actions taken to further a firm's business objectives but not involving manipulative, illegal, or otherwise anticompetitive acts."[1413]

1174. Coral states that all of its sales to CERS were legitimate and made to further Coral's business objectives and did not involve manipulative, illegal, or otherwise anticompetitive acts. Coral notes that its offers to CERS included a minimum risk premium to account for the substantial risk that CERS would default on its payment obligations to Coral.[1414] Coral asserts that it perceived that there was a significant risk that it would lose money on sales to CERS in the event of a default given the fact that the State of California did not guarantee backing CERS's purchases. Coral avers it was also concerned about regulatory clawback.[1415] Moreover, Coral notes that because CERS was a new and unknown entity created in the midst of a crisis, Coral could only "estimate the degree of credit and litigation risk entailed in selling to CERS."[1416] Coral contends that the fact that its estimates and assumptions may have been slightly different than those of other market participants that actually sold to CERS does not render Coral's offers manipulative, illegal, or otherwise anticompetitive. Coral argues that its decision to sell to CERS was both beneficial to the California Parties and protected Coral from the possibility of a default.

### 4. Commission Trial Staff Initial Brief

#### (a) Standard of Proof and Relevant Law

1175. Commission Trial Staff (Trial Staff) states that the Order on Remand directed the Presiding Judge to determine which parties engaged in unlawful market activity without a legitimate business reason and whether that unlawful market activity directly affected the negotiation of specific bilateral contracts, including transactions involving CERS.[1417] Trial Staff notes that the Commission also found that the *Mobile-Sierra* presumption

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[1413] *Id.* P 22 n.52.

[1414] Ex. SNA-1 at 13:6-9.

[1415] Ex. SNA-1 at 11:21-13:2. Professor Hogan also notes that "default risk should include not only whether the checks are sent the week after the transaction, but also the risk of future litigation and refunds." Ex. PNR-1 at 20:15-17.

[1416] Ex. PNR-1 at 22:4-6.

[1417] Order on Remand at PP 16, 23 & 29.

generally applies to short-term bilateral contracts like those at issue in this case.[1418] Thus, "the rates set forth in those contracts are presumed just and reasonable, except where certain criteria are met, where it can be shown that one party to a contract engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations."[1419]

1176. Trial Staff asserts that the Commission's finding that the *Mobile-Sierra* presumption generally applies is consistent with the Supreme Court's ruling in *Morgan Stanley*, which found that the presumption applies to contracts entered into under market-based rate authority without any specific determination by the Commission that the rates called for in the contracts are just and reasonable.[1420] The Court also recognized at least two circumstances in which the presumption would not apply – "where there is unfair dealing at the contract formation stage—for instance, if it finds traditional grounds for the abrogation of the contract such as fraud or duress. … [and] if the 'dysfunctional' market conditions under which the contract was formed were caused by illegal action of one of the parties."[1421]

1177. With respect to a party engaging in unlawful activity, Trial Staff notes that causality must be established, such that the seller must have engaged in illegal activity in the spot market that directly affected the contracts at issue.[1422] Trial Staff states that mere imperfection or even chaos in the market, however, is not sufficient to avoid the *Mobile-Sierra* presumption.[1423] Trial Staff notes that the Commission made clear that it was not enough for complainants to simply show "a general link between the dysfunctional spot market in California and the Pacific Northwest spot market" or that the Pacific Northwest spot market was generally dysfunctional.[1424] Rather, the Commission explained that the complainants must establish that "a particular seller

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[1418] *Id*. P 20.

[1419] *Id*.

[1420] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 545-47 (2008).

[1421] *Id.* at 547, 553-54.

[1422] Order on Remand at P 21.

[1423] *Morgan Stanley*, 554 U.S at 547-48.

[1424] Order on Remand at P 21.

engaged in unlawful market activity in the spot market" which directly affected the particular contracts to which that seller was a party.[1425]

### (b) The California Parties *Mobile-Sierra* Databases

1178. Trial Staff first discusses the *Mobile-Sierra* databases compiled by Mr. Taylor. Trial Staff notes that a 1(A) designation by Mr. Taylor indicates that he found "substantial evidence" that the *Mobile-Sierra* presumption should not apply because of fraud, duress, bad faith, or unlawful market manipulation by a Respondent that affected the negotiation of a specific contract.[1426] A 1(B) designation means that Mr. Taylor found "evidence of manipulative activity that elevated prices generally in the market, thus tainting contracts negotiated in affected markets so that the prices in those contracts should be found contrary to the public interest."[1427]

1179. Trial Staff states that for 1(A) designations of fraud, duress, or bad faith, Mr. Taylor looked for two things: "a discernible price impact with respect to each specific contract and the "weakened position of the buyer."[1428] For 1(B) designations, Mr. Taylor looked for manipulative activity, specifically in the form of False Export and selling non-firm energy as firm.[1429] Finally, for a both 1(A) and 1(B) designation, Mr. Taylor looked for fraud, duress, or bad faith, and price impact, or manipulation on the price impact, or price discrimination.[1430]

1180. Trial Staff asserts that Mr. Taylor's designations do not correspond to the identification of 1(A) and 1(B) issues in the Joint Statement of Issues. As discussed above, Trial Staff states that Issue 1(A) requires the California Parties to establish that "a particular seller engaged in unlawful market activity in the spot market" which directly affected the particular contracts to which that seller was a party.[1431] Trial Staff contends

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[1425] *Id*.

[1426] Ex. CAT-289 at 159:1-3.

[1427] *Id.* at 159:4-6.

[1428] Tr. 2943:9-13 (Taylor).

[1429] Tr. 2943:14-18 (Taylor).

[1430] Tr. 2944:14-17 (Taylor).

[1431] Order on Remand at P 21.

that the for an Issue 1(A) finding, the complainant must demonstrate that a particular Respondent violated the Western Systems Power Pool Agreement (WSPP Agreement) or a provision of its applicable tariff, or otherwise engaged in unlawful market activity without a legitimate business reason.[1432] Furthermore, Trial Staff notes that Issue 1(B) states that a party to a contract could also overcome the *Mobile-Sierra* presumption by presenting evidence that a particular contract imposes an excessive burden or seriously harms the public interest.[1433] Trial Staff concludes that Mr. Taylor's databases are inconsistent with the standard set forth in the Commission's orders in this proceeding and the agreed upon Joint Statement of Issues.

1181. Next, Trail Staff argues that the documents relied upon by Mr. Taylor do not demonstrate that any particular Respondent engaged in unlawful market activity. Trial Staff notes that many of the documents listed by Mr. Taylor are merely background documents that provide context for the transactions.[1434] Trial Staff states that Mr. Taylor also cites exhibits that occurred outside of the CERS Period or that are not related to a specific transaction between the Respondents and CERS. For example, for each Respondent, Mr. Taylor cites (1) the testimonies of other California Parties' witnesses in this proceeding; (2) a memo delineating guidelines to follow when purchasing and selling energy; (3) an e-mail that discusses a reduction of CDWR's credit line without notice; and (4) the WSPP Agreement. Trial Staff acknowledges that Mr. Taylor did cite some documents that specifically relate to CERS, Coral, and TransCanada.

1182. Trial Staff also notes that Mr. Taylor changed his 1(A) and 1(B) designations in both a November 2012 Errata and in his Rebuttal Testimony. Based on these changes, Trial Staff contends that there is no way to determine if Mr. Taylor consistently applied any criteria to each contract and that Mr. Taylor's conclusions rely on subjective judgment rather than objective criteria. For example, in some instances where only a price discrimination flag is evident, Mr. Taylor will make a 1(A) designation, other times a both 1(A) and 1(B) designation, occasionally a 1(B) designation, and on occasion, even a blank label indicating no allegations. Thus, Trial Staff concludes that Mr. Taylor's designations are unreliable and do not support setting aside the *Mobile-Sierra* presumption applicable to these transactions.

### (c) Allegations of Fraud, Duress, and Bad Faith

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[1432] Order on Remand at PP 16-18, 23.

[1433] Order Granting Interlocutory Appeal at PP 12-15.

[1434] Ex. S-15 at 6.

1183. Trial Staff asserts that Mr. Taylor relies on his "common understanding" of duress, fraud, and bad faith in making his claims. Trial Staff states that although Mr. Taylor sets forth separate definitions for duress, fraud and bad faith, he does not attempt to distinguish between these allegations in his *Mobile-Sierra* databases.[1435] Trial Staff further notes that Mr. Taylor acknowledged that the consideration of these terms cannot be reduced to a formula, the activities (i.e., duress, fraud or bad faith) are defined in legal rather than economic terms, and that, ultimately, it is "the Judge that will be required to weigh all the evidence accumulated for each Respondent and Respondent's transactions at issue in this proceeding."[1436]

1184. Trial Staff argues that Mr. Taylor's subjective, general approach to his allegations of duress, fraud, or bad faith is contrary to the Commission's directive that complainants must establish that a particular seller engaged in unlawful market activity in the spot market which directly affected the particular contracts to which that seller was a party. Trial Staff avers that the lack of specific documentation that applies to CERS's contracts and transactions also applies to Mr. Taylor's allegations of duress, fraud or bad faith.

### (d) Allegations of Undue Price Discrimination

1185. Trial Staff states that undue price discrimination is prohibited by section 205(b) of the FPA,[1437] noting that the Commission has stated that "undue discrimination is in essence an unjustified difference in treatment of similarly situated customers."[1438] Trial Staff asserts that simply identifying rate disparity is not sufficient to establish undue price discrimination because "differences in rates are justified when they are predicated upon differences in facts—costs of service or otherwise."[1439] Thus, to find price discrimination in violation of the FPA, the Commission must determine that similarly situated customers are treated differently and that any difference in treatment is not justified.[1440] Trial Staff

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[1435] Tr. 2382:9-13 (Taylor).

[1436] *See* Ex. CAT-289 at 150:9-24.

[1437] 16 U.S.C. § 824d(b) (2012).

[1438] *Transwestern Pipeline Co.*, 36 FERC ¶ 61,175, at 61,433 (1986).

[1439] *St. Michaels Util. Comm'n v. FPC*, 377 F.2d 912, 915 (4th Cir. 1967); *see also*, *City of Frankfort. v. FERC*, 678 F.2d 699, 706 (7th Cir. 1982).

[1440] *Transwestern Pipeline Co.*, 36 FERC ¶ 61,175, at 61,433 (1986); *Tex. E. Transmission Corp.*, 37 FERC ¶ 61,260, at 61,709 (1986).

notes that the particular showing that is required to establish undue discrimination "will necessarily turn upon the facts of each case, including the characteristics of the customer class involved and the service requested, as well as myriad other potentially relevant factors."[1441]

1186. Trial Staff avers that in his "matching analysis," Dr. Fox-Penner failed to make the necessary showing that similarly situated customers were treated differently. Furthermore, Trial Staff states that the evidence demonstrates that the difference in treatment was justified due to reasonable credit concerns resulting from information available to the parties at the time of the transactions at issue. Trial Staff also contends that Dr. Fox-Penner's comparison to long-run and short-run marginal costs of sellers carries no weight because it is irrelevant or contrary to widely-accepted economic principles.

1187. With respect to the "matching analysis," Trial Staff notes that Dr. Fox-Penner acknowledged at least six characteristics that can vary in spot power purchases: (1) duration of the transaction; (2) day-ahead vs. day-of transactions; (3) delivery location; (4) firm vs. non-firm transactions; (5) volume of power sold; and (6) credit terms.[1442] However, Trial Staff asserts that Dr. Fox-Penner did not properly control for all of these characteristics.

1188. First, Trial Staff avers that Dr. Fox-Penner did not properly control for the time the agreement was reached. Trial Staff notes that the hour of delivery does not reflect the hour of agreement and that energy prices were volatile during the CERS Period and could change by the hour.[1443] Second, Trial Staff asserts that Dr. Fox-Penner failed to consider the duration of the transactions. Thus, Dr. Fox-Penner could "match" a single-hour transaction with transactions for multi-hour blocks of energy.[1444] Trial Staff also notes that Dr. Fox-Penner extends his allegations of price discrimination to adjacent hours that do not have a "matching" transaction, compounding the issues with his analysis.

1189. Trial Staff asserts that Dr. Fox-Penner's analysis based on standard deviations from the average price is insufficient because it compares non-CERS daily average prices charged by all sellers with a single-hour CERS price. Trial Staff notes that both the

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[1441] *S. Cal. Edison Co.*, 46 FERC ¶ 61,052, at 61,243 (1989).

[1442] Ex. CAT-161 at 10:4-10.

[1443] Ex. TRC-1 at 30:4-14.

[1444] *See, e.g.*, Tr. 1149:6-1150:13, 1465:11-14 (Fox-Penner).

standard deviation analysis and Dr. Fox-Penner's regression analysis ignore important differences in the transactions, including credit risk and when the transaction was entered into.[1445]

1190. Next, Trial Staff contends that the California Parties failed to demonstrate that the difference in treatment of CERS, if any, was undue. Trial Staff notes that "[p]rice differences based on cost differences do not qualify as price discrimination, as higher product costs justify higher prices."[1446] Trial Staff states that Dr. Fox-Penner recognizes only two cost-based factors that could explain the difference in the prices of the allegedly identical sales: credit risk and volumetric differences.

1191. With respect to Dr. Fox-Penner's assertion that CERS was highly creditworthy, Trial Staff avers that Dr. Fox-Penner ignores the sellers' reasonable perceptions of CERS at the time of the transactions. Trial Staff notes that Dr. Morris testified that CERS was "an underfunded, unguaranteed and unknown entity."[1447] Trial Staff states that the perception that CERS was highly risky was so widespread and significant that at least twenty-two entities refused to sell to CERS.[1448] Trial Staff contends that Dr. Fox-Penner wrongly uses hindsight to show that the perceptions of credit risk were inaccurate because "[i]t is inappropriate to view risky decisions made at the time from today's riskless historical perspective, just as it is inappropriate to say insurance was a waste of money last year as there was no accident covered by the insurance."[1449] Trial Staff further argues that if Dr. Fox-Penner were correct, and there was little risk selling to CERS, then all twenty-two entities that refused to sell to CERS were irrational. Rather, Trial Staff asserts that the perception of entities at the time should be accorded greater weight than Dr. Fox-Penner's after-the-fact calculation.[1450]

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[1445] Tr. 1275:6-1276:24 (Fox-Penner).

[1446] Ex. S-13 at 28:2-4 (*citing* DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 435-51 (1990)).

[1447] Ex. TRC-1 at 31-41.

[1448] Ex. CAT-12 at 15:1-6; Ex. CAT-16; Ex. CAT-22 at 15:6-7; Ex. CAT-41 at 43:22-44:12.

[1449] Ex. S-13 at 30:16-21

[1450] Tr. 4261:2-11 (Savitski).

1192. Trial Staff also notes that the Commission allowed a ten percent adder to recognize the risk of nonpayment for the purposes of calculating refunds and mitigating prices in the centralized California spot markets.[1451] Although in a different context, Trial Staff notes that the ten percent adder is significantly larger than the risk premium calculated by Dr. Fox-Penner.[1452] For example, for a $500/MWh transaction, the Commission's risk premium would be more than 100 times larger than Dr. Fox-Penner's premium of $0.46/MWh.

1193. Next, Trial Staff contends that Dr. Fox-Penner's comparison to long-run and short-run marginal costs is not an appropriate measure of price discrimination. Trial Staff argues that this approach is misguided because it uses a cost-based benchmark to overcome the *Mobile-Sierra* presumption in a bilateral, market-based rate regime. Trial Staff notes that in *Morgan Stanley*, the Supreme Court specifically stated "a presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract-based regulation."[1453]

1194. Moreover, Trial Staff avers that even if costs are used as a benchmark, Dr. Fox-Penner's analysis is flawed. First, Trial Staff argues that long-run marginal costs are irrelevant because market entry is not the mechanism that set prices during the CERS Period.[1454] Trial Staff notes that the CERS Period lasted approximately 155 days—too short for new generation to be planned, permitted, and built based on prices observed during that period.[1455] Trial Staff states that Dr. Fox-Penner's "profitability calculation"[1456] is wrongly limited to the 155 day period and is too narrow because (1) it assumes that the hypothetical CT could have been built to take advantage of the prices

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[1451] *San Diego Gas & Elec. Co., et al. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418, at 62,564 (2001), *aff'd*, 97 FERC ¶ 61,275, at 62,209-10 (2001); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs., et al*., 96 FERC ¶ 61,120, at 61,519 (2001), *aff'd*, 97 FERC ¶ 61,275, at 62,211 (2001).

[1452] Ex. S-13 at 30:21-31:1

[1453] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[1454] Ex. S-13 at 21:16-20.

[1455] Ex. S-5 at 31:6-17; Ex. S-12; Tr. 1537:12-1538:5 (Fox-Penner).

[1456] The profitability calculation measures the margins earned by a hypothetical combustion turbine (CT) compared to its annual capital carrying costs.

during the CERS Period and (2) it ignores the risk of offsetting losses that the hypothetical CT could incur outside of the CERS Period. Trial Staff concludes that the calculation is flawed because it observes a long-term investment in a short-term time frame.[1457]

1195. Second, Trial Staff asserts that the use of short-run marginal costs ignores the realities of the Pacific Northwest market and misapplies economic principles. Trial Staff states that the Commission specifically stated that the approach used to calculate refunds for the California markets would not be appropriate here.[1458] Specifically, Trial Staff notes that the Pacific Northwest did not have an organized market with a single market clearing price and that sellers could not predict the precise market clearing price because the market was not transparent.[1459]

1196. Third, Trial Staff contends that the use of short-run marginal costs misapplies basic economic principles because an efficient market clears at the marginal cost of the *most expensive generator needed*, not at the marginal cost of an individual seller.[1460] Trial Staff states that Dr. Fox-Penner's use of an individual seller's marginal cost to measure efficiency assumes that the seller is irrational and would offer its product at the minimum amount it would be willing to sell, rather than its reasonable estimates of the market clearing price.[1461] Applying this reasoning to CERS, Trial Staff notes that CERS should have offered to buy power at $10,000-$20,000 per MWh because that is Dr. Fox-Penner's calculation of the value of avoiding a power outage.[1462] Moreover, Trial Staff states that if a generator always sold at its short-run marginal cost, it would never recover its fixed costs, including a return of and on its investment.[1463]

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[1457] Ex. TRC-1 at 112:4-113:17; Ex. PNR-1 at 30:7-32:3.

[1458] Order on Remand at P 24.

[1459] Ex. PNR-1 at 14-21-15:18.

[1460] Ex. S-13 at 24:20-25:3; Ex. PNR-1 at 13:8-19; Ex. TAE-8 at 36:15-37:15 (citing ROBERT S. PINDYCK & DANIEL L. RUBINFELD, MICROECONOMICS 267 (6th ed. 2005)).

[1461] Ex. S-13 at 25:3-9.

[1462] Ex. S-13 at 25:19-26:5 (citing Ex. CAT-161 at 84:1-87:7).

[1463] Ex. S-13 at 23:20-22; Ex. PNR-1 at 153:15-154:20.

1197. Lastly, Trial Staff asserts that although Dr. Fox-Penner acknowledged that scarcity existed at the time, he failed to consider the effect of scarcity on the market price in the Pacific Northwest.[1464] Trial Staff states that when scarcity pricing occurs, the market clearing price ceases to be a function of the marginal cost of the marginal seller. Rather, scarce output is allocated among buyers efficiently.[1465]

### (e) Allegations of False Export

1198. Trial Staff first notes that as Mr. Taylor acknowledged that a False Export is not the same as the Ricochet practice previously admonished by the Commission because the seller to CERS was not avoiding a price cap.[1466] Rather, Trial Staff states that sellers were arbitraging day-ahead and real-time prices. Thus, unlike a Ricochet transaction, which would raise the day-ahead and real-time prices by evading the real-time price cap, False Exports decreased the difference between the day-ahead and real-time prices by increasing the day-ahead price (by removing energy) and decreasing the real-time price (by adding energy).[1467]

1199. Trial Staff asserts that even if a False Export were a violation, Mr. Taylor's methodology to identify False Exports is flawed for the following reasons: (1) Mr. Taylor used the wrong unit of analysis; (2) Mr. Taylor's pairings of exports and imports are based on pure coincidence, rather than causation; and (3) Mr. Taylor ignores the parking element of a False Export transaction.

1200. Trial Staff contends that Mr. Taylor used the wrong unit of analysis because rather than evaluating an entire transaction, Mr. Taylor looks only at single hours. Therefore, Mr. Taylor fails to link his False Export analysis to a particular contract, as required by the Order on Remand. Trial Staff avers that examining individual hours leads to distorted results and overstates the number of trades, creating more opportunities to find the alleged manipulation.[1468] Trial Staff states that this is particularly true in the Pacific Northwest market because trades typically involved blocks of energy for light or heavy

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[1464] Ex. CAT-161 at 38:6-9.

[1465] *See* Ex. S-13 at 23:8-10.

[1466] *See* Tr. 2903:16-22 (Taylor); *Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at PP 37-38 (2003).

[1467] Ex. S-13 at 8.

[1468] Ex. S-13 at 5, 10.

load hours or 24-hour blocks. Trial Staff further notes that examining individual hours results in Mr. Taylor finding the same single contract to both include and not include a False Export.

1201. Next, Trial Staff argues that Mr. Taylor's pairings of exports and imports are based on pure coincidence. Trial Staff states that many of the exports flagged by Mr. Taylor were the result of contracts negotiated months or even years in advance.[1469] Trial Staff further notes that because Mr. Taylor constructs his analysis from two separate sources of data, export and import schedules for a given hour rather than a single transaction, he makes ad hoc adjustments to match on the basis of quantity.[1470] Trial Staff asserts that there is no way to know the extent to which the paired transactions reflect a coordinated strategy, as alleged by Mr. Taylor, or mere coincidence.

1202. Trial Staff avers that Mr. Taylor also fails to consider that False Exports impact both the day-ahead and real-time markets. Specifically, Mr. Taylor only examines the effect of reducing day-ahead supply and does not consider increasing supply in real-time. Trial Staff states that because real-time prices were in excess of day-ahead prices, competitive firms had an incentive to buy day-ahead and sell real-time, arbitraging the two markets.[1471] Trial Staff further notes that Mr. Taylor recognizes the flaws in his analysis because he describes his screen as detecting "*potential* False Export transactions."[1472]

1203. Next, Trial Staff contends that Mr. Taylor wrongly characterizes a False Export as withholding energy from the day-ahead market. Trial Staff states that this is inconsistent with the definition of withholding for two reasons. First, the energy is being offered into the market, as opposed to not being produced. Second, the transactions are consistent with the price signals because the real-time market had higher prices than the day-ahead market.

1204. Lastly, Trial Staff asserts that Mr. Taylor ignored the parking element of a False Export transaction. Trial Staff notes that although parking is a central component of a

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[1469] Ex. S-13 at 11. *See, e.g.*, Ex. AVI-1 at 15; Ex. TAE-8 at 52.

[1470] Specifically, if the quantities of the paired transactions are different, Mr. Taylor simply uses the smaller quantity.

[1471] Ex. S-13 at 13.

[1472] Ex. CAT-041 at 93 (emphasis added).

False Export,[1473] Mr. Taylor does not include it in his analysis. Trial Staff contends that without parking, the False Export screen boils down to one based on mere coincidence.

### (f) Allegations that Respondents Exercised Market Power

1205. Trial Staff notes that Dr. Reynolds alleged only that TransAlta exercised market power during the CERS Period and did not reach a conclusion regarding the other individual Respondents.[1474] As noted above, the California Parties and TransAlta have settled all remaining claims in this proceeding. However, Trial Staff also responds to the more general allegations made by the California Parties and their witnesses.

1206. Trial Staff contends that Dr. Reynolds did not apply the appropriate market power test that was used by the Commission during the CERS Period. Trial Staff states that during the CERS Period, the Commission applied the "hub-and-spoke" test and has long used a twenty percent generation market share as an indicator of potential market power.[1475] Trial Staff notes that in *Lockyer*, the Commission affirmed its rejection of the California Parties' argument that the hub-and-spoke analysis is an inappropriate market power screen for the Commission to use in that proceeding.[1476] The Commission stated that it "is required to use the standards for assessing market power of market-based rate sellers … in effect at the time the transaction took place" and that "doing otherwise would 'violate the requirement that all jurisdictional sellers be on notice as to what test will be applied to them' and would constitute the 'retroactive establishment of agency rules and tests.'"[1477] Trial Staff avers that the same rationale is applicable to this proceeding.

1207. Trial Staff asserts that Dr. Reynolds' assertion that "[t]he courts, the antitrust agencies, and antitrust scholars all agree that direct evidence is sufficient – on its own –

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[1473] Ex. CAT-041 at 88:8-12.

[1474] Ex. CAT-264 at 4:7-10.

[1475] *California ex rel. Lockyer v. British Columbia Power Exch. Corp*., 122 FERC ¶ 61,260, at P 35 n.70 (2008).

[1476] *California ex rel. Lockyer v. British Columbia Power Exch. Corp*., Opinion No. 512, 135 FERC ¶ 61,113 (2011) (*Lockyer*).

[1477] *Id*. P 39 (quoting *California ex rel. Lockyer v. British Columbia Power Exch. Corp*., 125 FERC ¶ 61,016, at P 30 (2008)).

to show market power"[1478] is not controlling in this proceeding. Trial Staff notes Dr. Reynolds does not specifically cite to court cases, but refers to "actual behavior of the antitrust agencies."[1479] Trial Staff states that in deciding not to modify the current market power analysis utilized for electric market-based rate applications to reflect the revised Horizontal Merger Guidelines issued by the U.S. Department of Justice and the Federal Trade Commission,[1480] the Commission stated that its "market-based rate analysis is not explicitly tied to the Antitrust Agencies' merger guidelines."[1481]

1208. Next, Trial Staff argues that Dr. Reynolds' tests suffer from other significant flaws. Trial Staff avers that Dr. Reynolds defines the product and geographic markets too narrowly and, thus, excludes obvious alternatives that bias the analyses in favor of finding market power. Trial Staff states that Dr. Reynolds' logic for defining the product as the day-ahead and day-of energy markets also applies to a broader range of products, such as the multi-day, balance-of-month, and forward markets.[1482] Similarly, Trial Staff contends that Dr. Reynolds' construction of a market concentration, based on real-time trades, is similarly flawed because it does not allow for substitution opportunities. For example, the fact that CERS bought energy day-ahead demonstrates that day-ahead energy is a substitute for real-time energy, and thus should be included in the product market, along with balance-of-month, forward products, and exchanges.

1209. With respect to the geographic market, Trial Staff asserts that Dr. Reynolds ignores trades at locations other than COB and NOB, even though they are clearly alternative locations at which to buy energy and in the relevant market. Trial Staff states that the fact that CERS may have limited its purchases to COB and NOB is immaterial as long as CERS has access to energy at different locations.[1483]

1210. Lastly, Trial Staff contends that Dr. Reynolds' regression analyses fail to properly model price and quantity. First, Trial Staff notes that the analyses have dependent

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[1478] Ex. CAT-631 at 40:4-5.

[1479] *Id*. at 7.

[1480] Ex. TAE-54.

[1481] *Analysis of Horizontal Market Power under the Federal Power Act*, 138 FERC ¶ 61,109, at P 55 (2012).

[1482] Ex. S-13 at 36.

[1483] Ex. S-13 at 37.

variables as explanatory variables, which lead to biased results.[1484] Trial Staff states that Dr. Reynolds should have conducted a simultaneous equations model to account for this problem. Second, Trial Staff argues that Dr. Reynolds' CERS baseline regression is not for any particular seller, and thus, fails to show a relationship between an individual seller's transactions and the price charged to CERS.[1485] Third, Trial Staff avers that the results for CAISO-declared stage emergency conditions are inconsistent with the California Parties' contention that CERS was subject to extreme market power in the real-time market. Trial Staff states that if this were true, emergency conditions would signal the sellers that the market is tight and they have even more market power with which to demand higher prices. However, Dr. Reynolds finds the emergency variables are statistically significant only four out of six times at five percent or better.[1486] Fourth, Trial Staff notes that Dr. Reynolds' analysis is conducted using hourly observations, rather than full transactions.

### 5. <u>The California Parties Reply Brief</u>

#### (a) Allegations of Fraud, Duress, and Bad Faith

1211. The California Parties first address Coral's argument that issues of duress, fraud, and bad faith are outside the scope of this proceeding. The California Parties contend that Coral fundamentally misinterprets Commission orders. The California Parties state that Commission made clear that the Order on Remand was "not intended to alter the general state of law, as summarized in *Morgan Stanley*."[1487] The California Parties assert that *Morgan Stanley* permits the Commission to consider challenges to the *Mobile-Sierra* presumption based on the traditional contract grounds of duress, fraud, or bad faith.[1488]

1212. With respect to Coral's claim that the Commission defers contract issues to courts, the California Parties assert that the question to be determined in this proceeding is whether the *Mobile-Sierra* presumption applies at all and claims of duress, fraud, or bad

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[1484] Ex. S-13 at 37-38 (citing Ex. TAE-18 at 3-15).

[1485] Ex. S-13 at 38.

[1486] Ex. CAT-264 at 12-16.

[1487] Order Granting Interlocutory Appeal at P 13.

[1488] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008) (citing *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at 62,399-400 (2003)).

faith are central to this question. The California Parties note that although the Commission is reluctant to resolve state contract law issues unless it is necessary to do so,[1489] challenges to contracts subject to the *Mobile-Sierra* presumption sometimes involve contract formation issues that the Commission must resolve, along with other claims that would justify avoiding the *Mobile-Sierra* presumption.[1490] The California Parties also note that most of the cases upon which Coral relies involve contract interpretation (not contract formation) and do not involve a *Mobile-Sierra* challenge. Moreover, the California Parties state that its litigation with Powerex on these grounds was stayed by the court because the duress claim was deemed at issue in this case before the Commission.

1213. Lastly, the California Parties aver that Coral wrongly asserts that deciding claims of alleged price exploitation is "not important" to the Commissions' regulatory mission. The California Parties contend that the Commission's primary task is remedying energy price exploitation.[1491]

1214. Next, the California Parties address Respondents' arguments that Mr. Taylor did not utilize legal definitions of duress, fraud, and bad faith in his analysis. With respect to Respondents' claims that "stress" does not constitute a claim of duress, the California Parties argue that this characterization misrepresents its claim – that Respondents made a conscious decision to exploit CERS's stress by demanding prices far above the market, knowing that CERS lacked reasonable alternatives.[1492] The California Parties state that they never claimed that "stress" caused CERS to make all of its real-time purchases under duress. Rather, the California Parties assert that they have presented quantitative and documentary evidence that Respondents exploited CERS's already stressed position.

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[1489] *See, e.g.*, *Prohibition of Energy Market Manipulation*, Order No. 670, FERC Stats. & Regs. ¶ 31,202, at P 37 (2006).

[1490] *See, e.g.*, *Morgan Stanley*, 554 U.S. at 547; *Nev. Power Co. v. Enron Power Mktg, Inc.*, 103 FERC ¶ 61,353, at P 110 (2003); *Utah Power & Light Co.*, 33 FERC ¶ 63,001, at 65,003-07 (1985), *aff'd*, 41 FERC ¶ 61,308 (1987).

[1491] *See, e.g.*, *Atl. Ref. Co. v. Pub. Serv. Comm'n of N.Y.*, 360 U.S. 378, 388 (1959); *accord NAACP v. FPC*, 520 F.2d 432, 438 (D.C. Cir. 1975).

[1492] The California Parties state that taking advantage in this way is precisely what the courts have found to constitute duress. *See, e.g.*, *Andreini v. Hultgren*, 860 P.2d 916 (Utah 1993) (cause of action in duress where the physician waited until just before commencement of surgery to demand, as a condition of commencing the procedure, that patient sign a release of liability for past and future claims).

1215. With respect to Respondents' criticisms of Mr. Taylor's price screens, the California Parties note that the Mid-C day-ahead price closely tracked both the Mid-C day-of price and the COB day-ahead price; the only outlier was the COB day-of price, which was driven by the sales to CERS.[1493] Furthermore, the California Parties assert that Mr. Taylor's analysis, which included evaluating evidence indicating that duress or bad faith may not have been a factor, was rigorous, objective, and provided Respondents the benefit of the doubt.

1216. The California Parties contend that Coral improperly relies on *Bethlehem Steel* to assert that Mr. Taylor's analysis shows only that CERS struck a "bad bargain" because in retrospect the prices were too high.[1494] The California Parties state that unlike *Bethlehem Steel*, where the United States government chose to negotiate the purchase of warships when it could have simply commandeered ships under the governing statute, CERS had no choice but to pay Respondents' prices because it lacked alternatives.[1495]

1217. The California Parties also argue that Respondents incorrectly claim that "bad faith has no legal status" because the courts and the Commission have held to the contrary. The California Parties note that both the Supreme Court and the D.C. Circuit have cited bad faith in the original negotiation of a contract as a basis for deciding not to apply the *Mobile-Sierra* presumption.[1496] Similarly, the Commission has held that evidence of bad faith in the formation justifies setting aside the *Mobile-Sierra* presumption.[1497]

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[1493] Ex. CAT-289 at 105-07, Figures IV-1 and IV-2.

[1494] *United States v. Bethlehem Steel Corp.*, 315 U.S. 289 (1942).

[1495] The California Parties note that in *Bethlehem Steel*, the Court affirmed the dismissal of the government's lawsuit because: (1) the government clearly had alternatives; (2) the government did not considered themselves "compelled" during negotiation; and (3) the profits earned by Bethlehem Steel were not "exceptional." *Id.* at 301-08. The California Parties assert that the opposite is true for each of these considerations in this proceeding.

[1496] *See, e.g., Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008); *Potomac Elec. Power Co. v. FERC*, 210 F.3d 403, 410 (D.C. Cir. 2000).

[1497] *See, e.g., Pub. Utils. Comm'n of Cal. v. Sellers of Long Term Contracts to the Cal. Dep't of Water Res.*, 103 FERC ¶ 61,354, at P 62, *order on reh'g*, 105 FERC ¶ 61,182 (2003).

1218. The California Parties state that Utah law defines bad faith as taking "unconscionable advantage of others."[1498] The California Parties assert that unconscionability "has generally been recognized to include an absence of meaningful choice on the part of one of the parties, together with contract terms which are unreasonably favorable to the other party."[1499] The California Parties aver that Respondents conducted the contracts with CERS in bad faith by charging CERS prices far above market when CERS was faced with an "absence of meaningful choice."

1219. The California Parties further contend that Respondents' assertion that a False Export is not fraud lacks support. The California Parties state that Mr. Taylor documented Coral representing to the ISO that they were exporting power out of California when they were reselling it to CERS at COB for import into the ISO. The California Parties maintain that this clearly constitutes fraud.

1220. Next, contrary to Respondents' claims that their sales to CERS somehow benefitted California, the California Parties aver that duress, fraud, and bad faith were harmful. The California Parties state that the *Mobile-Sierra* presumption is based upon the notion that sellers with equal bargaining power are likely to strike a deal that is just and reasonable,[1500] but here, CERS dealt with Respondents from a powerless bargaining position.

1221. The California Parties also aver that Coral wrongly asserts that it could not have exerted duress or acted in bad faith because CERS purchased from Coral in only 928 of approximately 3,700 hours, and thus had other options. The California Parties state that the evidence demonstrates that (1) Coral's stated goal was to sell only when CERS was desperate enough to pay whatever Coral demanded[1501] and (2) CERS traders frequently refused Coral when any other lower-priced options existed.[1502] Thus, the California Parties argue that Coral engaged in economic withholding by being highly selective in its sales to CERS and targeting a limited number of sales at only the highest possible prices.

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[1498] *Valcarce v. Fitzgerald*, 961 P.2d 305, 316 (Utah 1998).

[1499] *Ryan v. Dan's Food Stores, Inc.*, 972 P.2d 395, 402 (Utah 1998) (emphasis omitted).

[1500] *See Morgan Stanley*, 554 U.S. at 545.

[1501] Ex. CAT-137.

[1502] *See* Ex. CAT-289 at 95-96; Tr. 2690:21-2691:6 (Taylor).

1222. Furthermore, the California Parties contend that Coral incorrectly relies on Ms. Lee's explanation of CERS's bargaining. The California Parties state that Ms. Lee's explanation of other prices in the market was only explaining where a particular price that CERS agreed to pay fit within other prices that CERS was paying in the same hour. The California Parties assert that the fact that Coral may have been charging CERS a price similar to other sellers that were also overcharging CERS proves nothing and does not exonerate Coral from its practice of exerting duress or acting in bad faith.

1223. The California Parties also contend that the evidence disputes TransCanada's claim that its parking transactions had a legitimate business purpose – allowing TransCanada to sell to CERS energy that originated from Portland General, an entity not willing to transact with CERS. The California Parties note that this purpose did not require TransCanada to wait until real-time in order to sell the energy to CERS. Rather, TransCanada waited until real-time to extract the highest price from CERS.

1224. Lastly, the California Parties aver that Trial Staff wrongly asserts that Mr. Taylor's analysis is subjective and renders his claim insufficiently specific. The California Parties state that the ample objective and specific evidence that the California Parties submitted clearly supports their claims of duress, fraud, or bad faith as to each contract challenged for each Respondent.

### (b) Allegations of Undue Price Discrimination

1225. First, the California Parties argue that attacks on Dr. Fox-Penner's credentials should be rejected. The California Parties state that Dr. Fox-Penner is a highly qualified economist with a background in engineering and is familiar with the electric industry, energy markets, including the unique features of the markets at issue in this case, and Commission regulation.[1503]

1226. Next, the California Parties state that Respondents generally imply that price discrimination is unlikely, unprovable, and not of much concern in a market-based rate regime involving bilateral contracts. The California Parties assert that both the Commission and the courts have found that price discrimination is a critical concern under a market-based rate regime.[1504]

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[1503] *See* Ex. CAT-162.

[1504] *See, e.g., California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1016 (9th Cir. 2004); *W. Sys. Power Pool*, 64 FERC ¶ 61,063 at 61,605 (1993).

1227. The California Parties state that once the claimant has proven that similarly-situated purchasers were treated differently, the burden of producing evidence shifts to the seller to justify the disparity on the basis of factual differences.[1505] The California Parties further note that the Commission clarified that it "need not find customers to be identical before requiring the pipeline to justify a disparity in treatment."[1506] The California Parties argue that they met their initial burden and Respondents and Trial Staff failed to offer adequate justifications to justify the price disparity.

1228. The California Parties next address Respondents' and Trial Staff's assertion that CERS was not similarly situated to other customers because of the credit and other risks in selling to CERS. The California Parties assert that Respondents provided no objective contemporaneous evidence that any Respondent actually charged a price to CERS during the CERS Period that included risk premiums equivalent to, or even approaching, the margins that they obtained from CERS. The California Parties aver that TransCanada's credit file for CERS demonstrates that TransCanada had a strong desire to trade with CERS to "[o]ptimize profits on transmission," "[c]ut out middlemen," and "[e]nhance liquidity,"[1507] allowing TransCanada to take advantage of high market prices.[1508]

1229. Next, the California Parties contend that Coral wrongly argues that the ten percent credit adder used in MMCP calculations cannot be translated to an appropriate risk premium for bilateral sales in this proceeding. The California Parties argue that Coral ignores the reality of the markets at the time the Commission first adopted the credit adder. The California Parties state that there had already been defaults in the CalPX markets resulting in chargebacks to other market participants as the result of the "mutualization" or "socializing" of the defaults.[1509] Thus, under the circumstances of the MMCP, mutualization increased the risk to an individual participant in the ISO and CalPX markets. Furthermore, the California Parties note that the WSPP agreement had

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[1505] *Transwestern Pipeline Co.*, 36 FERC ¶ 61,175, at 61,433 (1986).

[1506] *Id.* at 61,435.

[1507] Ex. CAT-703 at 32.

[1508] Tr. 3661:6-22 (Kunz).

[1509] *Pac. Gas and Elec. Co. v. Cal. Power Exch. Corp.*, 95 FERC ¶ 61,020, at 61,045 (2001).

additional tools that could have been deployed if credit had in fact been the concern that Coral and other Respondents now assert.[1510]

1230. Additionally, the California Parties contend that Coral's claim is undercut by the 2004 Policy Statement itself, which explained that default risk in organized markets is outside the control of participants and thus leaves participants with "little ability to mitigate the risk."[1511] Thus, a seller's risk may be mutualized with respect to a particular buyer in an organized single-price clearing market, but unlike the bilateral market, a seller in an organized market is exposed to default risk with respect to every buyer in that market. The California Parties also note that another key recommendation in the 2004 Policy Statement – to employ shorter settlement periods – was already effectively adopted in transactions between CERS and Respondents.[1512]

1231. The California Parties also argue that Trial Staff's credit premium calculation is based on an incorrect understanding of the MMCP and is logically flawed. The California Parties aver that Trial Staff incorrectly assumes that the MMCP's ten percent adder should apply to CERS even though CERS, unlike the ISO, never defaulted on any payment and the payment terms to CERS were much shorter.[1513] Moreover, the California Parties note that the MMCP risk premium was not added to a price that was the result of market dysfunction, but was added to an already mitigated price.[1514] Thus, the average risk adder for the CERS Period was $7.27/MWh.[1515] The California Parties note that this is drastically smaller than the ten percent adjustment Trial Staff calculated based on a $500/MWh sale. The California Parties also note that Trial Staff incorrectly added the credit risk premium to the sale price rather than the cost to the seller.

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[1510] *See* Ex. CAT-124 at 49-50.

[1511] *Policy Statement on Electric Creditworthiness*, 109 FERC ¶ 61,186, at P 18 (2004).

[1512] *Id.* P 21; Ex. CAT-161 at 22.

[1513] Ex. CAT-161 at 22; Ex. CAT-413 at 43-44.

[1514] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 129 FERC ¶ 61,147, at P 6 n.15 (2009).

[1515] Ex. CAT-232 at 24-40 (taking average of all MMCP prices for the CERS Period and computing an average credit premium based on that average MMCP price).

1232. The California Parties also contend that Respondents reliance on CERS's credit related documents is improper because those documents do not demonstrate how Respondents viewed CERS. The California Parties state that the documents only reveal that CERS was concerned with its place in the market.[1516]

1233. Next, the California Parties address Respondents' argument that the duration of the contracts and difference in time of when the contracts were entered into justify the price differentials. The California Parties note that all transactions relevant to this case involved spot market energy sold in the Pacific Northwest day-of market. Thus, the California Parties state that no difference extended beyond the day, except for those transactions that Dr. Fox-Penner carried from one day to the next during the 11:00 PM to 6:00 AM off-peak period. Additionally, the California Parties aver that Dr. Fox-Penner distinguished between on and off-peak transactions. Thus, the California Parties conclude that impact of duration and time of day on Dr. Fox-Penner's conclusions have "little practical consequence."[1517]

1234. Furthermore, the California Parties state that Dr. Fox-Penner conducted a duration analysis for the transactions with Coral and determined that the differences are inconsequential.[1518] With respect to the timing of a trade, the California Parties assert that this would be an issue only "if there were extreme and wholly unpredictable intra-day or intra-hour price volatility in market conditions."[1519] The California Parties aver that to the extent such price dispersion did exist, it would have been captured within the $50/MWh threshold.[1520]

1235. The California Parties also argue that contrary to Respondents' and Trial Staff's claims, Dr. Fox-Penner appropriately accounts for locational differences. The California Parties assert that in a competitive market without congestion the expectation would be that the price differentials between any two points would be the price of transmission.[1521]

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[1516] *See, e.g.*, Ex. TRC-25; Ex. TRC-26.

[1517] Ex. CAT-413 at 17.

[1518] *Id.* at 18.

[1519] *Id.* at 17.

[1520] *Id.*

[1521] *Id.* at 21. The California Parties note that congestion was not common during the CERS Period in the Pacific Northwest, and there was no evidence of significant congestion limiting Respondents' ability to transact across the BPA system on an hourly

(continued…)

With respect to arguments that the price differential between the two locations should be used, the California Parties argue the existence of a consistent price differential in excess of the actual transmission costs suggests a dysfunctional market, one that is not competitive, and one in which price discrimination can thrive.

1236. Next, the California Parties contend that Dr. Fox-Penner's marginal cost analyses were reasonable and support the conclusion that Respondents discriminated against CERS. The California Parties state that Trial Staff wrongly asserts that the marginal cost analyses were an independent measure of undue price discrimination or an independent basis for overcoming the *Mobile-Sierra* presumption. Rather, the California Parties state that the analyses only demonstrate that the discrimination could not be explained by Respondents' costs or justified on economic efficiency grounds.[1522]

1237. The California Parties also assert that criticisms of Dr. Fox-Penner's regression analyses are misguided. The California Parties state that Dr. Fox-Penner explained how he accounted for credit, time of agreement, and duration in his analyses.[1523] The California Parties further note that the use of regression analysis in discrimination litigation has been described as "probably the best empirical tool for uncovering discrimination."[1524] However, the California Parties state that the regression analysis was not a stand-alone measure of undue discrimination and was used only to validate Dr. Fox-Penner's other analyses.[1525]

1238. Next, the California Parties address Coral's defense that Mr. Tranen's "back-to-back" analysis justified the price charged to CERS. The California Parties contend that because the analysis reveals that "some other seller was willing to sell otherwise-identical power to Coral at a much lower price than Coral was able to command from CERS," it bears "the unmistakable signature of price discrimination."[1526]

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basis. *Id.* at 22-24.

[1522] Ex. CAT-161 at 38-39.

[1523] Tr. 1275:6-1276:24 (Fox-Penner).

[1524] Ex. CAT-421 at 7 n.5.

[1525] Ex. CAT-413 at 38.

[1526] *Id.* at 67.

1239. With respect to TransCanada's assertion that the "matched" transactions are not comparable because the underlying sales were part of blocks of hourly sales, the California Parties assert that Dr. Fox-Penner appropriately compared the CERS transactions to sales by TransCanada to other purchasers. The California Parties argue that the fact that the purchases may have been arranged on a single call does not diminish what TransCanada acknowledges are "blocks of hourly sales."[1527]

1240. The California Parties also contend that TransCanada's assertion that Dr. Fox-Penner relied on an incorrect monthly calculation of the rate disparity is inaccurate. The California Parties state that none of Dr. Fox-Penner's conclusions rely on this figure because it was a monthly average and not transaction specific.[1528] The California Parties also argue that TransCanada's assertion that there were instances where Dr. Fox-Penner did not find price discrimination despite the price being six standard deviations above the mean should be rejected because it is based on uncited or extra-record evidence.[1529]

1241. The California Parties next state that TransCanada claims that CERS had to obtain approval from the California government for each infusion of capital. The California Parties assert that this is simply false. Securing additional funds under AB1X merely required that CERS provide notice of its intent to take the money.[1530]

1242. The California Parties also contend that TransCanada wrongly argues that because Dr. Fox-Penner used the term "identical" at various points in his testimony and the comparable transactions he used in his comparison were not exactly identical, the analysis is flawed. The California Parties note that as a matter of law, "similarly situated" does not mean that transactions must be "identical." Furthermore, the California Parties assert that Dr. Fox-Penner's methodology was clearly stated in his testimony and work papers to ensure there was comparability between the transactions.[1531]

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[1527] TransCanada Initial Br. at 48.

[1528] *See* Ex. TRC-49.

[1529] The specific example that is provided in Dr. Morris' testimony relates to a Powerex transaction that was redacted from Exhibit CAT-163. Ex. TRC-1 at 75.

[1530] Tr. 1246:6-12 (Dr. Fox-Penner); Tr. 717:18-718:24 (Hart); Ex. CAT-280 at 10; Ex. CAT-015 at 16.

[1531] *See, e.g.*, Ex. CAT-161 at 10.

1243. Lastly, the California Parties address TransCanada contention that the California Parties failed to provide a supply curve for the Pacific Northwest during CERS Period. The California Parties state that more relevant to Dr. Fox-Penner's analysis were company-specific short-run supply and sales curves for the CERS Period, which he did create for each Respondent.[1532] The California Parties note that Dr. Fox-Penner concluded that TransCanada's supply curve was "consistent with [his] earlier findings on TransCanada's price discrimination."[1533]

### (c) Allegations of False Export

1244. The California Parties assert that Coral and Trial Staff incorrectly argue that False Exports are not a violation under Commission precedent because there was not price cap in effect in the Pacific Northwest.[1534] The California Parties note that the Commission's Order on Remand states that "parties may present evidence that any of the types of violations specified in the May 26, 2011 Order resulted in unjust and unreasonable contract rates."[1535] The California Parties state that the Commission expanded the scope of the hearing to include "(1) market practices that were previously excluded from the list and definitions of MMIP violation categories in the Show Cause Proceedings; (2) other []ISO and []PX tariff violations; (3) violations of Commission Orders."[1536] Thus, the California Parties assert that evidence of illicit market practices, including False Export violations, can be litigated in this proceeding.

1245. Moreover, the California Parties contend that the element of evasion of a price cap is immaterial to Mr. Taylor's False Export analysis because the behavior involves other tariff violations due to the harm to markets and reliability.[1537] The California Parties argue that False Exports involved fraudulent representations to the ISO and CERS and anomalous behavior in violation of the ISO Tariff, its MMIP, and Respondents'

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[1532] *See id.* at 48-58.

[1533] *Id.*

[1534] Respondents and Trial Staff rely on the Commission's 2003 Gaming Show Cause Order. *Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345 (2003), *order on reh'g*, 106 FERC ¶ 61,020 (2004).

[1535] Order on Remand at P 19.

[1536] *Id.* P 26.

[1537] Ex. CAT-289 at 135-36.

market-based rate tariffs. The California Parties contend that regardless of Respondents' and Trial Staff's assertions, False Exports had negative price and reliability effects.[1538]

1246. Next, the California Parties argue Coral's claims regarding the assumptions made by Mr. Taylor are irrelevant. The California Parties assert that Coral routinely exported the power out of California to NOB so that it could be resold to CERS at COB.

1247. Lastly, the California Parties respond to Trial Staff's criticism that the False Export analysis is on an hour-by-hour, rather than a transaction-by-transaction, basis. The California Parties note that Trial Staff did not attempt to perform its own analysis on a transaction-by-transaction basis nor undertake to identify the specific transactions. Furthermore, the California Parties state that Dr. Savitski agreed that Mr. Taylor's hour-by-hour analysis typically is the rule in the analysis of electric market data, and that he did not believe it would be possible to uniquely identify every transaction that he contended Mr. Taylor should have analyzed.[1539]

#### (d) Allegations that Respondents Exercised Market Power

1248. The California Parties argue that Respondents and Trial Staff rely on inapplicable market power screens, ignore direct evidence of market power, and repeat technical critiques of regression analyses that were successfully rebutted. The California Parties assert that Respondents ignore the fact that the California Parties' market power evidence encompasses multiple prongs and includes evidence submitted by Mr. Taylor and Dr. Fox-Penner.

1249. The California Parties contend that Respondents and Trial Staff wrongly contend that the Commission requires the hub and spoke test to determine whether market power was exercised during the CERS Period. The California Parties aver that (1) the hub and spoke and other such tests are merely preliminary screens; (2) the Commission stopped using the hub and spoke test; (3) there is no Commission precedent stating that the hub and spoke screen must be used to measure whether market power was actually exercised; and (4) significant precedent and economic authorities conclude that direct evidence is the appropriate way to measure whether the exercise of market power actually occurred.

1250. The California Parties assert that the hub and spoke screen determines whether market-based rate authority should be granted in the first instance and does not analyze

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[1538] Ex. CAT-041 at 90-92.

[1539] Tr. 4257:13-4258:7 (Savitski).

whether a seller possessed or exercised market power.[1540] The California Parties aver that the fact an entity was granted market-based rates does not make that entity immune from accusations of market power.

1251. Furthermore, the California Parties state that unlike *Lockyer*,[1541] the Commission hearing order does not expressly direct the use of the hub and spoke test because the issue in this proceeding is whether Respondents actually used market power.[1542] Additionally, the California Parties note that the March 26, 2003 Commission Staff Report concluded that it is entirely appropriate to base conclusions about the use of market power on measures of actual market behavior, not the predictive hub and spoke test.[1543] Relying in part on those findings, the Commission revoked Enron's market-based rate authority, even though Enron would not have failed a re-run of the hub and spoke test.[1544]

1252. Next, the California Parties argue that Dr. Savitski's criticisms of Dr. Reynolds' analyses should be disregarded. The California Parties assert that in response to Dr. Savitski's instrumental variables argument, Dr. Reynolds ran the instrumental variables regression, and found that his market power analyses were not affected.[1545]

1253. Lastly, the California Parties address Coral's claims regarding market power. With respect to Coral's assertion that the California Parties do not allege that Coral possessed market power, the California Parties state that Coral acknowledges that Dr. Reynolds' rebuttal testimony stated that Coral's realization of higher prices for larger quantities was consistent with the exercise of market power. Additionally, the California Parties contend that Coral mischaracterizes Dr. Reynolds' statements regarding back-to-back transactions because Dr. Reynolds never independently analyzed Mr. Tranen's testimony.

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[1540] *See Huntington Beach Dev., L.L.C.*, 97 FERC ¶ 61,256 (2001).

[1541] *California ex rel. Lockyer*, 135 FERC ¶ 61,113, at PP 9-10 (2011).

[1542] *See* Order on Remand at PP 26-27 & n.57.

[1543] *See* Ex. CAT-045 at 226, 236 (March 26, 2003 Commission Staff Report).

[1544] *Enron Power Mktg., Inc.*, 102 FERC ¶ 61,316 (2003).

[1545] Ex. CAT-631 at 13.

### (e) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1254. The California Parties assert that they have demonstrated that each Respondent "engaged in such extensive unlawful market manipulation as to alter the playing field for contract negotiations" such that the *Mobile-Sierra* presumption should not apply. The California Parties contend that Respondents have only criticized discrete aspects of the California Parties' evidentiary presentation and have failed to sufficiently challenge the vast majority of market manipulation evidence leveled against them.

1255. Next, the California Parties address the differences in how they and the Respondents define specific contracts. The California Parties state that they are challenging the sales to CERS at issue based on the contracts designated by "CERS ID" number, as recorded in the CERS transaction database. Based on the CERS ID, Mr. Taylor identified 156 contracts for Coral and 161 contracts for TransCanada.[1546] Conversely, TransCanada identified contracts by analyzing each trader tape and determined that there were 1,078 separate transactions.[1547] For Coral, the California Parties aver that Coral relies on Exhibit SNA-14, which identifies 323 "relevant contracts."[1548]

1256. The California Parties contend that TransCanada's trader tape analysis should not be dispositive. The California Parties state that Mr. Kunz, the person who analyzed the tapes, did not begin to work in TransCanada's electricity trading group until 2004,[1549] had only reviewed a limited number of trader tapes before becoming involved in this case in 2012,[1550] had not previously reviewed trader tapes for the purpose of deciding what was a contract,[1551] received no legal guidance as to what constituted a "transaction,"[1552] and had

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[1546] Ex. CAT-041 at 124, 127.

[1547] Ex. TRC-221 at 63.

[1548] Ex. SNA-14.

[1549] Tr. 3577:5-22 (Kunz).

[1550] Tr. 3579:13 (Kunz).

[1551] Tr. 3579:13 (Kunz).

[1552] Tr. 3611:21-3615:14 (Kunz).

no particular expertise in making judgment calls as to which transactions might properly be grouped together as part of a contract.[1553]

1257. The California Parties assert that the fact that each Respondent used a different approach to identify contracts indicates that there is some level of subjectivity in grouping particular hourly transactions into "contracts." With respect to the "hourly transactions," the California Parties state that there is no dispute regarding the quantities sold or the prices. The California Parties contend that its use of CERS's contemporaneous records was reasonable and provided consistent results across all Respondents.

### (f) Legitimate Business Behavior by Respondents

1258. First, the California Parties address Respondents' claim that market fundamentals constitute legitimate business behavior and excuse the prices that they charged to CERS. The California Parties argue that market fundaments do not meet the Commission's definition of "legitimate business behavior" and should be rejected.[1554] Additionally, for the reasons discussed in their initial brief, the California Parties assert that Respondents failed to demonstrate that market fundamentals explain Respondents' high prices to CERS.

1259. Second, the California Parties argue that Respondents wrongly assert that flawed market design and IOU behavior were major "contributing factors" to the high prices charged CERS. The California Parties contend that market design and IOU behavior are completely irrelevant to the issues to be decided in this proceeding. The California Parties state that these factors do not refute evidence that Respondents exercised duress or acted in bad faith, engaged in False Exports, exercised market power, and/or engaged in undue price discrimination. Furthermore, the California Parties note that the Respondents failed to undertake any analysis to quantify the effect of market design and IOU behavior on the market prices. The California Parties acknowledge that market design was flawed and did play a role in the Crisis. However, as stated in the Commission Staff Report, the California Parties assert that the market design made it easier for Respondents to engage in manipulation.[1555]

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[1553] Tr. 3611:21-3615:14 (Kunz).

[1554] Order on Remand at P 22 n.52.

[1555] Ex. CAT-045 at 17.

1260. Third, the California Parties state that Respondents and Trial Staff claim that credit and litigation risks justify the high prices. The California Parties assert that Respondents are inconsistent in their arguments about credit risk because they argue both that credit risk justified high prices and that CERS had many options in their purchases. With respect to litigation risk, the California Parties aver that pointing out that there may have been litigation risk is not sufficient to satisfy the legitimate business action standard. The California Parties further state that no Respondent attempted to quantify this generalized risk.

1261. Fourth, the California Parties argue that Respondents' claims that their prices were comparable to other sellers should be rejected. The California Parties assert that these arguments assume that the range of prices paid to other sellers was reasonable.

1262. Fifth, the California Parties address Coral's claim that its sales to CERS were "back-to-back" transactions. The California Parties assert that this claim has been fully rebutted,[1556] and Coral's blanket statement that "[n]o witness has disputed, and numerous trader tapes confirm, that Coral bought power from its B2B supplier at COB and then immediately resold that power to CERS"[1557] is not supported. The California Parties note that some California Parties witnesses assumed, solely for purposes of responding to Coral's testimony, that Coral's contentions were true.

1263. Sixth, the California Parties addresses TransCanada's claims regarding its parking transactions. The California Parties assert that the evidence in the record demonstrates that TransCanada's two parking transactions with Portland General were for the purpose of withholding power.[1558] The California Parties state that the fact that Portland General refused to sell to CERS does not mean that TransCanada had to park its day-ahead purchases from Portland so that it could extract a higher price in real-time.

### 6. <u>TransCanada Reply Brief</u>

#### (a) Burden of Proof

1264. TransCanada asserts that the California Parties failed to provide evidence sufficient to avoid the *Mobile-Sierra* presumption. TransCanada contends that the

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[1556] *See* California Parties Initial Br. at 113-16.

[1557] Coral Initial Br. at 44.

[1558] *See* Ex. CAT-289 at 102-04; Ex. CAT-041 at 85; Ex. CAT-118 at 5; Ex. CAT-699 at 12, 26.

California Parties initial brief includes a series of broad and incorrect arguments that suggest a "one size fits all" approach rather than a focus on individual contracts as required by the Commission.

1265. TransCanada avers that the California Parties wrongly claim that they have made a *prima facie* case and that the burden of establishing an affirmative defense rests with TransCanada. TransCanada states that a *prima facie* case requires the presentation of sufficient evidence to justify a verdict in favor of a party making the claim, provided that the evidence is not rebutted by the other party. TransCanada further states that the claimant must provide evidence sufficient to establish each element of each claim.[1559] Thus, the test is "whether there are facts in evidence which if unanswered would justify men of ordinary reason and fairness in affirming the question which the plaintiff is bound to maintain."[1560]

1266. TransCanada asserts that to overcome or avoid the *Mobile-Sierra* presumption, the California Parties must submit the following contract-specific evidence: (1) evidence that an individual seller violated the WSPP Agreement or the terms of a specific bilateral contract that resulted in unjust and unreasonable rates; (2) evidence that an individual seller violated a provision of its tariff that resulted in unjust and unreasonable rates; (3) evidence that an individual seller engaged in unlawful market activity that resulted in unjust and unreasonable rates; or (4) evidence that a specific contract imposed an excessive burden based on rates to consumers.[1561] TransCanada contends that the Commission rejected the use of (1) evidence of violations of state law good faith obligations; (2) evidence of unlawful activity by a non-contracting party; and (3) claims of uniformly higher prices in the Pacific Northwest.[1562] TransCanada argues that the California Parties failed to present the evidence required by the Commission and instead relied on evidence that the Commission specifically held would be insufficient to avoid or overcome the *Mobile-Sierra* presumption.

### (b) Allegations of Fraud, Duress, and Bad Faith

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[1559] *See, e.g., San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 142 FERC ¶ 63,011, at P 63 (2013).

[1560] California Parties Initial Br. at 13 (quoting *Nantahala Power & Light Co.*, 19 FERC ¶ 61,152, at 61,276 (1982)).

[1561] Order on Remand at PP 18-28; Order on Rehearing at P 27.

[1562] Order on Rehearing at PP 25, 26, 30.

1267. TransCanada asserts that the California Parties rely solely on an allegation that TransCanada acted in bad faith. TransCanada avers that the California Parties' initial brief demonstrates fails to establish a *prima facie* case because the California Parties rely on Mr. Taylor's *Power Markets Week* price test to support their aggregate fraud, duress, and bad faith claims.

1268. With respect to the California Parties' allegation that TransCanada's "unconscionable margins" demonstrate bad faith, TransCanada avers that even if true, this allegation does not support a finding that TransCanada acted with fraud or deception in its negotiations, let alone that it was prompted by a sinister motive.

1269. TransCanada states that the only specific activity that the California Parties alleged constituted bad faith involved parking of energy for a handful of hours on March 20, and 21, 2001. TransCanada states that the California Parties rely only on the deal tickets in making their claim. However, TransCanada asserts that these deal tickets fail to demonstrate fraud and deception in formation of a contract or a sinister motive.

1270. Next, TransCanada asserts that although the California Parties recognized that fraud, duress, and bad faith are separate and distinct legal claims, the California Parties incorrectly failed to distinguish between fraud, duress and bad faith. TransCanada states that the California Parties based their legal claims on definitions proffered by Mr. Taylor, who has no legal expertise.[1563] TransCanada states that even under the California Parties' definitions, both duress and fraud require an intentional act by the seller. However, as discussed above, TransCanada states that the California Parties have provided no evidence on an intentional act by the TransCanada. Thus, the California Parties failed to present a *prima facie* case against TransCanada under any definition.

1271. Next, TransCanada states that although the California Parties agree that Utah law governs its claims of bad faith, the California Parties fail to recognize that bad faith is not among the grounds to invalidate a contract under Utah law. TransCanada notes that the only Utah precedent cited by the California Parties is *Valcarce v. Fitzgerald*, which has nothing to do with contract formation, but concerned whether a tort action was brought in bad faith and whether attorneys' fees were available.[1564]

1272. TransCanada states that to support the premise that "each Respondent took advantage of [CERS' weak bargaining position] to obtain a disproportionate exchange of

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[1563] Tr. 2372:18-21, 2375:3-5 (Taylor).

[1564] *Valcarce v. Fitzgerald*, 961 P.2d 305, 316 (Utah 1998).

value," the California Parties relied upon *CrossTalk Prods. v. Jacobson*.[1565] However, TransCanada avers that this case interprets California state law, which is irrelevant to the California Parties' claims. Moreover, TransCanada notes that the portion of *CrossTalk* the California Parties quote in their Initial Brief only applies to claims in connection with economic duress and would not be relevant to the California Parties' claims of bad faith against TransCanada.

1273. Furthermore, TransCanada asserts that even if *CrossTalk* is found to be relevant, the case quoted therein, *Rich & Whillock, Inc. v. Ashton Dev., Inc.*, supports TransCanada's position because it would require the California Parties to demonstrate that TransCanada committed "a wrongful act which is sufficiently coercive to cause a reasonably prudent person faced with no reasonable alternative to succumb to the perpetrator's pressure."[1566] TransCanada contends that the California Parties presented no evidence regarding a "sufficiently coercive" act by TransCanada in connection with each contract as to constitute economic duress. The California Parties also presented no evidence demonstrating that CERS had "no reasonable alternative [but] to succumb to [TransCanada's] pressure."

1274. Next, TransCanada argues that Commission precedent also supports the rejection of the California Parties' allegations because Mr. Taylor admitted that he did not even conceive of these claims *until 2012*, almost a dozen years after the alleged misconduct occurred.[1567] TransCanada states that the passing of so many years from the alleged coercive, fraudulent, or deceitful act in negotiations is fatal to the California Parties' claims of duress, fraud, and bad faith.[1568] TransCanada argues that this is particularly relevant in this proceeding because the claims are not asserted by any witness with firsthand knowledge of the parties' negotiation, but rather by an expert witness who thought up the theory twelve years after the fact and only after the Commission had rejected the California Parties' previous theories concerning the identical transactions.[1569]

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[1565] *CrossTalk Prods. v. Jacobson*, 65 Cal. App. 4th 631, 645 (Cl. Ct. App. 1998).

[1566] *Rich & Whillock, Inc. v. Ashton Dev., Inc.*, 157 Cal. App. 3d 1154, 1158-59 (Cal. Ct. App. 1984).

[1567] Tr. 2430:12-2431:7 (Taylor).

[1568] *Utah Power & Light Co.*, 33 FERC ¶ 63,001, at 65,006 (1985).

[1569] Tr. 2423:13-2427:3, 2430:15-2431:14 (Taylor); *see also California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 135 FERC ¶ 61,113 (2011); *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178 (2011), *reh'g denied*, 139 FERC

(continued…)

1275. With respect to the California Parties claim that CERS was in a weak bargaining position, lacked reasonable alternatives, and Respondents were aware and took advantage of CERS's position, TransCanada asserts that CERS was not, in fact, in a "precariously weak bargaining position." TransCanada argues that CERS was a dominant market participant and acquired wide-ranging market pricing knowledge from many sellers. Conversely, TransCanada typically was selling 50 MWh to only 1 buyer at COB.[1570] TransCanada also states that CERS traders had access to confidential ISO information. TransCanada notes that Mr. Taylor admitted that where one party to a transaction has better market intelligence than the other party, the party with the better market intelligence has a competitive advantage.[1571] Moreover, TransCanada asserts that CERS's traders recognized their superior knowledge.[1572]

1276. Additionally, TransCanada contends that trader tapes of CERS traders turning down TransCanada's offers demonstrate that the California Parties overstated the "weakness" of CERS's bargaining position.[1573] TransCanada also notes that CERS often set the price either without any negotiation by TransCanada or by refusing to negotiate with TransCanada.[1574]

1277. Next, TransCanada states that the California Parties assert it is unrefuted that "CERS faced a 'seller's market,' in which 'every day was devoted to a triage approach to purchasing … where sellers 'knew we were stretched thin and … took full advantage of it.' "[1575] However, TransCanada notes that for twenty-seven percent of the hours during the CERS Period, CERS did not buy any power from TransCanada.[1576] Thus, CERS was not stretched so thin that it could not decline to buy power from TransCanada, which it

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¶ 61,210 (2012).

[1570] Ex. TRC-1 at 25:3-4; Ex. TRC-77 at 49:15-17.

[1571] Tr. 2538:2-6 (Taylor).

[1572] Ex. TRC-120 at 1:4-5.

[1573] *See, e.g.*, Ex. TRC-81; Ex. TRC-114; Ex. TRC-115; Ex. TRC-118; Ex. TRC-222 at 346, 746E, 1054, 1190, 2260-61, 2295, 2726.

[1574] *See* Ex. TRC-222; EX-TRC-222-A.

[1575] California Parties Initial Br. at 24.

[1576] *See* Ex. CAT-161 at 4 n.2; Ex. CAT-TRC-1; Ex. TRC-221.

did on numerous occasions.[1577] Moreover, TransCanada notes that only rarely did it refuse to reduce its offer price, and such refusals, without more, do not reflect TransCanada taking advantage of CERS.

1278. TransCanada also argues that the California Parties misrepresent the record in claiming that CERS was at a huge disadvantage in negotiations with sellers who were well aware of CERS's position in the market and its mandate to avoid blackouts.[1578] TransCanada first notes that these statements do no demonstrate an intentional bad act on the part of TransCanada. Additionally, TransCanada states that there is no evidence demonstrating that TransCanada knew CERS's position in the market. To the contrary, CERS internal emails suggest that CERS kept close guard of the quantity of energy that CERS was looking to purchase to meet the net short on an hourly basis.[1579] Further, TransCanada notes that the statement that CERS had a "mandate to avoid blackouts" is contradicted by the testimony of Mr. Hart that he was considering the option of blackouts in response to high prices.[1580]

1279. Moreover, TransCanada states that CERS traders often engaged in friendly banter with other traders, and one trader even described his position as "pretty good."[1581] Lastly, TransCanada notes that there were occasions in which CERS turned back quantities it previously had sought to acquire, or simply rejected TransCanada's offers outright.[1582] TransCanada argues that these actions do not indicate that CERS traders felt duress because of constant threats of blackouts.

1280. Next, TransCanada states that the California Parties' claim that Respondents shifted their sales to real-time is erroneous regarding TransCanada. TransCanada asserts that the California Parties have not cited any support in the record for this statement and, any "shift" and disparity in prices between the day-ahead and day-of markets was the

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[1577] *See, e.g.*, Ex. TRC-81; Ex. TRC-114; Ex. TRC-115; Ex. TRC-118; Ex. TRC-222 at 346, 746E, 1054, 1190, 2260-61, 2295, 2726.

[1578] California Parties Initial Br. at 23, 28.

[1579] Ex. TRC-140; *see also* Tr. 947:16-948:12 (Lee).

[1580] Tr. 620:20-621:23 (Hart).

[1581] Ex. TRC-151; Ex. TRC-146; Ex. TRC-222 at 877:21; Tr. 974:18-19 (Lee).

[1582] Ex. TRC-81; Ex. TRC-114; Ex. TRC-115; Ex. TRC-118; Ex. TRC-222 at 346, 746E, 1054, 1190, 2260-61, 2295, 2726.

result of CERS's purchasing strategy.[1583] Furthermore, because it did not have firm transmission capacity from Alberta to COB, TransCanada was not capable of ensuring deliveries of sales made in day-ahead markets.[1584]

1281. With respect to the California Parties allegation that there was only a small, oligopolistic group of sellers willing to transact with CERS at COB, TransCanada avers that the California Parties' implication of market power is unsupported. TransCanada notes that the California Parties' own witnesses admit that they did not perform any studies or analyses to examine whether TransCanada had market power.[1585] Moreover, TransCanada asserts that the predominate reason that there was a smaller number of suppliers available to CERS was due to concerns about CERS's credit.[1586] TransCanada states that its entry into the market *expanded* rather than contracted the universe of merchants at COB. Thus, TransCanada concludes that there is no evidence in the record to support the proposition that TransCanada, or any other supplier who chose to sell power to CERS at COB, was part of "an oligopolistic group."

1282. Next, TransCanada contends that the California Parties "cherry-pick" certain trader tapes to support their position that CERS was in a "must buy" situation, lacked reasonable alternatives, and that its traders had become resigned to paying very high prices to avoid blackouts. TransCanada notes that the California Parties cite trader tapes from the first two days that TransCanada entered the market. Therefore, any "resignation" of prices would not have been caused by TransCanada.

1283. TransCanada also disputes the California Parties' allegation that "it was common knowledge that CERS was 'over a barrel' and in no position to bargain."[1587] TransCanada notes that the California Parties cite to Mr. Taylor's testimony even though Mr. Taylor never spoke to a single real-time trader for CERS or any seller involved in any day-of transactions and offered no evidentiary support for the basis upon which he

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[1583] *See* Ex. TRC-1 at 18:12-15, 119:1-124:2; Ex. TRC-77 at 45:15-46:1.

[1584] Ex. TRC-1 at 116:5-15.

[1585] Tr. 1843:25-1844:5, 1851:14-19 (Reynolds); Tr. 2464:23-25 (Taylor); *see also* Ex. CAT-264 at 4:9-10.

[1586] Tr. 633:12-633:21 (Hart); Tr. 931:2-932:8 (Lee); Tr. 1211:19-1212:2 (Fox-Penner); Tr. 2714:3-7 (Taylor).

[1587] California Parties Initial Br. at 27.

could testify about so-called "common knowledge."[1588] TransCanada again notes that the trader tapes refute any claim that TransCanada knew and took advantage of a weakened CERS position.

1284. Moreover, TransCanada states that its prices "were typically below the average price that CERS paid at COB and about forty-nine percent of the time the lowest price that CERS paid at COB."[1589] TransCanada notes that the California Parties maintained that suppliers willing to sell energy at lower prices than other suppliers represented "instances … [where] traders did not seek to take advantage of CERS."[1590]

1285. Next, TransCanada asserts that the California Parties mischaracterize an email by a TransCanada employee to TransCanada's credit department seeking expedited credit approval to transact with CERS.[1591] TransCanada argues that this email in no way supports a claim that TransCanada knew CERS's position regarding the necessity of avoiding blackouts and only reflects an effort by the TransCanada employee to get expedited credit approval so that TransCanada could begin selling energy to CERS.

1286. Lastly, TransCanada states that the California Parties inappropriately characterize Mr. Taylor's price test as "conservative." TransCanada contends that Mr. Taylor's analysis completely lacks any probative value and is a radical departure from the traditional way of showing duress, fraud or bad faith.

1287. Next, TransCanada asserts that the California Parties failed to demonstrate that the contracts allegedly involving fraud, duress, or bad faith were harmful. TransCanada states that the only evidence of harm cited by the California Parties was Mr. Taylor's unsupported assertion that the rates were above the market price. However, TransCanada notes that its prices were typically below the average price paid by CERS and often the lowest price within a given hour.[1592]

1288. Next, TransCanada addresses the California Parties' allegation that TransCanada's profit margin demonstrates that the contracts were made in bad faith. TransCanada first

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[1588] Tr. 2431:15-2432:11 (Taylor); Ex. CAT-042.

[1589] Ex. TRC-1 at 8:15-19.

[1590] California Parties Initial Br. at 27.

[1591] Ex. CAT-703 at 39.

[1592] Ex. TRC-1 at 8:15-19.

states that profit margin is not relevant to the issue of bad faith in negotiations. TransCanada notes that Mr. Taylor acknowledged that maximizing profits is insufficient to show that a seller engaged in duress, fraud, or bad faith.[1593] Additionally, TransCanada states that *Morgan Stanley* makes clear that contracts should not be voided on the basis of gross margins because that would constitute "a reinstitution of cost-based rather than contract-based regulation."[1594]

1289. TransCanada also contends that adopting the California Parties' position "would impose an onerous new burden on the Commission, requiring it to calculate the marginal cost of the power sold under a market-based contract" and then determining, given market conditions, a price avoiding an "excessive" gross margin.[1595] Moreover, TransCanada argues that this could have a "chilling effect on investments and a seller's willingness to enter into [such] contracts."[1596]

1290. TransCanada further argues that the California Parties failed to present evidence sufficient to support their allegations of TransCanada's profit margins. TransCanada notes that the California Parties rely on an estimate that settled energy prices in the PPoA over the entire course of the CERS Period averaged approximately $80/MWh. However, TransCanada asserts that this estimate cannot be replicated from data in the record.[1597]

1291. Additionally, TransCanada states that the California Parties also estimate a typical non-Crisis mark-up of no more than $25/MWh, which includes recover of non-production costs and a reasonable profit. The California Parties allege that any mark-up above the $25/MWh is "pure profit." TransCanada asserts that reliance on assumed profit margins is improper because Mr. Taylor admitted that he was not familiar with the rules of the PPoA, did not do any assessment of the risks the parties may have encountered as a result of transacting in the PPoA, and had no evidence to support his

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[1593] Tr. 2536:8-12 (Taylor).

[1594] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[1595] *Morgan Stanley*, 554 U.S. at 550.

[1596] *Morgan Stanley*, 554 U.S. at 551.

[1597] TransCanada states that the $80/MWh figure was a rough estimate that Witness Taylor provided by eyeballing the graph lines on Exhibit CAT-662, Tr. 2922:6-8 (Taylor). Further, TransCanada notes that not all its sales to CERS were sourced from the PPoA. Ex. TRC-77 at 6:3-5.

allegation that the price in the PPoA at the time of the transactions was around $100 or $200.[1598] TransCanada notes that prices in the PPoA were as high as a $568/MWh.[1599] Additionally, TransCanada states that Mr. Taylor did not investigate TransCanada's overhead expenses or opportunity costs.[1600]

1292. TransCanada also avers that the California Parties' reliance on an average settled price of energy in the PPoA diminishes the minute-by-minute volatility of prices that occurred. Thus, TransCanada asserts that there were instances in which TransCanada sold at a loss[1601] and times in which forecasted PPoA pricing, which was used by TransCanada in its sales to CERS, reflected prices substantially higher than those cited by Mr. Taylor.[1602] TransCanada further notes Mr. Kunz testified about the importance of various risks associated with procuring energy from the PPoA and the information that was available to TransCanada's traders at the time of negotiations.[1603]

1293. With respect to the California Parties claim that PPoA volatility is an after the fact, litigation inspired justification, TransCanada argues that there is no basis for this claim. TransCanada states that it was necessary for it to consider price risk when negotiating with CERS at the time of the transactions.[1604] Moreover, trader tapes refute the California Parties' contention.[1605]

1294. Furthermore, TransCanada contends that the California Parties ignore the precise cost data for TransCanada that was analyzed by Dr. Morris.[1606] TransCanada states that

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[1598] *See* Tr. 2371:13-2372:3, 2406:15-2407:13 (Taylor).

[1599] Ex. TRC-225; Ex. TRC-226; Ex.TRC-231; Tr. 2444:16-2445:10 (Taylor).

[1600] Tr. 2494:24-2495:14; 2496:6-2497:5 (Taylor).

[1601] Ex. TRC-225; Ex. TRC-231.

[1602] Ex. TRC-226; *see also* Ex. TRC-225; Ex. TRC-231.

[1603] Tr. 3544:3-3556:20, 3653:24-3654:6, 3690:15-3691:24 (Kunz).

[1604] *See* Ex. TRC-231; Ex. TRC-225.

[1605] *See* Ex. TRC-222 at 114, 1738, 2280-81, 2368, 2374, 2506-07, 2509, 2514, 2517, 2614, 2621, 2627, 2634, 2747, 2751, 2766, 2768, 2772, 2802, 2826, 2851-54, 3052.

[1606] *See* Ex. TRC-1 at 88:11-92:7.

Dr. Morris explained that non-production costs, such as line losses for services on transmission facilities, can be based on a percentage.[1607] Thus, the price of the power purchased may affect these costs.

1295. Lastly, TransCanada states that the California Parties rely on a TransCanada document showing its operating income for its electric operations was significantly above plan due to high market prices created by the power shortages in California and the rest of the Western region. TransCanada asserts that the document, at best, reveals that TransCanada was maximizing profits, and attempting to take advantage of profit opportunities in the market, and is not evidence of bad faith in negotiations.[1608]

### (c) Allegations of Undue Price Discrimination

1296. TransCanada also avers that the California Parties failed to make a *prima facie* showing of undue discrimination. TransCanada states that the California Parties cite to a 1979 case in describing the applicable legal standard – "[u]ndue price discrimination results from a violation of the requirement that 'those who are similarly entitled must be treated equally.'"[1609] However, TransCanada asserts that *Sebring Utilities* provides an incomplete standard because the only way to know whether a party is "entitled" to equal treatment is to determine if another party to whom it is being compared is similarly-situated. TransCanada contends that the actual test for undue discrimination is: "discrimination is 'undue' when there is a difference of rates, terms or conditions among similarly situated customers."[1610] Thus, TransCanada states that the entitlement to equal treatment under the FPA is not unqualified, but in fact significantly constrained, namely only when a preference or discrimination is undue.[1611] TransCanada concludes that the California Parties have failed to show similarly situated transactions with similarly situated counterparties that were charged different rates.

1297. TransCanada argues that the California Parties' undue discrimination allegations (1) misinterprets precedent, (2) incorrectly accuses TransCanada of "systematically"

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[1607] *See id.*

[1608] Tr. 2536:8-12 (Taylor).

[1609] *Sebring Utils. Comm'n v. FERC*, 591 F.2d 1003, 1008 (5th Cir. 1979).

[1610] *Cal. Indep. Sys. Operator Corp.*, 119 FERC ¶ 61,076, at P 369 n.310 (citing *Calpine Oneta*, 116 FERC ¶ 61,282); *see also* 16 U.S.C. §§ 824d, 824e (2012).

[1611] 16 U.S.C. § 824d(b).

engaging in undue discrimination, and (3) makes unsupported and misleading factual statements regarding TransCanada and the analysis of Dr. Fox-Penner.

1298. TransCanada asserts that the California Parties did not discuss how claims of undue discrimination are affected by *Mobile-Sierra*. TransCanada states that the D.C. Circuit recognized that "a tension arises between *Mobile-Sierra* and Section 205(b) whenever there exists a group of customers some of whom are guaranteed rather low rates by fixed-price contracts while others who are similarly situated save for the absence of such contracts are charged more."[1612] TransCanada notes that D.C. Circuit held that such a result was tolerable so long as "nothing else" had been demonstrated.[1613] Thus, TransCanada avers that *Town of Norwood* makes clear that a host of factors must be examined to determine whether customers actually are similarly situated as to render a price differential unduly discriminatory.

1299. TransCanada notes that in *City of Bethany*, the D.C. Circuit provided further guidance, stating that "the anti-discrimination mandate of section 205(b) should not be read to obliterate the public policy supporting private rate contracts between utilities and their customers" and that "[a] fixed rate contract between the parties may justify a rate disparity, rendering it lawful under section 205(b)."[1614] Thus, TransCanada concludes that the California Parties must prove more than the fact that TransCanada charged CERS a different price than other customers, they must also show that there is a "reason to question what occurred at the contract formation stage."[1615]

1300. TransCanada asserts that the California Parties fail to fully explain the required showing to demonstrate undue discrimination, including the fact that pricing can differ for a plethora of reasons as recognized in *Town of Norwood*. TransCanada argues that the California Parties' legal standard would produce results that are incompatible with the concept of market-based pricing because it would essentially imply a most favored nations clause into every bilateral contract.

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[1612] *Town of Norwood v. FERC*, 587 F.2d 1306, 1310-11 (D.C. Cir. 1978).

[1613] *Town of Norwood*, 587 F.2d at 1311-12.

[1614] *City of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) (citing *Town of Norwood*, 587 F.2d at 1310; *Boroughs of Chambersburg v. FERC*, 580 F.2d 573, 577 (D.C. Cir. 1978)).

[1615] *Town of Norwood*, 587 F.2d at 1312.

1301. Next, TransCanada avers that the California Parties wrongly accuse TransCanada of "systematically" engaging in price discrimination. TransCanada notes that the California Parties allege undue discrimination in just four contracts and just 26 of 2,610 delivery hours. TransCanada asserts that when accusing Coral of systematic discrimination, the California Parties rely on the number of alleged violations. However, when accusing TransCanada, the California Parties alter their analysis, claiming that TransCanada systematically charged higher than competitive prices to CERS. TransCanada argues that this shift in argument effectively turns the undue discrimination claim into a carbon copy of the California Parties' fraud, duress and bad faith claims.

1302. TransCanada also contends that the California Parties undertake a circular analysis because Mr. Taylor relies solely on Dr. Fox-Penner,[1616] and the California Parties rely on Mr. Taylor to supplement Dr. Fox-Penner's analysis.

1303. Next, TransCanada avers that because virtually all of TransCanada's sales during the CERS Period were to CERS, Dr. Fox-Penner and the California Parties developed a theory of undue discrimination that did not require a similarly situated customer. Specifically, the California Parties insinuate that had TransCanada made sales to other parties, then a pattern of undue discrimination would have emerged.[1617] Thus, TransCanada asserts that the California Parties attempt to hold TransCanada liable for actions it did not take, but could have taken had TransCanada had a "sinister motive."

1304. Furthermore, TransCanada contends that Dr. Fox-Penner failed to justify his $50/MWh threshold. TransCanada states that the California Parties assert that the threshold accounts for "non-observed potential cost differences" or price dispersion, but provided no rationale to justify the $50/MWh value. TransCanada notes that the threshold seems to have been randomly selected and remains static for all sales above $125/MWh.[1618]

1305. Next, TransCanada argues that Dr. Fox-Penner made no attempt to investigate the reasons for the disparities in prices he identified. For example, in hour ending 7 on February 20, 2001, TransCanada had to enter into a fire sale to sell power it had purchased to sell to CERS pursuant to an oral confirmation that CERS canceled less than an hour before the power was to be delivered.

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[1616] Tr. 2418:15-2419:10 (Taylor).

[1617] California Parties Initial Br. at 54.

[1618] *See* Ex. CAT-163 at 110.

1306. With respect to Dr. Fox-Penner's standard deviation analysis, TransCanada contends that the California Parties' claim that six standard deviations represents a 1 in 537 million chance that the price is part of a normal distribution[1619] assumes all prices were for the same product. However, TransCanada states that Dr. Fox-Penner's standard deviation analysis compares TransCanada price for a specific hourly delivery to CERS with the daily average sales prices that other sellers charged throughout the day to other buyers.[1620] Hourly sales made by TransCanada to CERS at peak delivery times were compared to sales made by other market participants across the entire day including off-peak times, and perhaps including transactions only during off-peak times. TransCanada further notes that Dr. Fox-Penner admitted that sales made at the same time, but for delivery at different hours, were not the same product.[1621] Thus, TransCanada concludes that the California Parties' claims regarding normal distribution of prices cannot be relied upon.

1307. Next, TransCanada argues that TransCanada's sales to CERS do not fit the California Parties' theory of systematic undue price discrimination.[1622] TransCanada again notes that in virtually all hours, there was not "a different group of customers" to route cheaper power to. Additionally, 90 percent of TransCanada's energy was purchased from the PPoA, not from a number of different sources.[1623]

1308. TransCanada also contends that Dr. Fox-Penner did not appropriately account for the risk in selling to CERS. TransCanada asserts that Dr. Fox-Penner wrongly relies on the default risk associated with junk bonds because (1) junk bonds retain a claim on the debtor's assets or revenue streams;[1624] (2) the comparison fails to consider litigation

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[1619] California Parties Initial Br. at 54 n.207.

[1620] *See* Ex. CAT-163, Column 3.

[1621] Tr. 1207:16-20 (Fox-Penner).

[1622] The California Parties state that systematic discrimination occurs when "a marketer *buying power from a number of sources* and systematically choosing to sell to one particular customer at the highest price with the highest priced purchases that it made, and then in effect, routing the cheaper power *to a different group of customers* because that other group of customers was much less price-sensitive, didn't have to buy it …."

[1623] Ex. TRC-77 at 5:3-6:5.

[1624] *See* 11 U.S.C. § 507 (2012)

risks;[1625] and (3) junk bonds issued by private parties do not present the same risks as those associated with dealing with a sovereign.

1309. Next, TransCanada states that the California Parties make numerous statements regarding Dr. Fox-Penner's analysis that are unsupported and misleading.

1310. First, TransCanada asserts that the California Parties incorrectly state that Dr. Fox-Penner's undue discrimination analysis compared sales made by TransCanada to CERS and other buyers of the very same product in the very same markets. TransCanada notes that Dr. Fox Penner actually performed two different analyses – a "matched" transaction analysis and a standard deviation analysis. TransCanada states that its initial brief explains why neither analysis can be described as comparing sales made by TransCanada to CERS and other buyers as "the very same product in the very same markets."

1311. Moreover, TransCanada argues that the California Parties later admitted in their initial brief that they were not seeking to compare "the very same product in the very same markets" but to compare prices TransCanada charged CERS versus other buyers "for power *delivered* at the same date, time, and location."[1626] Thus, the comparison did not account for the duration of the transaction, the time the sale was negotiated, the source of supply, or the risk of the transaction.

1312. TransCanada also avers that even the assertion that Dr. Fox-Penner compared the prices TransCanada charged CERS versus other buyers for power *delivered* at the same date, time, and location is misleading. TransCanada notes that for those few transactions with a "match," the non-CERS transaction did not occur at the same location.[1627] Furthermore, TransCanada states that the standard deviation analysis, which uses daily averages and include only hours where TransCanada did not sell to a non-CERS buyer, clearly fails to compare power delivered at the same date, time, and location.

1313. Second, TransCanada states that there is no evidentiary support for the California Parties' claim that TransCanada was "able to opportunistically extract discriminatorily high prices from CERS, and did so" because "CERS was often purchasing less than an hour, and sometimes only minutes, before it needed energy to flow."[1628] TransCanada

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[1625] Ex. TRC-1 at 96:2-16.

[1626] California Parties Initial Br. at 46 (emphasis added).

[1627] Ex. TRC-1 at 87:13-15.

[1628] California Parties Initial Br. at 42-43.

states that only one of the sales by TransCanada that the California Parties claimed were unduly discriminatory took place less than hour before delivery (59 minutes),[1629] and the remainder of the sales all took place between one hour and 23 hours before delivery.[1630] TransCanada further notes that Dr. Fox-Penner offered no testimony that showed that he reviewed or was knowledgeable about any of TransCanada's trader tapes.[1631]

1314. Third, TransCanada asserts that the California Parties incorrectly calculate the "premiums" included in their Initial Brief and evidence. Specifically, TransCanada states that the premium for May 2001 should be negative $6/MWh rather than negative $14/MWh, and the full period average should be $40/MWh, not $54/MWh.[1632]

1315. Fourth, TransCanada states that there is no support for the California Parties' claim that a CERS Premium existed in February because CERS was "most vulnerable and markets were especially dysfunctional."[1633] TransCanada notes that the California Parties cite to no evidence for this conclusory statement. TransCanada argues there is ample evidence, including a presentation from CERS's own consultant,[1634] demonstrating that February was the riskiest month to transact with CERS because of the circumstances under which CERS was created and funded.[1635]

### (d) Allegations that Respondents Exercised Market Power

1316. Next, TransCanada contends that the California Parties did not make a *prima facie* case of market power against TransCanada. TransCanada states that the appropriate Commission test to determine if an entity had market power was the hub and spoke

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[1629] Ex. TRC-222 at 293:4-23; Ex. TRC-221 at 9, Transaction No. 84; Ex. TRC-77 at 10:7-11.

[1630] *See* Ex. TRC-222 at 66-77, 290-307, 1972; Ex. TRC-221 at 2-10, 48; Ex. TRC-77.

[1631] *See* Tr. 1154:19-1156:7 (Fox-Penner).

[1632] *See* Ex. CAT-163.

[1633] California Parties Initial Br. at 43.

[1634] Ex. TRC-161 at 4.

[1635] *See* Ex. TRC-1 at 32-37.

test.[1636] TransCanada argues that the California Parties failed to provide any evidence that would satisfy this standard with regard to TransCanada, made no claims of market power against TransCanada, and provided no individualized analysis of market power with respect to TransCanada.

1317. TransCanada states that that there are no allegations that TransCanada had or exercised market power, and the California Parties' initial brief only uses the generic term "Respondents." TransCanada further notes that none of the California Parties' summary charts include any allegations that TransCanada exercised market power.[1637]

#### (e) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1318. TransCanada avers that the only specific bad acts alleged by the California Parties against Trans Canada are (1) two parking transactions and (2) a comparison of "average" daily acquisition purchase and sale prices, even during hours when TransCanada was not selling to CERS. TransCanada states that with the exception of deal tickets related to the two parking transactions, the California Parties' case against TransCanada does not rely on any emails, company memoranda, or documents that corroborate the California Parties' claims.

1319. TransCanada also notes that the California Parties incorrectly state that a stipulation concerning transactions has not been reached. TransCanada states the parties did reach a stipulation concerning the vast majority of the transactions details.[1638] Additionally, TransCanada notes that the California Parties incorrectly state that they challenge 96 "contracts," under Issue 1(A). TransCanada states the correct number is 91 transactions using the California Parties' grouping of "contracts."[1639]

#### (f) Legitimate Business Behavior by TransCanada

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[1636] Ex. S-13 at 34:11-12; *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 122 FERC ¶ 61,260, at 62,505 n.70 (2008); *see, e.g., W. Resources*, 83 FERC ¶ 61,110, at 61,532 (1998).

[1637] California Parties Initial Br. at 89-90, B-10 through B-12.

[1638] *See* Ex. CAT-TRC-1.

[1639] California Parties Initial Br. at B-10; *see also* Ex. TRC-178; Ex. CAT-412.

1320. TransCanada first addresses the California Parties' assertions with respect to the credit and litigation risk associated with selling to CERS. TransCanada argues that the California Parties wrongly claim that Dr. Fox-Penner was the only witness to calculate a risk premium associated with sales to CERS during the CERS Period. TransCanada states that Dr. Morris provided an extensive analysis of CERS's credit risk, relying upon contemporaneous documents, and concluded that the ten percent "adder that the Commission utilized for calculating refunds within California" was "the minimum cost of risk appropriate for sales to CERS."[1640]

1321. Additionally, TransCanada contends that the California Parties improperly rely on the fact that CERS never defaulted on payment and had a shorter time period of outstanding credit risk. TransCanada states that CERS not actually defaulting is a *post-hoc* analysis of the risk of trading with CERS. TransCanada notes that Dr. Morris explained that "[t]he biggest flaw [in Dr. Fox-Penner's risk analysis] is that he bases his analysis upon information that we know *today* as opposed to information available."[1641] Additionally, TransCanada argues that the shorter payment times did not alleviate the credit risk because "CERS did not pay [its bills] until up to 51 days after a transaction"[1642] even though on average, CERS obtained new funding from the General Fund every twelve days.[1643]

1322. TransCanada also disagrees with the California Parties' argument that litigation risk should not be considered because sellers will be assured a just and reasonable, compensatory rate. TransCanada states that at minimum, the cost of litigation should be considered when addressing the price TransCanada received in its transactions with CERS. TransCanada notes that litigation also imposes a reputational cost on the Respondents.

1323. Next, TransCanada states that the California Parties' claim that TransCanada's sales to CERS did not help CERS because the rates were unjust and unreasonable and TransCanada waited until real-time to sell energy to CERS in order to gain the highest possible profits. TransCanada states that its presence in the market increased competition among suppliers to CERS, and during most hours, TransCanada's sales were made at

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[1640] Ex. TRC-1 at 30:15-50:6, 96:1-99:4.

[1641] Ex. TRC-1 at 31:12-14 (emphasis in original).

[1642] Ex. TRC-1 at 38:18-19.

[1643] Ex. TRC-19 at 7.

prices below CERS's average price of acquisition.[1644] Moreover, TransCanada asserts that its sales were well before the hour of delivery. TransCanada further notes that in some instances, CERS refused to buy power from TransCanada because TransCanada called them "too early."[1645] Lastly, TransCanada states that because it did not control any firm transmission or generation, it was constrained in its ability to sell in the day-ahead market.

1324. With respect to the California Parties' assertion that TransCanada's parking transactions were done for the purpose of withholding energy, TransCanada states that Mr. Kunz testified that TransCanada's offers to CERS were consistent with TransCanada's typical practice when marketing light load hours and consistent with the times of day CERS had an interest in purchasing from TransCanada.[1646] Additionally, TransCanada states that the California Parties accuse TransCanada of concealing where energy was going by entering into the two parking transactions. TransCanada asserts that it was not concealing the source of energy from CERS by parking the power, but was concerned regarding its position in the market relative to other potential *Canadian* merchants of power.[1647]

1325. Next, TransCanada argues that contrary to the California Parties' contention, Dr. Morris correctly found that TransCanada's sales in real-time were a legitimate response to CERS's failure to show its true demand in the day-ahead market. TransCanada states that by not revealing the full scope of demand day-ahead, CERS artificially lowered pricing in that market which in turn raised pricing in the day-of market once CERS's full scope of demand became known.[1648]

1326. Lastly, TransCanada addresses the California Parties' contentions regarding high prices and margins. As discussed above, TransCanada states that its prices were consistent with market pricing and were often below average prices CERS paid.

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[1644] *See* Ex. TRC-1 at 8:15-19.

[1645] *See, e.g.*, Ex. TRC-222 at 57, 305, 362, 471, 534, 700, 747-48, 774, 781, 1716, 2754, 3005, 3014.

[1646] Ex. TRC-77 at 45:1-5.

[1647] Tr. 3700:8-3702:3 (Kunz).

[1648] Ex. TRC-1 at 119:6-11, 122:1-4, 148:2-3, 151:16-18.

1327. TransCanada states that the California Parties also argue that the volatility in the PPoA did not justify TransCanada's prices to CERS because: (1) TransCanada traded regularly in the PPOA market and understood its dynamics; (2) TransCanada could choose to stop selling until that volatility stopped; and (3) TransCanada charged other purchasers far lower prices than CERS. TransCanada avers that this demonstrates that the California Parties do not understand the PPoA market or how energy trading functions. TransCanada states that Mr. Kunz testified on the price risk associated with procuring energy from the PPoA and the factors that could produce dramatic price increases in a short period of time.[1649] TransCanada again notes that it would not know the price of its purchases from the PPoA prior to selling that energy to CERS, which resulted in negative margins in some cases.[1650] Thus, TransCanada's traders needed to gauge whether current market pricing at COB was sufficient to cover TransCanada's after-the-fact price risk for its sales to CERS from the PPoA.[1651]

1328. With respect to the California Parties' claim that TransCanada could have stopped trading, TransCanada states that this would have reduced supply to California, which would run contrary to California's effort to procure its net short and caused further increases to the cost of energy at COB.[1652] TransCanada further notes that prices in the PPoA exhibited volatility through most of the CERS Period,[1653] and therefore TransCanada would not have made most, if not all, of its sales to CERS.

### 7. Coral Reply Brief

#### (a) Coral's Back-to-Back Transaction Defense

1329. Coral argues all contemporaneous evidence confirms that Coral sold to CERS only through back-to-back transactions.[1654] Coral assert that the Commission previously found, based on uncontested evidence, that on average a unit of power in the Pacific

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[1649] Ex. TRC-77 at 7:1-6.

[1650] Ex. CAT-697 at 41; Ex. TRC-221 at 43.

[1651] Tr. 3690:15-3691:24 (Kunz); Ex. TRC-225; Ex. TRC-226; Ex.TRC-231; Ex. TRC-77 at 7:1-6.

[1652] *See* Ex. TRC-1 at 164:2-18.

[1653] *See* Ex. TRC-226.

[1654] Tr. 4014:11-13 (Bowman); Ex. SNA-1 at 5:7-19; Ex. SNA-14.

Northwest during the relevant period changed hands six times between generator and ultimate wholesale purchaser.[1655] Thus, Coral concludes that contrary to Mr. Taylor's assertions, its upstream purchases were unremarkable.

1330. Coral states that Exhibit SNA-14 shows a Coral sale to CERS and a corresponding purchase by Coral from a counterparty in the Pacific Northwest of the identical volume during the identical day and hour of the sale to CERS. Coral asserts the California Parties stipulated to the accuracy of the 1,703 Coral sales to CERS,[1656] and that Dr. Fox-Penner and Mr. Taylor affirmed that each sale to CERS is perfectly matched to a purchase by Coral.[1657] Moreover, Coral notes that trader audiotapes confirm that Coral sold to CERS only in back-to-back transactions.[1658]

1331. Coral also contends that the California Parties incorrectly claim that a number of transactions identified as back-to-back were not. Coral asserts that each exhibit cited for this contention demonstrates that the transactions were back-to-back. Coral argues that the two transactions identified by Mr. Taylor[1659] were executed outside the ISO control area and did not originate from a portfolio of power.[1660]

1332. Next, Coral argues that the California Parties attempt to discredit Mr. Tranen's testimony are irrelevant. Coral states that although Mr. Tranen did not review all of Coral's emails and other documents from the relevant period, he did review documents

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[1655] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at P 47 (2003).

[1656] Ex. SNA-CAT-1. The California Parties identified minor discrepancies in the volume, price, or location of seven sales only.

[1657] Tr. 2560:17-20 (Taylor); Tr. 1316:7-12, 1350:8-20 (Fox-Penner); Ex. CAT-413 at 66:4-8.

[1658] *See* Ex. CAT-356; Ex. CAT-358; Ex. CAT-360; Ex. CAT-362; Ex. CAT-366; Ex. CAT-462; Ex. CAT-464; Ex. CAT-672.

[1659] Tr. 2976:1-2999:11 (Taylor); Ex. CAT-669; Ex. CAT-670; Ex. CAT-672; Ex.CAT-674; Ex. CAT-675.

[1660] Coral bought energy from its marketing partner, the City of Glendale, California, at the trading point Mead, located outside the ISO in Southern Nevada. Coral then sold the energy at NOB, also outside the ISO, using the DC line to transmit the energy north from Mead to NOB. Coral then made a purchase of energy at COB and immediately resold that energy to CERS.

related to credit issues and was able to observe Coral's trading strategy based on those documents.[1661] Coral notes that these documents were not the source of Mr. Tranen's Exhibit SNA-14, which the California Parties do not contest the accuracy of. Furthermore, Coral contends that the California Parties mischaracterize Mr. Tranen's statement that he did not investigate "whether Coral would ever sell power to a party … at COB and then buy it back from [that same party] at the same time and place and then sell it to CERS."[1662] Coral asserts that this hypothetical, initially misunderstood by Mr. Tranen,[1663] is irrelevant because the California Parties do not allege that Coral ever executed such a series of transactions. With respect to California Parties claim that Mr. Tranen did not investigate "upstream transactions," Coral asserts that Mr. Tranen did perform an additional investigation in response to Mr. Taylor's testimony.

1333. Coral also avers that the California Parties wrongly allege a "pattern" of multi-party False Exports.[1664] Coral states that in response to Mr. Taylor's hearing testimony, Mr. Tranen conducted an analysis and found a total of eleven deals representing thirty total hours that involved the same trading behavior.[1665] Coral states that of the thirty hours, there is specific trader tape or documentary evidence of some coordination in only eight instances.[1666]

1334. Moreover, Coral argues that the California Parties falsely represent that Mr. Tranen found 300 additional hours "of the same nature" as Mr. Taylor's alleged "violations." Coral first notes that Mr. Taylor has not alleged that any of these 300 transactions, or transactions of a similar pattern, is a False Export violation. Additionally, Coral states that in those 300 hours, the volume of Coral's sale to the non-CERS buyer was different than its sale to CERS, and Coral's upstream sale was to a different party than the seller that supplied Coral for its transaction with CERS.[1667] Thus,

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[1661] Tr. 3912:11-31914:7 (Tranen).

[1662] California Parties Initial Br. at 114.

[1663] Tr. 3996:21-3997:4 (Tranen).

[1664] Tr. 3018:24-3019:13 (Taylor); CAT-041 at 98:13-19.

[1665] Tr. 3961:22-3962:13 (Tranen).

[1666] Ex. CAT-104 (Coral emails); Ex. CAT-672, Ex. CAT-705, Ex. CAT-706 (trader tapes).

[1667] Tr. 3960:16-3962:25 (Tranen) (describing Screen 1, which requires a Coral sale at NOB and purchase back at COB from the same counterparty and in the same

(continued…)

Coral contends that there is no evidence of coordination between the upstream transactions and the sale to CERS and these transactions do not follow the pattern identified by Mr. Taylor at hearing.

1335. Lastly, Coral avers that the information in Exhibit SNA-14 demonstrates Coral's "true profits." Coral states that the California Parties provide no evidence relating to their claim that there may be profits associated with upstream transactions. Coral notes that all thirty transactions discussed above begin with Coral buying from its marketing partner the City of Glendale, California.[1668] Coral states that because it had a marketing agreement with Glendale, the two entities shared profits, with Glendale receiving the "initial gross profits."[1669] Moreover, Coral assert that a trader tape put into evidence by the California Parties demonstrates that Glendale, not Coral, made the sale at NOB in the transaction that is potentially upstream from Coral's back-to-back sale to CERS.[1670]

### (b) Allegations of Fraud, Duress, and Bad Faith

1336. Coral states that despite acknowledging that Utah law governs the claims of fraud, duress, and bad faith, the California Parties ignore the legal definitions of these terms and claim that Mr. Taylor's common-sense interpretations are close enough. Coral argues that the legal definitions must be followed, and that Mr. Taylor's definitions are not, in fact, "close enough." Coral contends that by failing to allege that Coral's actions met the legal definitions of duress, fraud, or bad faith, the California Parties failed to make a *prima facie* case on any of these allegations.

1337. Coral avers that the cases cited by the California Parties in their initial brief demonstrate that they have not made the requisite showing of duress. For example, in

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volume – 30 transactions identified). Tr. 3985:10-16 (Tranen) (describing Screen 2, which requires a Coral sale at NOB and purchase back at COB from the same counterparty, but could be in a different volume – approximately 100 transactions identified). Tr. 3963:1-3964:15 (Tranen) (describing Screen 3, which requires a Coral sale at NOB and purchase back at COB, but could be from a different counterparty and different volume than the transaction at NOB – approximately 300 transactions identified).

[1668] Tr. 3012:13-3018:15 (Taylor).

[1669] Tr. 3929:11–12 (Tranen); Ex. CAT-123 (describing the profit sharing arrangement).

[1670] Ex. CAT-673 at 9-11; *see also* Tr. 2986:24-2987:9 (Taylor).

*Utah Power & Light Co.*, the Commission recognized that duress requires an "improper threat" and emphasized that "[e]conomic duress may not be implied merely from the making of a hard bargain."[1671] Thus, the Commission concluded that "economic pressure and 'even the threat of considerable financial loss' are not duress."[1672]

1338. With respect to fraud, Coral asserts that the only action the California Parties allege was fraudulent is False Export. However, Coral contends that the evidence shows that Coral never misrepresented the source of its power sales to CERS or anything else. Moreover, Coral notes that Mr. Taylor admitted that the harm in his "False Export" allegations was the alleged shifting of sales to real-time, not any misrepresentation.[1673]

1339. Coral also maintains that bad faith typically is not recognized as a separate claim under Utah law. Coral notes that the case cited by the California Parties dealt with whether an award of attorney's fees could be sustained based on "a finding that a party has attempted to avoid liability by testifying falsely … *combined with* a finding of bad faith."[1674] Coral further states that the California Parties describe the elements of bad faith in their initial brief, but make no attempt to match these elements to any of Coral's sales to CERS.

1340. Coral argues that the California Parties claims of bad faith are insufficient and based only on the fact that Coral received prices higher than CERS wanted to pay.[1675] Coral asserts that the law does not prohibit making opportunistic business decisions, and the Commission must find "evidence of unfairness, bad faith, or duress" consistent with relevant legal standards to avoid the *Mobile-Sierra* presumption.[1676]

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[1671] *Utah Power & Light Co.*, 38 FERC ¶ 63,038, at 65,240 (1987) (citing *Aircraft Assocs. & Mfg. Co. v. United States*, 357 F.2d 373, 378 (Ct. Cl. 1966)), *aff'd in relevant part*, 44 FERC ¶ 61,166 (1988).

[1672] *Id.* (citing *Int'l Tel. & Tel. Corp. v. United States*, 509 F.2d 541, 549 n.11 (Ct. Cl. 1975)).

[1673] Tr. 2611:6-2613:1 (Taylor).

[1674] *Valcarce v. Fitzgerald*, 961 P.2d 305, 315 (Utah 1998) (emphasis added).

[1675] *Pac. Gas & Elec. Co.*, 111 FERC ¶ 61,312, at P 9 (2005).

[1676] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008) (citing *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353 at 62,399-400 (2003)).

1341. Next, Coral argues that Mr. Taylor's *Power Markets Week* price screen improperly evaluates price first and then infers conduct. Coral states that fraud, duress, or bad faith can affect the contract negotiations that produce contract rates.[1677] Thus, causality begins with the contract formation stage that may result in high rates, not the other way around. Coral further states that Mr. Taylor's screen ignores the fact that Coral sold to CERS through back-to-back transactions, and that in many instances, Coral's purchase price of energy resold to CERS exceeded the screen.

1342. With respect to the California Parties claim that Respondents shifted their sales to real-time and created an "oligopolistic group," Coral argues that there is no evidence that it shifted sales.[1678] Moreover, Coral states that Mr. Taylor admitted that no "shift" ever occurred with respect to Coral's sales.[1679] Coral also asserts that the California Parties never before alleged the existence of an oligopoly, which has a specific legal meaning that the California Parties do not address.[1680] Regardless, Coral states that CERS had multiple purchasing options and did not always buy from Coral.[1681]

1343. Coral also contends that the California Parties improperly rely on a series of Coral emails that were discredited at hearing.[1682] Additionally, Coral argues that trader tapes demonstrate that its sale on January 26 Hour-Ending 24 was at the initiated by CERS traders asking Coral to procure more resources.[1683] Coral notes that in this transaction it charged CERS $625 per MWh even though CERS had offered to pay $675 per MWh.[1684] Coral concludes that it was acting in the public interest by assisting CERS to find additional energy at a price lower than CERS was willing to pay, and that Coral traders joking about a "parking space in hell" in an email is immaterial. Coral argues that the

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[1677] *See id*.

[1678] *See* Ex. SNA-1 at 15:23 ("CERS'[s] demand appeared more in the real-time markets").

[1679] *See* SNA-14; Tr. 2665:18-21 (Taylor).

[1680] *See Bailey v. Allgas, Inc.*, 284 F.3d 1237, 1251 (11th Cir. 2002).

[1681] *See, e.g.*, Ex. CAT-360.

[1682] Tr. 2691:7-2694:1 (Taylor).

[1683] Ex. SNA-39; Ex. SNA-40.

[1684] Ex. SNA-40; Ex. SNA-41.

California Parties' reliance on such documents reflects its strategy of cherry-picking the facts and taking trader shop-talk out of context to concoct a story that simply is not true.

1344. Coral also asserts the California Parties cited zero evidence for its allegation that Ms. Bowman "created [an environment] in which, as a matter of corporate policy, [traders] were required to exploit CERS'[s] weakened position."[1685]

1345. Next, Coral avers that the California Parties mistake rational economic behavior as evidence of wrongdoing. Coral states that like all sellers, it sought higher prices just like CERS, as a buyer, sought lower prices. Coral asserts that the California Parties' claim that Coral waited "until CERS could not meet ISO load"[1686] before offering energy to CERS is contrary to the evidence, which demonstrates that Coral sold both during ISO stage emergencies and during hours without stage emergencies. Furthermore, Coral contends that the California Parties conducted no pivotal supplier analysis to support its assertion that Coral waited to sell to CERS until it became a pivotal supplier.[1687]

1346. Lastly, Coral argues that the California Parties' allegation that certain Coral sales to CERS "clearly were fraudulent" has no basis in evidence.[1688] Coral notes that Mr. Taylor admitted that he did not allege that these transactions constituted "fraud" apart from his allegations of "False Exports."[1689]

### (c) Allegations of Undue Price Discrimination

1347. Coral argues that the California Parties failed to demonstrate that the entities compared in their undue discrimination analysis were similarly situated. Rather, Coral contends that the California Parties attempt to reverse the burden of proof and trivialize Respondents' criticisms.

1348. With respect to the California Parties' claim that Professor Hogan inappropriate compared to CERS to Argentina, Coral asserts that the California Parties mischaracterize and misunderstand Professor Hogan's comparison. Coral states that Professor Hogan did not perform and nowhere purports to have performed a credit "analysis" of CERS

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[1685] California Parties Initial Br. at 34.

[1686] *Id.* at 35-36.

[1687] Tr. 2696:6-8 (Taylor).

[1688] Tr. 3953:1-3955:4 (Tranen).

[1689] Tr. 2610:8-10 (Taylor).

because Respondents have no affirmative burden of proof. Rather, Professor Hogan looked to the contemporaneous seller expressions of how they perceived the risk of selling to CERS as the best evidence of what that risk was at the time and found the perceived risk to be very great.[1690] Coral states that in comparing extending credit to CERS to Argentina's sovereign debt, Professor Hogan was simply observing that there is no basis for Dr. Fox Penner's after-the-fact assumption that a junk bond represents a worst case for ascertaining how sellers at the time perceived the risk of extending credit to CERS.[1691] Coral notes that Professor Hogan explained that a junk bond is "not the worst case" comparison because what little was known about CERS at the time caused it to have "a very high probability of failure."[1692] Moreover, Coral asserts that Argentina was an apt comparison because at the time, CERS was similarly perceived as a default risk given the recent bankruptcies and defaults in the California energy markets.[1693]

1349. Lastly, Coral argues that Dr. Fox-Penner's opinions regarding an "appropriate premium" are irrelevant because they are based on information that could have only been known after the fact. Coral asserts that the California Parties' criticism that there are no contemporaneous Coral calculations of a risk premium ignores the fact that when CERS first came into existence, there was no information on which a calculation could be made.[1694] Coral states that given the risk, it set credit limits and minimum acceptable price margins for its traders. Coral notes that the credit limits were set by Coral's credit department, just as it did for Coral's other counterparties,[1695] and the trade desk periodically set *minimum* price margins.[1696] Coral contends that the California Parties

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[1690] Tr. 4089:22-4090:8, 4149:23-4150:6 (Hogan); *see also* Ex. S-13 at 30:18-21; Tr. 4038:14-4039:2 (Bowman).

[1691] Ex. CAT-161 at 26.

[1692] Ex. PNR-1 at 19.

[1693] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 94 FERC ¶ 61,132 (2001); *see* Ex. SNA-3.

[1694] Ex. SNA-1 at 9:13-17.

[1695] Ex. SNA-5; Ex. CAT-137; *see* Tr. 4037:19-4038:2 (Bowman).

[1696] Ex. CAT-137; Tr. 4038:20-4039:2 (Bowman).

inappropriately argue from hindsight that Coral's concerns did not justify its risk premium.[1697]

### (d) Allegations of False Export

1350. Coral argues the California Parties misrepresent Commission precedent and mistakenly reference violations of the CAISO tariff. Coral asserts that the California Parties ignore the Commission's clear holding that what made a False Import objectionable was that it evaded an applicable price cap.[1698] Thus, Coral concludes that there is no Commission precedent condemning so-called False Exports.

1351. Coral also contends that the California Parties wrongly rely on section 2.1.3 of the California MMIP[1699] and sections 2.2.11.1.1–2 of the California ISO Tariff.[1700] Coral states that it sales at issue were not made pursuant to the CalPX or ISO Tariff, and even if they were, the California Parties failed to show how a "False Export" violated any of the provisions. Coral states that whenever CERS asked about the source of the power it bought, Coral was honest and forthcoming in its answers.[1701] Furthermore, Coral notes that the California Parties concede that any "False Export' was only an "implicit" tariff violation.[1702]

1352. Next, Coral argues that its back-to-back sales do not fit into Mr. Taylor's False Export definition. Coral states that Mr. Taylor assumes that Coral sold to CERS out of a portfolio of power purchases and did not associate Coral's supposed "False Exports" with

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[1697] Ex. S-13 at 30:17-21.

[1698] *Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at PP 38-39 (2003); *Am. Elec. Power Serv. Corp.*, 106 FERC ¶ 61,020, at P 88 (2004).

[1699] Section 2.1.3 prohibits gaming or taking unfair advantage of the rules and procedures set forth in the CalPX or ISO tariffs. Ex. CAT-147 at 158.

[1700] These sections involve information submitted by a scheduling coordinator to the California ISO, specifically the Location Code of the Take-Out Point and the quantity, in MWh, of Demand being served at each Take-Out point for which a schedule has been submitted. Ex. CAT-147 at 22.

[1701] *See* Ex. SNA-1 at 17:3-10.

[1702] *Id.* at 56.

any specific Coral exports.[1703] Coral notes that in his rebuttal testimony, Mr. Taylor alleged only that each back-to-back sale to CERS "*could be* the completion of a False Export transaction," if Coral's purchase in the Pacific Northwest was from a "parking" provider.[1704] However, Coral asserts that Mr. Taylor provided no evidence of parking and no evidence connecting any of Coral's back-to-back sales with an export out of the ISO.[1705] Moreover, Coral notes that Mr. Taylor claimed that he would find Coral's sales to CERS objectionable even if his "False Export" allegations were simply fabrications.[1706]

1353. Lastly, Coral avers that the California Parties' initial brief alleges 139 hours of False Export, but only discusses transactions associated with allegations that Mr. Taylor has withdrawn.[1707] Coral asserts that the California Parties now contend in their initial brief that these withdrawn transactions are False Exports or *could be* False Exports. Coral contends that even if these transactions are considered, they do not meet Mr. Taylor's False Export definition. First, Coral states that the "upstream" transaction does not involve scheduling energy out of the ISO because each transaction was coming out of the City of Glendale, Mead, or NOB.[1708] Second, Coral states that the California Parties define "False Export" in their Initial Brief's Glossary as a transaction in which a seller "falsely represent[s] that it was importing the power into California for sale in Real Time."[1709] However, Coral states that all its sales to CERS were outside California at COB.

1354. Third, with respect to the alleged additional 300 hours identified by Mr. Tranen, Coral states that Mr. Taylor does not allege that any of these hours were "False Exports."

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[1703] Tr. 2583:22-2585:8, 2643:8-11 (Taylor).

[1704] Ex. CAT-289 at 127:23-24 (emphasis added).

[1705] *Id.* at 127:16-21; Tr. 2600:25-2601:21 (Taylor).

[1706] Ex. CAT-289 at 128:21-23.

[1707] Coral states that Mr. Taylor withdrew all of his multiparty False Export allegations in his pre-filed Rebuttal Testimony and confirmed at hearing he no longer alleged that these transactions were False Exports. Ex. CAT-289 at 129:4-9; Tr. 2572:6-2573:12, 2664:23-2666:10, 2964:2-5, 2760:12-23, 3010:20-3011:8 (Taylor).

[1708] Ex. CAT-041 at 87:13-88:5.

[1709] California Parties Initial Br. at xii.

Coral also asserts that the California Parties fail to point to any law, rule, order, or tariff that these transactions are alleged to violate. Although the California Parties allege that the transactions were "clearly fraudulent," Coral avers that the California Parties failed to demonstrate any harm associated with the transactions - i.e. that energy could have been purchased for less in California.[1710] Coral also notes that the California Parties ignore the fact that CERS requested energy at COB. Coral further states that the California Parties cite no law, rule, order, or tariff that would have required Coral to inform CERS of the energy's generation source or trace the complete genealogy of that power from source to sink.

**(e) Allegations that Respondents Exercised Market Power**

1355. Coral first states that the California Parties both "conclu[de] that Coral exercised market power,"[1711] and assert that Coral did not exercise market power.[1712] Coral suggests that this confusion arises from the fact that Dr. Reynolds never alleged that Coral actually possessed or exercised market power. Coral asserts that to the extent the California Parties are now alleging that Coral possessed and exercised market power, there is no evidentiary support for such an allegation.

1356. Coral also argues that Dr. Reynolds's conclusory statement that Coral realized higher prices for higher volumes is not an independent basis for finding that Coral exercised market power. Coral states that the California Parties' direct evidence is premised on the Dr. Reynolds' tests to support his agglomeration theory. However, as noted above, because Coral did not sell from a portfolio or resources, there is no evidence that Coral engaged in such a strategy.

1357. Next, Coral contends that the California Parties inappropriately rely on *Toys "R" Us*, a case involving explicit collusion among competitors that constituted a *per se* illegal boycott.[1713] Coral states that the Ninth Circuit has instructed that market power may be demonstrated either through "direct evidence of injurious exercise of market power" or

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[1710] *Dugan v. Jones*, 615 P.2d 1239, 1246 (Utah 1980) (providing the elements of actual fraud, including harm).

[1711] California Parties Initial Br. at 80; *see also id.* at B-10.

[1712] *Id.* at 90.

[1713] *Toys "R" Us v. FTC*, 221 F.3d 928, 933-34 (7th Cir. 2000).

"circumstantial evidence pertaining to the structure of the market."[1714] With respect to direct evidence, the court stated that "[i]f the plaintiff puts forth evidence of restricted output and supracompetitive prices, that is direct proof of the injury to competition which a competitor with market power may inflict, and thus, of the actual exercise of market power."[1715] Coral avers that the California Parties have not shown that Coral's prices were supracompetitive[1716] or that Coral withheld electricity.[1717] Thus, Coral concludes that the California Parties claim is legally insufficient to establish through direct evidence.[1718] With respect to circumstantial evidence of market structure, Coral states that the California Parties submitted no market analyses. Lastly, Coral notes that the Commission previously rejected the California Parties' argument that the best evidence of market power is direct evidence.[1719]

#### (f) Unlawful Activity Directly Affected Negotiation of Specific Bilateral Contracts, Resulting in Unjust and Unreasonable Rates

1358. Coral argues that the California Parties exaggerate the number of contracts that could possibly be affected by market manipulation. Coral notes that in the Order on

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[1714] *Rebel Oil Co. v. Atl. Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir. 1995) (citing *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 460-61 (1986)); *see Forsyth v. Humana, Inc.*, 114 F.3d 1467, 1475 (9th Cir. 1997).

[1715] *Rebel Oil Co. v. Atl. Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir. 1995).

[1716] Coral notes that its prices reflected prevailing market prices. Ex. CAT-414.

[1717] *See* Tr. 2651:6-8 (Taylor); Ex. SNA-9 at 26:9-10.

[1718] *See Forsyth*, 114 F.3d at 1476 ("The plaintiffs submitted evidence that Sunrise Hospital routinely charged higher prices than other hospitals while reaping high profits. With no accompanying showing of restricted output, however, the plaintiffs have failed to present direct evidence of market power.").

[1719] *See California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 129 FERC ¶ 61,276, at PP 7-8 (2009); *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 139 FERC ¶ 61,211, at PP 10-11 (2012).

Remand, the Commission held that the *Mobile-Sierra* presumption will apply absent evidence of "extensive unlawful market manipulation."[1720]

1359. Coral states that the California Parties allege that between 131 and 133 of CERS's contracts with Coral were the product of unlawful market behavior.[1721] Coral notes that this included all allegations of duress, fraud, and bad faith, undue price discrimination, and False Export. However, Coral asserts that duress, fraud, and bad faith are not the "market manipulation" that the Commission was referring to. Coral states that in *Morgan Stanley*, the basis of the Commission's statement, the Court distinguished between "traditional grounds for the abrogation" of a contract, like fraud, duress, and bad faith, and unlawful market activity.[1722] Additionally, Coral argues that undue price discrimination is not a type of market manipulation, but rather a separate violation under the Federal Power Act.[1723]

1360. Coral states that the only alleged violation that would constitute market manipulation is Mr. Taylor's "False Export," which the California Parties allege affected between 36 and 47 contracts between Coral and CERS. Coral concludes that considering the thousands of contracts CERS entered into during the relevant period and the $2.67 billion spent by CERS on spot market purchases in the Pacific Northwest, between 36 and 47 contracts cannot possibly constitute "extensive" market manipulation sufficient to alter the playing field and avoid the *Mobile-Sierra* presumption.[1724]

### (g) Legitimate Business Behavior by Coral

1361. Coral contends that its activities during the relevant period were normal for a power marketer in a competitive market. Coral avers that the California Parties allegation that its risk premium was just profit maximizing ignores the fact that the risk premium was designed to cover both Coral's concern about nonpayment or future clawback, as well as to ration a counterparty's credit throughout the monthly billing

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[1720] Order on Remand at P 20 (citing *Nev. Power Co. v. Enron Power Mktg., Inc.*, 125 FERC ¶ 61,312, at P 3 (2008)).

[1721] *Compare* California Parties Initial Br. at 89-90 *with* Initial Br. at B-7–B-10.

[1722] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 5554 (2008).

[1723] *Compare* 16 U.S.C. § 824e (2012) *with* 16 U.S.C. § 824v (2012).

[1724] *See* Ex. CAT-037 at 8:3-5.

cycle.[1725] Coral notes that Ms. Bowman stated that the risk premium was not capped and could include additional profit available in the marketplace.[1726] Thus, Coral states that it was only acting to maximize profit, as all marketers do.[1727]

### 8. Commission Trial Staff Reply Brief

#### (a) Standard of Proof and Relevant Law

1362. Trial Staff states that the California Parties reframe the proceeding as presenting "the simple question of whether, as Respondents and Staff maintain, there is no limit under the FPA to what Respondents may charge for power, or, whether, as the California Parties maintain, the rates that Respondents charged CERS are subject to the FPA's 'just and reasonable' mandate."[1728] Trial Staff's also asserts that the California Parties describe Trial Staff's position as, "under the Commission's market-based rate scheme, the FPA has become an empty shell that offers no protection at all to ratepayers."[1729] Trial Staff argues that the by reframing the purpose of the proceeding, the California Parties attempt to circumvent the Commission's specific directions in this case, confuse the issues, and mischaracterize Trial Staff's testimony.

1363. Trial Staff also contends that the California Parties' oversimplification of the proceeding wrongly conflates "just and reasonable rates" with a cost-based "zone of reasonableness." Trial Staff asserts that no party in this proceeding suggests that rates do not have to be just and reasonable. However, a zone of reasonableness predicated on cost is a standard employed by the Commission and reviewing courts to determine justness and reasonableness under a cost-based regulatory regime, not a market-based regime.

1364. Trial Staff further argues that the California Parties' assertion that Trial Staff's position is not compatible with *Morgan Stanley* is unfounded. Trial Staff states that the Supreme Court in *Morgan Stanley* clearly found that a cost-based zone of reasonableness

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[1725] Tr. 4063:14-4064:17 (Bowman).

[1726] Tr. 4036:13-4037:7, 4038:14-4039:5, 4045:11-20, 4063:23-4064:20 (Bowman).

[1727] Tr. 4038:20-4039:2 (Bowman).

[1728] California Parties Initial Br. at 4.

[1729] *Id*.

method is inappropriate for market-based rates.[1730] Trial Staff asserts that Ms. Steffy's statement that there was "no zone of reasonableness" was made in the context of the Commission having determined that the seller did not have market power.

### (b) Allegations of Fraud, Duress, and Bad Faith

1365. Trial Staff states that the California Parties failed to distinguish between duress, fraud, or bad faith as separate contentions, claiming that that there was no reason to do so.[1731] Rather, the California Parties base their allegations on the view that CERS was dealing from a weak position and the contracts do not reflect parties of equal bargaining power, and that each Respondent preyed on CERS's weak bargaining position.

1366. Trial Staff states that the California Parties agree that the Commission applies the governing state contract law, in this case Utah, in deciding whether there was duress, fraud, or bad faith in the formation of the contract. Trial Staff also notes that the California Parties do set forth separate legal definitions for duress, fraud, and bad faith despite claiming that there is no need to distinguish between the three allegations. However, Trial Staff asserts that the California Parties failed to apply these separate definitions to the specific contracts at issue in this case.

1367. Next, Trial Staff argues that the California Parties' wrongly contend that CERS's weak bargaining position is sufficient to make claims of fraud, duress, or bad faith. Trial Staff notes that the California Parties generally dismiss the actual trader tapes that clearly show CERS traders offering a higher price than demanded or simply agreeing to the price offered by the Respondents without any attempt to counter the offered price.[1732]

1368. Trial Staff states that the California Parties rely on Mr. Taylor's price test for their allegations of fraud, duress, or bad faith. Trial Staff asserts that this test is not evidence of fraud, duress, or bad faith, and the Commission specifically held that that "simply identifying high prices [is not] sufficient to overcome or avoid the [*Mobile-Sierra*] presumption."[1733] Moreover, Trial Staff notes that in the long-term contracts case, the Commission concluded that CDWR had options and that the rate, terms and conditions of

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[1730] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 549-50 (2008).

[1731] Tr. 2382:9-13 (Taylor).

[1732] Ex. TRC-171 through TRC-177.

[1733] Order Granting Interlocutory Appeal at P 15.

the long-term contracts indicate that the contracts were not the product of unequal bargaining power.[1734] Thus, Trial Staff concludes that it would be surprising if CDWR's expertise and bargaining power in negotiating long-term bilateral contracts were completely absent from its balance-of-month, day-ahead, and day-of trading activities.

### (c) Allegations of Undue Price Discrimination

1369. Trial Staff states that the California Parties' price discrimination analysis (1) does not show that similarly situated customers were treated differently and (2) does not show that the difference, if any, was unjustified. Trial Staff states that its initial brief demonstrates the flaws in Dr. Fox-Penner's analysis in more detail.

1370. Next, Trial Staff addresses the California Parties' claim that undue price discrimination was possible because a limited set of sellers knew that CERS had to buy large amounts of energy in real-time. Trial Staff notes that the California Parties cite to no evidence in the record to support this claim. Trial Staff asserts that there is no basis to claim that only a limited number of sellers knew of CERS's position because the rolling blackouts, political uproar and media coverage surrounding the energy crisis.[1735] Furthermore, Trial Staff notes that Ms. Lee testified that "[s]ellers knew from the start that CERS was a buyer and that it fell to CERS to go out to try to meet the extremely high demand by purchasing bilaterally" and "of course [this] was obvious to any individual seller."[1736] Trial Staff also asserts that the California Parties claim ignores evidence that demonstrates that CERS's limited options were the result of credit concerns and the ISO's directive to purchase only at COB, neither of which can be blamed on the Respondents.

1371. Lastly, Trial Staff notes that the California Parties' initial brief does not attempt to defend Dr. Fox-Penner's use of long-run and short-run marginal costs as evidence that prices were economically inefficient.

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[1734] *Pub. Util. Comm'n of Cal. v. Sellers of Long Term Contracts,*103 FERC ¶ 61,354, at PP 42-60 (2003), *order on reh'g and clarification*, 105 FERC ¶ 61,182 (2003).

[1735] *See, e.g.*, Ex. CAT-012 at 3:18-4:20; Ex. CAT-022 at 7:7-8.

[1736] Ex. CAT-022 at 7:14-20.

### (d) Allegations of False Export

1372. Trial Staff asserts that the California Parties have not demonstrated that False Export was a violation of the CAISO tariff. Trial Staff notes that the provisions alleged to have been violated, the MMIP and provisions dealing with operating requirements and with scheduling and bidding, were not discussed by the California Parties. Trial Staff further notes that the California Parties failed to produce contract specific evidence demonstrating that the required information was not submitted.

1373. Trial Staff states that the California Parties also rely on Mr. Taylor's implicit understanding that the scheduling requirements would not be intentionally inaccurate or misleading. However, Trial Staff asserts that the California Parties again failed to show that specific schedules applicable to the alleged False Export transactions were inaccurate, purposefully or otherwise.

1374. Next, Trial Staff avers that the California Parties rely on the on the Commission's findings related to False Import in its Gaming Order.[1737] However, Trial Staff states that the California Parties reliance upon these rulings is misplaced and misleading. Trial Staff notes that False Import violations were premised on the party attempting to evade a price cap, whereas the False Export allegations do not involve such a price cap. Furthermore, Trial Staff states that on rehearing of the Gaming Order, the Commission rejected the California Parties' request to expand False Import to include transactions, among other things, that did not exceed the price cap.[1738] Specifically, the Commission found that the "*essence of the false representation* in False Import is that the seller falsely represented the energy as an import in order to make an OOM transaction and receive a price above the cap."[1739]

1375. Lastly, Trial Staff asserts that the California Parties have not demonstrated that the False Exports were harmful. Trial Staff states that the California Parties provided no evidentiary support for its claims that False Exports (1) hastened the financial collapse of the IOUs; (2) strengthened Respondents' bargaining power over CERS; and (3) created misleading shortage signals within the day-ahead energy market.[1740]

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[1737] *Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at P 39 (2003).

[1738] *Am. Elec. Power Serv. Corp.*, 106 FERC ¶ 61,020, at PP 87-88 (2004).

[1739] *Id*. P 88 (emphasis added).

[1740] *See Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at P 63 n.69 (2003) (to the extent this practice does not involve collusion with other market participants, it

(continued…)

**(e) Allegations that Respondents Exercised Market Power**

1376. Trial Staff argues that the California Parties confuse the issue of market power by claiming that the Commission's market power screens are irrelevant and shifting the burden to the Respondents, stating that Respondents did not refute the California Parties' direct evidence of market power.

1377. Trial Staff contends that the California Parties wrongly assert that the Commission's market power screens that were used to determine the exercise of market power during the CERS Period are outdated and irrelevant. Trial Staff argues that none of the California Parties' justifications are sufficient to cast aside the market power test used by the Commission during the CERS Period.

1378. Trial Staff further notes that in the *Lockyer* proceeding, the Commission reiterated that it "is required to use the standards for assessing market power of market-based rate sellers … in effect at the time the transaction took place."[1741] The Commission explained that "doing otherwise would 'violate the requirement that all jurisdictional sellers be on notice as to what test will be applied to them' and would constitute the 'retroactive establishment of agency rules and tests.'"[1742] Trial Staff avers that this same rationale applies equally in this proceeding.

1379. Next, Trial Staff asserts that the California Parties presume that their claims that Respondents exercised market power have been established and allege that the Respondents failed to refute these claims. Trial Staff contends that this is an improper attempt to shift the burden of proof to the Respondents. Trial Staff states that the California Parties failed to make a *prima facie* case on this issue because Dr. Reynolds did not use the applicable Commission market power test and the tests that were used by Dr. Reynolds were seriously flawed.

1380. With respect to the California Parties' discussion of Dr. Savitski's testimony, Trial Staff asserts that the California Parties do not establish any causal links between price

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"represents legitimate economically rational attempts by the market participants to maximize their profits").

[1741] *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, Opinion No. 512, 135 FERC ¶ 61,113, at P 39 (2011) (*Lockyer*).

[1742] *Id*. (quoting *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 125 FERC ¶ 61,016, at P 30 (2008)).

and quantity, and attempt to shift the burden to Trial Staff to demonstrate that "this variable issue" affected any indication of market power by larger sellers.

1381. Trial Staff also contends that the California Parties' criticisms of Dr. Savitski's critiques regarding emergency stage variables, hourly observations, and product market are unfounded. Trial Staff avers that the California Parties attempt to direct attention away from Dr. Reynolds' flawed analysis by stating that Dr. Savitski failed to analyze the content of Dr. Reynolds' market power analyses and made no attempt to produce any of his own empirical analyses.

1382. Additionally, Trial Staff states that the California Parties contend that Dr. Savitski was incorrect in claiming that emergency stage results were inconsistent with the exercise of market power, relying on Dr. Reynolds' testimony that he included variables in his regression analysis to control for the independent effects of "ISO Emergencies." However, Trial Staff argues that regardless of which variables were included in Dr. Reynolds' analysis to control for emergency stage conditions, the point is that the results are inconsistent with the contention that CERS was subject to extreme market power. Trial Staff states that if Dr. Reynolds' results were consistent with the California Parties' contention, emergency conditions would signal the sellers that the market is tight and they have even more market power with which to demand higher prices than in non-emergency periods.[1743] Trial Staff asserts that Dr. Reynolds' analyses do not find this to be the case.

### B. Findings and Conclusion

1383. Initially this proceeding encompassed a number of other Respondents who have since settled, but whose active participation in earlier stages of this contentious and lengthy litigation have left behind a voluminous and complex record to sift out and weigh as it pertains to the two remaining Respondents to claims raised by the California Parties, TransCanada and Coral (Coral Power LLC, predecessor to Shell Energy North America (US), L.P.).[1744] This challenge is all the more daunting because the California Parties

[1743] Ex. S-13 at 38.

[1744] The Phase I hearing commenced on August 27, 2013 and ended on October 24, 2013, with testimony by 33 witnesses during 24 hearing days over 7 weeks (excluding a two-week recess). The scheduled hearing days and witnesses were substantially reduced as the result of settlements between Powerex Corp. and the California Parties and between Powerex Corp. and the City of Seattle that were reached just prior to and during the hearing, respectively. Settlements post-hearing have been reached between the California Parties and Avista Utilities, Avista Energy, and TransAlta. By stipulation of the parties and the Chief Judge's Order Granting Procedural

(continued…)

have raised many general allegations of unlawful market activity that have not been particularized to these two remaining Respondents.

### 1. The California Parties Failed to Demonstrate that TransCanada Engaged In Unlawful Market Activity

1384. This section of the Initial Decision will address the claims pending for adjudication pertaining to TransCanada, noting that TransCanada's first sale to CERS during the CERS Period occurred on January 31, 2001.[1745]

1385. To *avoid* the *Mobile-Sierra* presumption that the specific bilateral contracts the California Parties seek to abrogate are just and reasonable under Issue 1(A), the California Parties bear the burden of demonstrating that TransCanada engaged in "unfair dealing at the contract formation stage,"[1746] which "alter[ed] the playing field for contract negotiations,"[1747] and had "a causal connection … [to] the contract rate."[1748] In other words, TransCanada must have "engaged in unlawful market activity in the spot market and … such unlawful activity directly affected the particular contract or contracts to which [TransCanada] was a party."[1749] For the reasons discussed below, not only have the California Parties failed to demonstrate that TransCanada engaged in such unlawful activity, but the California Parties have failed to demonstrate any causal connection between their allegations of unlawful activity and the specific bilateral contracts entered into between TransCanada and CERS.

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Relief, issues between those settling parties are not addressed in this Initial Decision. *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Mar. 6, 2014) (Order of Chief Judge Suspending Initial Decision as to the California Parties' Allegations Against Settling Parties and Granting Brief Extension of Initial Decision Date).

[1745] Ex. TRC-222 at 1.

[1746] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008).

[1747] *Id*. at 554; Order on Remand at P 20.

[1748] *Morgan Stanley*, 554 U.S. at 555.

[1749] Order on Remand at P 21.

**(a) The California Parties Failed to Demonstrate that TransCanada Had or Exercised Market Power**

1386. The California Parties' Initial Brief included charts to specify the claims they alleged against each of the Respondents.[1750] None of these charts include any allegations that TransCanada exercised market power.[1751] Indeed, given that the record reflects that TransCanada was typically selling between 13 MWh and 50 MWh in an hourly market in which total volume could exceed 3,900 MWh,[1752] allegations that TransCanada had or exercised market power are insupportable.

**(b) The California Parties Failed to Demonstrate that TransCanada Engaged in Fraud, Duress, or Bad Faith**

1387. The California Parties acknowledge that they have not distinguished between the three practices of fraud, duress or bad faith.[1753] The California Parties explain that they have shown their aggregated claims of fraud, duress, and bad faith using the same evidence because "each Respondent … collected a price that was far above the (already distorted) prevailing market price …"[1754]

1388. According to the California Parties:

> [t]he essence of the California Parties' "duress, fraud, or bad faith" claim is that each Respondent exploited CERS by charging a price far above the competitive market levels and well above the prices that Respondents

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[1750] *See* California Parties Initial Br. at 89-90, B-10 through B-12.

[1751] The California Parties list all alleged Issue 1(A) violations by Respondent. The table on pages 89-90 of the Initial Brief lists all of the alleged forms of unlawful activity by Coral and TransCanada. The last row on page 90 relates to the exercise of market power and has no indication that there is any claim being made against TransCanada. In Appendix B of the Initial Brief, nowhere on pages B-10 through B-12, the pages that list all of the alleged 1(A) violations against TransCanada, is there a claim that TransCanada exercised market power. *Id.*

[1752] *See* Ex. TRC-82 at 136 (total of 3,965 MWh in hour ending 24).

[1753] California Parties Initial Br. at B-10 through B-12.

[1754] California Parties Initial Br. at 23 (stating that Mr. Taylor did not distinguish between the three practices and that "there was no reason to do so").

> charged other buyers, because Respondents knew that CERS, which was required to obtain the energy critical to reliable ISO operation, lacked reasonable alternatives.[1755]

1389. The principle evidence provided by the California Parties in support of these claims is Mr. Taylor's *Power Markets Week* plus $75 per MWh test,[1756] a generic "benchmark" screen that does not take into account in any way the actual contract negotiations that occurred between the parties regarding specific contracts. Rather, the transactions for which Mr. Taylor allegedly finds evidence of duress, fraud, or bad faith are primarily those in which the price charged to CERS was greater than the highest price recorded in *Power Markets Week* for COB or Mid-C, plus $75/MWh.[1757] Even assuming *arguendo* that the *Power Markets Week* price test provides a reasonable benchmark for measuring the prevailing Pacific Northwest market price, a point strongly contested by TransCanada,[1758] such a generic benchmark does not establish evidence of duress, fraud, or bad faith in the formation of the contract. Indeed, the Commission has squarely rejected the California Parties' argument that "simply identifying high prices should be sufficient to overcome or avoid the [*Mobile-Sierra*] presumption."[1759]

1390. To demonstrate "*unlawful activity*" of fraud, duress or bad faith sufficient to *avoid* the *Mobile-Sierra* presumption that these bilaterally negotiated contracts are just and reasonable, something more than identifying high prices is required. Specifically, duress requires "an improper threat" on the part of the wrongdoer, while fraud requires a material representation that the representor knew was false, while bad faith requires an

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[1755] *Id*. at 21.

[1756] *Id*. at 29, 41-42.

[1757] *Id*. at 29. Mr. Taylor excluded instances in which the Respondents charged other purchasers higher prices during the same hours and those transactions in which some evidence (for example, trader tapes) suggested that the seller may not have been attempting to exploit CERS. *Id.* at 29-30 & n.102.

[1758] *See* TransCanada Initial Br. at 22-29. TransCanada states that the *Power Markets Week* reported after the fact, day-ahead peak and off-peak pricing that was assembled by phone calls to energy companies that voluntarily reported their sales. Thus, TransCanada concludes that the *Power Markets Week* data may not reasonably reflect the prices in the marketplace. *Id.*

[1759] Order Granting Interlocutory Appeal at P 15.

act of fraud or deception prompted by a sinister motive.[1760] General allegations of "unconscionable margins" based on a formulaic post hoc application of Mr. Taylor's *Power Markets Week* screen are insufficient to support a finding that TransCanada acted with fraud or deception, as required for a showing of "bad faith" in its negotiations.[1761]

1391. Although the California Parties assert that there is no need to distinguish between allegations of duress, fraud, or bad faith, they did provide the appropriate separate legal definitions for duress, fraud, and bad faith in their Initial Brief.[1762] Trial Staff correctly observes that the California Parties must apply these separate definitions to the facts of this case in order for the undersigned Presiding Judge to find that "a particular seller engaged in unlawful market activity in the spot market," which directly affected the particular contracts to which that seller was a party.[1763] Thus, the California Parties must first show that TransCanada engaged in duress, fraud, or bad faith in the formation of the subject contracts by applying the appropriate legal definitions, and then demonstrate that such activity directly affected those contracts to which it was a party.[1764] The California

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[1760] *See* TransCanada Initial Br. at 15-18. Duress requires "an improper threat" on the part of the wrongdoer, while fraud requires a material representation that the representor knew was false, and bad faith requires an act of fraud or deception prompted by a sinister motive. *Utah Power & Light Co.*, 33 FERC ¶ 63,001, at 65,003-04 (1985), *aff'd*, 41 FERC ¶ 61,308, at 61,807 (1987). *See Andreini v. Hultgren*, 860 P.2d 916, 921 (Utah 1993) ("We … explicitly adopt the legal standards of duress set forth in sections 175 and 176 of the Restatement (Second) of Contracts"); *State Bank v. Troy Hydro Sys.*, 894 P.2d 1270, 1275 (Utah Ct. App. 1995) ("Utah has adopted the legal standards of duress set forth in sections 174 through 176 of the Restatement (Second) of Contracts"); RESTATEMENT (SECOND) OF CONTRACTS § 175(1) (1979).

[1761] Order on Rehearing at P 25.

[1762] *See* California Parties Initial Br. at 22 & notes 77-79.

[1763] Order on Remand at P 21.

[1764] Mr. Taylor's price test, and the California Parties' claims regarding TransCanada's profit margins, inappropriately assumes unlawful market activity by the seller. Under the analysis applicable to Issue 1(A), the California Parties must first establish that the seller has "engaged in unlawful market activity in the spot market" and then may examine prices to determine whether "… such unlawful activity directly affected the particular contract or contracts to which the seller was a party."

Parties did not make this showing for any of the ninety-one TransCanada contracts that Mr. Taylor identified under his benchmark screen for fraud, duress, or bad faith.[1765]

1392. The only specific activity by TransCanada that the California Parties alleged constituted bad faith involved parking of energy for a handful of hours on March 20 and 21, 2001.[1766] As support for their claim that TransCanada engaged in bad faith in connection with the two parking transactions, the California Parties rely on deal tickets that reflect the fact that there were two parking transactions and TransCanada's intention to park energy.[1767] The California Parties argued that "TransCanada undertook its parking transactions not for legitimate reasons, but for the purpose of withholding energy so that it could be sold in Real Time."[1768] However, the California Parties failed to rebut Mr. Kunz's testimony that "[t]he times at which these offers were made to CERS were consistent with TransCanada's typical practice when marketing light load hours. They were also consistent with the times of day at which CERS had indicated an interest in purchasing such hours in previous telephone conversations."[1769] Furthermore, there is no indication that TransCanada used the parking transactions to conceal *from CERS* the source of the energy that was provided to CERS. Ninety percent of the energy that TransCanada sold to CERS was sourced from the PPoA[1770] and the transcripts of the trader tapes demonstrate that CERS traders were aware of the source of the energy that they were purchasing from TransCanada.[1771] The California Parties failed to provide any evidence demonstrating that TransCanada engaged in bad faith in undertaking the two

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[1765] *Cf.* California Parties Initial Br. at B-10 (identifying 91 "contracts"); *see also* Ex. TRC-178 (listing 91 transactions at issue); Ex. CAT-412.

[1766] *See* California Parties Initial Br. at 39-40 (citing Ex. CAT-117). Only one instance of parking is identified in the California Parties Initial Brief, but two were identified by Mr. Taylor. Ex. CAT-041 at 12:14-15, 84:17-86:2, 107:21-23.

[1767] California Parties Initial Br. at 40 n.147 (quoting a handwritten note on the deal ticket that said "sold to preschedule in order to park & move hourly in real time …") (citing Ex. CAT-041 at 84-85; Ex. CAT-117).

[1768] California Parties Initial Br. at 121.

[1769] Ex. TRC-77 at 45:1-5; *see also* TransCanada Initial Br. at 35.

[1770] Ex. TRC-77 at 5:4-6:2.

[1771] *See generally*, Ex. TRC-222.

parking transactions at issue or that these two parking transactions were not part of a legitimate business practice.[1772]

1393. Lastly, TransCanada was the only party in this proceeding to submit the trader tapes for every transaction between it and CERS.[1773] These trader tapes provide the "best evidence" of the actual contract negotiations between the parties. The trader tapes demonstrate that the parties often engaged in no negotiations at all, with either CERS or TransCanada merely accepting the offered price.[1774] On other occasions, the TransCanada and CERS traders negotiated until an agreed upon price was reached.[1775] However, nothing in these negotiations demonstrate "duress, fraud, or bad faith" on the part of TransCanada.

#### (c) The California Parties Failed to Demonstrate Undue Discrimination by TransCanada

1394. The California Parties assert that TransCanada "unduly discriminated against CERS during the CERS Period" by charging "CERS more than they were charging similarly-situated customers for the very same product in the very same markets …."[1776] The California Parties bear the burden of substantiating their allegation of undue discrimination[1777] by showing that "(1) two classes of customers are treated differently; and (2) that the two classes of customers are similarly situated."[1778]

1395. In addition, the Commission has "long recognized" that rate differentials may be justified by cost or other factual differences between customers.[1779] Complainants must

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[1772] TransCanada Initial Br. at 34-37.

[1773] Ex. TRC-222.

[1774] *See, e.g., id*. at 1130-38.

[1775] *See, e.g., id*. at 278-79.

[1776] California Parties Initial Br. at 42.

[1777] *See Transwestern Pipeline Co.*, 36 FERC ¶ 61,175, at 61,433 (1986).

[1778] *Energy Transfer Partners, L.P.*, 120 FERC ¶ 61,086, at P 169 (2007).

[1779] *Village of Belmont v. Wis. Power & Light Co.*, 84 FERC ¶ 61,056, at 61,255 (1998) (citations omitted); *see Cities of Newark, New Castle & Seaford v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985).

address "the threshold issue of whether the rate disparity is nonetheless justified. … [R]ate differences are not, in and of themselves, evidence of undue discrimination."[1780] Furthermore, as the D.C. Circuit later explained regarding its ruling in *Town of Norwood*:

> This court noted in *Town of Norwood v. FERC* that the anti-discrimination mandate of section 205(b) should not be read to obliterate the public policy supporting private rate contracts between utilities and their customers. A fixed rate contract between the parties may justify a rate disparity, rendering it lawful under section 205(b).[1781]

1396. Looking at the specific evidence of record on this issue, the California Parties assert that TransCanada engaged in undue discrimination in just four "contracts"[1782] or 26 hours out of the 2,610 relevant delivery hours examined.[1783] The California Parties acknowledge that Dr. Fox-Penner identified less than one percent or only twenty-six of the hourly transactions between TransCanada and CERS during the CERS Period as unduly discriminatory.[1784] Further, Mr. Taylor confirmed that his data regarding undue discrimination was taken solely from Dr. Fox-Penner.[1785]

1397. To measure what he regarded as undue discrimination, Dr. Fox-Penner conducted a matched transaction comparison using a $50/MWh difference between the price TransCanada charged to CERS and the price TransCanada charged a different buyer as a

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[1780] *Village of Belmont*, 84 FERC at 61,255 (citations omitted).

[1781] *City of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984) (citing *Town of Norwood v. FERC*, 587 F.2d 1306, 1310 (D.C. Cir. 1978); *Boroughs of Chambersburg & Mont Alto v. FERC*, 580 F.2d 573, 577 (D.C. Cir. 1978)).

[1782] California Parties Initial Br. at 89, B-11 through B-12.

[1783] California Parties Initial Br. at 54; Ex. CAT-163 at 121.

[1784] California Parties Initial Br. at 54. Dr. Fox-Penner found only a limited number of hours during which TransCanada is alleged to have discriminated against CERS. Specifically, Dr. Fox Penner found only four hours based on matching sales and twenty-two hours based on his calculation of sales in excess of 6 standard deviations from the mean of sales in the Pacific Northwest during the same time period.

[1785] Tr. 2418:15-2419:10 (Taylor).

threshold.[1786] The California Parties assert that Dr. Fox-Penner's $50/MWh "buffer" was "an extremely conservative buffer given the hourly-price basis of the matched transaction comparison."[1787] TransCanada takes issue with the validity and/or appropriateness of Dr. Fox-Penner's $50/MWh threshold; but points out that even using Dr. Fox-Penner's analysis, the evidence of record still does not support a systematic pattern of undue discrimination by TransCanada. As Dr. Fox-Penner showed in Exhibit CAT-163, TransCanada made spot sales in the Pacific Northwest to parties other than CERS in just 14 of the 2,610 hourly sales during the CERS Period.[1788] While there were four hours when CERS paid at least $50/MWh more than other TransCanada customers,[1789] there were also four hours when CERS paid $50/MWh less than other TransCanada customers.[1790] Of the remaining six hours, CERS paid essentially the same price ($0.47/MWh less) than other TransCanada customers in five of the hours.[1791] This evidence of record is insufficient to support a finding of undue discrimination against TransCanada even assuming *arguendo* that the other TransCanada customers were similarly situated to CERS for purposes of such a comparison.

1398. In fact, the evidence of record when considered as a whole strongly supports a finding that CERS was "uniquely situated" as compared to other buyers in the Pacific Northwest market during the relevant time period in a number of material ways including the fact that CERS was required to obtain the energy critical to reliable ISO operation, credit risk issues, and the sheer volume of its energy purchases. In fact, Dr. Fox-Penner admitted that "CERS was a uniquely situated entity in the whole WECC."[1792]

1399. Furthermore, assuming *arguendo* that CERS was similarly situated to other buyers, Dr. Fox-Penner's standard deviation analysis fails to demonstrate undue price

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[1786] Dr. Fox-Penner applied a threshold of forty percent for transactions less than $125/MWh. Ex. CAT-161 at 71.

[1787] California Parties Initial Br. at 47.

[1788] Ex. CAT-163 at 121 ("Total Matched Transactions: 14").

[1789] Even these sales occurred for what Dr. Fox-Penner admitted were not comparable durations. Ex. CAT-163 at 87, 113; *see* TransCanada Initial Br. at 48-49.

[1790] Ex. CAT-163 at 110.

[1791] *Id*.

[1792] Tr. 1245:18-1246:4 (Fox-Penner).

discrimination. Specifically, Dr. Fox-Penner compares the daily average price of all transactions based on data submitted in Docket No. PA02-2 with individual hourly sales by TransCanada.[1793] This methodology cannot show undue price discrimination because (1) it compares TransCanada sales to CERS to sales made by parties other than TransCanada and (2) it does not compare similar products. Thus, Dr. Fox-Penner's standard deviation analysis failed to demonstrate that two similarly situated classes of customers were treated differently by TransCanada.

1400. TransCanada also points to a number of inaccuracies and deficiencies in the California Parties' allegations and evidentiary showing regarding this issue. Of particular note is TransCanada's response to the California Parties claim that TransCanada was "able to opportunistically extract discriminatorily high prices from CERS, and did so" because "CERS was often purchasing less than an hour, and sometimes only minutes, before it needed energy to flow."[1794] TransCanada provides compelling evidence that in reality, only one of the sales by TransCanada that the California Parties claimed were unduly discriminatory took place less than hour before delivery (59 minutes, as shown below), and the remainder of the sales all took place between one hour and 23 hours before delivery:

- Power delivered on February 4 at hour ending 15 was sold to CERS on February 3 at 2:26 pm (over 23 hours before delivery for hour ending 15 and more than 9 hours before delivery for the first hour of the transactional block (i.e., hour ending 1) of 24 hours);[1795]

- Power delivered on February 5 at hour ending 1 was sold to CERS on February 4 at 3:01 pm (nearly 9 hours before delivery for hour ending 1, which was the first hour of the transactional block of 7 hours);[1796]

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[1793] *See* Ex. CAT-161 at 74-75.

[1794] California Parties Initial Br. at 42-43.

[1795] Ex. TRC-222 at 66:7-67:3; Ex. TRC-221 at 2, Transaction No. 17 (the date and time of the call when the sale took place is recorded in the WAV File name; "ch012" refers to the channel, "20010203" provides the date (02/03/2001), and "14264524" provides the time the call began to the hundredth of a second (14:26.4524 (i.e., 2:26 p.m.)).

[1796] Ex. TRC-222 at 69:4-70:22; Ex. TRC-221 at 3, Transaction No. 18.

- Power delivered on February 5 at hour ending 23 was sold to CERS on February 5 at 12:26 pm (over 9 hours before delivery for hour ending 23 and more than 2 hours before delivery of the first hour of the transactional block (i.e., hour ending 15) of 10 hours);[1797]

- Power delivered on February 22 at hours ending 1 through 7 was sold to CERS on February 21 at 9:49 pm (between 2 and 8 hours before delivery for the transactional block of 7 hours);[1798]

- Power delivered on February 22 at hour ending 8 was sold to CERS on February 22 at 6:01 am (59 minutes before delivery);[1799]

- Power delivered on February 22 at hour ending 9 was sold to CERS on February 22 at 7:00 am (1 hour before delivery);[1800]

- Power delivered on February 22 at hours ending 10 through 16 was sold to CERS on February 22 at 8:04 am (between 1 and 7 hours before delivery for the transactional block of 7 hours);[1801]

- Power delivered on February 22 at hours ending 17 through 21 was sold to CERS on February 22 at 2:04 pm (between 4 and 8 hours before delivery for the transactional block of 5 hours);[1802]

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[1797] Ex. TRC-222 at 76:4-77:21; Ex. TRC-221 at 3, Transaction No. 21.

[1798] Ex. TRC-222 at 290:14-291:10; Ex. TRC-221 at 9, Transaction No. 83; Ex. TRC-77 at 9:13-14.

[1799] Ex. TRC-222 at 293:4-23; Ex. TRC-221 at 9, Transaction No. 84; Ex. TRC-77 at 10:7-11.

[1800] Ex. TRC-222 at 295, 298-299; Ex. TRC-221 at 9, Transaction No. 85; Ex. TRC-77 at 10:18-19.

[1801] Ex. TRC-222 at 300:19-301:23; Ex. TRC-221 at 9, Transaction No. 86; Ex. TRC-77 at 11:3-4.

[1802] Ex. TRC-222 at 303:6-23; Ex. TRC-221 at 9, Transaction No. 87; Ex. TRC-77 at 11:11-14.

- Power delivered on February 22 at hour ending 22 was sold to CERS on February 22 in a series of three calls, the last of which began at 4:28 pm (CERS actually declined to take the initial call regarding the sale because "it's kind of early for that for us at least")[1803] (over 4 hours before delivery of hour ending 22, which was the first hour of the transactional block of 10 hours);[1804] and

- Power delivered on May 11 at hour ending 16 was sold to CERS on May 11 at 1:00 pm (2 hours before delivery of hour ending 16, which was the first hour of the transactional block of 7 hours).[1805]

1401. Accordingly, TransCanada demonstrated that it made sales to CERS well before the hour of delivery and did not follow "a pattern of waiting to sell energy to CERS until CERS was 'desperate.'"[1806] In fact, it appears that in some instances, CERS refused to buy power from TransCanada because TransCanada called them "too early."[1807]

1402. The California Parties also appear to have mistakenly believed that TransCanada had a "preference for sales in [real-time]."[1808] However, TransCanada has demonstrated that it was constrained in its ability to sell in the day-ahead market because TransCanada did not hold any firm transmission or generation;[1809] therefore, the energy could be cut in Alberta or lack transmission anywhere along the thousands of miles of transmission paths crossing multiple jurisdictions before it reached COB. For that reason, CERS would not have been able to rely on TransCanada's supplies if TransCanada had tried to sell in the day-ahead market. Thus, TransCanada has demonstrated a lawful business justification for this market activity.

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[1803] Ex. TRC-222 at 305:9-10.

[1804] Ex. TRC-222 at 305:5-307:7; Ex. TRC-221 at 10, Transaction No. 88; Ex. TRC-77 at 11:17-21.

[1805] Ex. TRC-222 at 1972:7-26; Ex. TRC-221 at 48, Transaction No. 664.

[1806] This evidence also reflects that the timing of TransCanada's sales to CERS do not demonstrate "bad faith" on TransCanada's part.

[1807] *See, e.g.*, Ex. TRC-222 at 57, 305, 362, 471, 534, 700, 747-48, 774, 781, 1716, 2754, 3005, 3014.

[1808] California Parties Initial Br. at 122.

[1809] Ex. TRC-1 at 116:5-15.

1403. In conclusion, the California Parties failed to demonstrate that TransCanada engaged in unlawful activity that directly affected a particular contract or contracts between TransCanada and CERS.[1810] Thus, the California Parties have not *avoided* the *Mobile-Sierra* presumption that the specific bilateral contracts between CERS and TransCanada are just and reasonable.

### 2. The California Parties Have Demonstrated that Coral Engaged In Unlawful Market Activity

1404. To *avoid* the *Mobile-Sierra* presumption that the specific bilateral contracts the California Parties seek to abrogate as to Coral are just and reasonable under issue 1(A), the California Parties bear the burden of demonstrating that Coral engaged in "unfair dealing at the contract formation stage,"[1811] which "alter[ed] the playing field for contract negotiations,"[1812] and had "a causal connection … [to] the contract rate."[1813] In other words, Coral must have "engaged in unlawful market activity in the spot market and … such unlawful activity directly affected the particular contract or contracts to which [Coral] was a party."[1814] For the reasons discussed below, the California Parties have established a ***prima facie*** case that at least 47 of the subject contracts were tainted by False Export activities and that as many as 119 of the subject contracts may have been tainted by "bad faith." The California Parties have failed to establish that Coral engaged in undue price discrimination or that Coral had or exercised market power during the CERS Period.

#### (a) The California Parties Have Demonstrated that Coral Engaged in False Exports

1405. The California Parties have provided compelling evidence that Coral engaged in False Exports in its sales to CERS.[1815] The California Parties describe a False Export as a

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[1810] Order on Remand at P 21.

[1811] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008).

[1812] *Id*. at 554; Order on Remand at P 20.

[1813] *Morgan Stanley*, 554 U.S. at 555.

[1814] Order on Remand at P 21.

[1815] California Parties Initial Br. at 55-65; *see also* Ex. CAT-041 at 96-98 & Table III-2; Ex. CAT-289 at 130-131.

transaction in which "a supplier purchasing power generated within the ISO would file with the ISO a Day Ahead or Day Of schedule showing a fictitious 'export' of power that was generated within the ISO to a recipient with load (or a 'sink') outside California and then sell the energy to CERS as OOM in Real Time, falsely representing it as coming from outside the ISO."[1816] The California Parties contend that this fiction allowed Coral to divert power generated within the ISO control area away from resources available on a day-ahead basis, thus taking maximum advantage of CERS's weak bargaining position and the conditions that the threat of imminent blackouts posed during real-time.[1817]

1406. The California Parties' assertion that Coral engaged in False Exports is based primarily on Mr. Taylor's testimony and False Export screen. This single-party screen examined whether in any given hour a supplier: (1) submitted a day-ahead or day-of export schedule to the ISO that was not a wheel-through or circulation transaction and (2) made a real-time sale in the same hour to CERS.[1818] The screen excluded exports that wheeled through the ISO system because those exports did not originate within the ISO.[1819] The screen also excluded "inter-zonal" circulation transactions in which there was congestion in the ISO; Mr. Taylor did this in order to address Commission concerns that certain matched day-ahead/day-of exports and real-time imports in different zones might have assisted the ISO in addressing congestion and thus should not be considered False Exports.[1820]

1407. On rebuttal, Mr. Taylor adjusted his analysis based on additional data and in response to points that certain witnesses had raised. These adjustments reduced the volume of False Export transactions, but did not alter his conclusion that Coral engaged in False Exports.[1821] The amounts and delivery hours in which Mr. Taylor found False Exports are identified in Exhibit CAT-408.[1822] Mr. Taylor concluded that Coral falsely exported 2,798 MWh, across 139 individual hours, of energy sold to CERS in

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[1816] Ex. CAT-041 at 88.

[1817] *Id.* at 87-88.

[1818] *Id.* at 93.

[1819] *Id.* at 94.

[1820] *Id.* at 95.

[1821] Ex. CAT-289 at 130-31 & Table V-2.

[1822] *See id.* at 151; Ex. CAT-408 (*Mobile-Sierra* Database – Coral).

real-time.[1823] Mr. Taylor's screen also "linked his False Exports to each hour and sales contract in which the California Parties assert that Coral extracted premiums above the *Power Markets Week* prices for the corresponding hour."[1824]

1408. False Export transactions consisted of at least two instances of deceptive conduct: first, a false indication to the ISO that energy generated in California was being exported outside of the ISO and second, a false indication to CERS that the energy that it was purchasing in real-time came from the Pacific Northwest.[1825]

1409. False Exports are inconsistent with the operation of efficient, competitive markets,[1826] violate the ISO Tariff's MMIP,[1827] and violate the ISO Tariff provisions dealing with operating requirements and with scheduling and bidding.[1828] Scheduling Coordinators had to file with the ISO a schedule reflecting exports;[1829] implicit in this obligation was the requirement that such schedules would not be intentionally inaccurate or misleading; thus, purposefully inaccurate schedules violate the tariff's scheduling requirements.[1830] Moreover, because the sales to CERS in these False Export transactions were based upon deceptive representations that the energy was sourced from the Pacific Northwest, they also violate Coral's obligations under its market-based rate

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[1823] Ex. CAT-289 at 131; Ex. CAT-408 (Mr. Taylor's *Mobile-Sierra* database for Coral showing when each of those hours was delivered, the prices that CERS paid, and the premium that Coral extracted); California Parties Initial Br. at B-9.

[1824] Ex. CAT-408.

[1825] Ex. CAT-041 at 87-88.

[1826] *See Am. Elec. Power Serv. Corp.*, 103 FERC ¶ 61,345, at P 25 (2003). The MMIP was one of several protocols incorporated into the ISO and PX Tariffs. It contained gaming and anomalous market behavior provisions describing behavior inconsistent with the operation of efficient, competitive markets. Ex. CAT-041 at 92.

[1827] *See* Ex. CAT-147 at 152-70 (ISO Tariff, MMIP).

[1828] Although the sales to CERS were conducted under the WSPP Agreement, the export transactions were either conducted pursuant to the CAISO tariff or scheduled for export through the CAISO.

[1829] Ex. CAT-147 at 22-23 (ISO Tariff §§ 2.2.11.1-.2); Ex. CAT-041 at 93.

[1830] Ex. CAT-041 at 93.

tariff.[1831] In the Commission's Gaming Order, the Commission noted that "companies failing to adhere to proper standards are subject to immediate revocation of their market-based rate authority" and that "implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation."[1832] As previously stated, False Export transactions involve both a deception and misrepresentation on the part of the seller regarding the source of energy being sold.

1410. Coral contends that it sold to CERS only in back-to-back, or B2B, transactions, not through a portfolio of purchased power, and that this fact causes *all* of the California Parties' Issue 1(A) allegations to fail.[1833] Coral supports this contention primarily through Mr. Tranen, the first President and CEO of the ISO, who sponsored Exhibit SNA-14, which details each of Coral's 1,703 B2B transactions with CERS. For each sequentially numbered and paired transaction, Exhibit SNA-14 shows a Coral sale to CERS and a corresponding purchase by Coral from a counterparty in the Pacific Northwest of the *identical* volume, during the *identical* day and hour of the sale to CERS. Exhibit SNA-14 also contains contemporaneously created deal numbers that sequentially identify contracts between Coral and CERS, on one hand, and Coral and its B2B supplier, on the other hand. Coral points out that the California Parties stipulated to the accuracy of the 1,703 Coral sales to CERS.[1834] Further, Coral asserts that Dr. Fox-Penner and Mr. Taylor affirmed that each of these 1,703 stipulated sales to CERS is perfectly matched to a purchase by Coral and agreed to the accuracy of the SNA-14 transaction data showing B2B sales.[1835]

1411. However, the California Parties have demonstrated that Mr. Tranen's analysis cannot be relied upon to establish the true sources of the energy that Coral sold to CERS. Instead, Coral's alleged B2B transactions were shown to have actually involved upstream transactions in which Coral sold power out of California to a third party and then bought

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[1831] *Enron Power Mktg., Inc.*, 103 FERC ¶ 61,343, at P 52 (2003) (Gaming Order) (Ex. CAT-540); Ex. CAT-041 at 93.

[1832] *Enron Power Mktg., Inc.*, 103 FERC ¶ 61,343, at P 52 (2003).

[1833] Coral Reply Br. at 6.

[1834] Ex. SNA-CAT-1. The California Parties identified minor discrepancies in the volume, price, or location of only seven sales.

[1835] Coral Reply Br. at 6-7 (citing Tr. 2560:17-20 (Taylor)).

it back at COB.[1836] Coral emails cited in Mr. Taylor's Direct Testimony[1837] demonstrated these coordinated transactions, as did numerous trader recordings and Coral transaction data that those recordings illuminated.[1838]

1412. Mr. Tranen's B2B analysis simply reflects the last stage of a strategy on Coral's part to take energy out of California, often from Glendale, move it north, sleeve it through a Pacific Northwest entity for a fee, and sell it back to CERS, misrepresented as coming from the Pacific Northwest.[1839] Mr. Tranen admitted that multi-party transactions of the sort discussed above could constitute False Exports.[1840] He also admitted that in all but 19 of the 1,703 transactions that he examined in his original analysis of Coral's sales to CERS (Exhibit SNA-14), he did not investigate whether the sales originated as sales from Coral.[1841]

1413. Although Trial Staff and Coral point to flaws in the robustness of Mr. Taylor's evidence of False Export,[1842] the California Parties did provide sufficient evidence to establish a *prima facie* case against Coral. Thus, the California Parties successfully shifted the burden of production to Coral with respect to these limited number of transactions.[1843] As discussed above, Mr. Taylor's hearing testimony demonstrated Mr. Tranen's B2B analysis is insufficient to meet Coral's burden of production in this regard. Specifically, Mr. Tranen failed to demonstrate that each transaction was in fact back-to-back. Mr. Tranen conducted an additional analysis following Mr. Taylor's

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[1836] *See* Ex. CAT-041 at 80.

[1837] *Id.* at 80; Ex. CAT-104.

[1838] Tr. 2969:20-2970:5 (Taylor) (summarizing evidence that refutes Coral's claim that B2B transactions constitute a legitimate business reason for its behavior); California Parties Initial Br. at 63-65.

[1839] Tr. 2993:10-21 (Taylor).

[1840] *See* Tr. 3955:24-3956:14 (Tranen).

[1841] Tr. 3957:6-20 (Tranen).

[1842] Trial Staff Initial Br. at 37-46; Coral Initial Br. at 50-59.

[1843] *See Nantahala Power & Light Co.*, 19 FERC ¶ 61,152, at 61,276 (citations omitted), *reh'g denied*, 20 FERC ¶ 61,430 (1982), *aff'd sub nom*., *Nantahala Power & Light Co. v. FERC*, 727 F.2d 1342 (4th Cir. 1984).

hearing testimony, but that analysis was not introduced into the record,[1844] and thus, Mr. Tranen's statements regarding this analysis are not supported. Coral's lack of rebuttal evidence is in stark contrast to the evidence submitted by TransCanada. As noted above, TransCanada submitted the trader tapes for *all* its transactions with CERS, which provided a complete picture of TransCanada's dealings with CERS over the course of the CERS Period. Conversely, Coral provided only on a limited number of trader tapes that viewed Coral in its most favorable light and failed to adequately address issues raised by the California Parties regarding the subject transactions.

1414. The California Parties have successfully established a ***prima facie*** case that certain transactions were tainted by False Export. Coral's insufficient production in response precluded the undersigned from analyzing the transactions with the level of granularity necessary to support a contract specific inquiry. As a result, there remain significant questions of fact and law with respect to these transactions that must be resolved in Phase II of this proceeding. In Phase II, Coral may demonstrate that the contracts were not in fact False Exports and/or that the rates charged to CERS with respect to these contracts were nonetheless just and reasonable based on Coral's actual costs and market conditions.

#### (b) The California Parties Have Demonstrated that Coral Engaged in Fraud, Duress, or Bad Faith

1415. The California Parties acknowledge that they have not distinguished between the three practices of fraud, duress or bad faith.[1845] The California Parties explain that they have shown their aggregated claims of fraud, duress, and bad faith using the same evidence[1846] because "each Respondent … collected a price that was far above the (already distorted) prevailing market price ….**"**[1847]

1416. According to the California Parties:

> [t]he essence of the California Parties' "duress, fraud, or bad faith" claim is that each Respondent exploited CERS by charging a price far above the

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[1844] Tr. 3974:25-3975:1, 3992:6-11 (Tranen).

[1845] California Parties Initial Br. at 23.

[1846] *Id.* (stating that their witness Taylor did not distinguish between the three practices and that "there was no reason to do so").

[1847] *Id.*

> competitive market levels and well above the prices that Respondents charged other buyers, because Respondents knew that CERS, which was required to obtain the energy critical to reliable ISO operation, lacked reasonable alternatives.[1848]

1417. The principle evidence provided by the California Parties in support of these claims is Mr. Taylor's *Power Markets Week* plus $75 per MWh test,[1849] a generic "benchmark" screen that does not take into account actual contract negotiations which may have occurred between the parties regarding specific contracts in any way. For the reasons discussed more fully *supra* in the Section of this Initial Decision pertaining to TransCanada, such a generic benchmark, standing alone, does not establish evidence of duress, fraud, or bad faith in the formation of the contract.

1418. However, unlike with TransCanada, the California Parties have provided compelling evidence demonstrating that during the December 25, 2000 through June 20, 2001 period, with respect to the wholesale bilateral Pacific Northwest spot market energy contracts at issue in this case, Coral engaged in unlawful market activity without a legitimate business reason at the contract formation stage that directly affected the particular contracts to which Coral was a party; i.e. False Exports. For the reasons discussed below, this same evidence supports a finding that the subject contracts were tainted by "bad faith" negotiations on the part of Coral at the contract formation stage.

1419. Respondents' sales to CERS were made under the WSPP Agreement which requires construction under Utah law.[1850] Further, the Commission applies the governing state contract law in deciding whether there was duress, fraud, or bad faith in the formation of a contract.[1851] Under Utah law "[t]o find that a party acted in 'bad faith,' the trial court must find that *one or more* of the following factors existed: (i) [t]he party lacked an honest belief in the propriety of the activities in question; (ii) the party intended to take unconscionable advantage of others; *or* (iii) the party intended to or acted with the knowledge that the activities in question would hinder, delay, or defraud others."[1852] The

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[1848] *Id.* at 21.

[1849] *Id.* at 29, 41-42.

[1850] Ex. CAT-012 at 16; Ex. CAT-124 at 48.

[1851] *Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 115 FERC ¶ 61,375, at P 70 (2006) (Commission found contract voidable on basis of fraud in the inducement).

[1852] *See Valcarce v. Fitzgerald*, 961 P.2d 305, 316 (Utah 1998) (citing *Cady v. Johnson*, 671 P.2d 149, 151 (Utah 1983)).

California Parties have provided compelling evidence that Coral was, in a concerted and deceptive manner, exporting power at NOB so that it could have that power turned around and resold to CERS as sourced from the Pacific Northwest.[1853] As previously explained, these transactions consisted of at least two instances of deceptive conduct: first, a false indication to the ISO that energy generated in California was being exported outside of the ISO and second, a false indication to CERS that the energy that it was purchasing in real-time came from the Pacific Northwest.[1854] These deceptive trade practices clearly demonstrate that Coral engaged in contract negotiations with CERS in "bad faith" as that term is defined under Utah state law.

1420. Further, the record reflects that Coral's deceptive trade practices associated with these transactions may have contributed to or exacerbated the situation the California Parties often found themselves in of either suffering the significant direct and indirect costs and disruptions associated with a blackout or paying the high rates necessary to purchase energy on the spot markets during the relevant time period. Blackouts, a phenomenon that even Respondents' own expert, Mr. Tranen, readily conceded had to be avoided at all costs,[1855] occurred as late as May 7 and 8, 2001, towards the end of the CERS Period.[1856] In fact, virtually all of the Stage 3 Emergencies that the ISO called occurred during the CERS Period.[1857] Sellers were aware that CERS had to buy large amounts of energy in real-time to avoid blackouts – in trader parlance, that CERS was "short."[1858] Moreover, and perhaps more importantly, Coral was aware that CERS was in a vulnerable position and ready to pay high prices if necessary to avoid blackouts.[1859]

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[1853] Tr. 3973:6-13 (Tranen).

[1854] Ex. CAT-041 at 87-88.

[1855] Tr. 3980:8-23 (Tranen).

[1856] Ex. CAT-041 at 30 n.49.

[1857] *See* Ex. CAT-134 (ISO Alert, Warning, and Emergency Record); Ex. CAT-041 at 30 n.49; Ex. CAT-289 at 110 n.223.

[1858] *See, e.g.*, Ex. CAT-012 at 3:18-4:20 (discussing blackouts and the California Governor's proclamation of a state of emergency); Ex. CAT-022 at 7:7-8 (stating that the Governor's proclamation was "front page news"). *See also* Ex. CAT-022 at 7:14-20.

[1859] *See, e.g.*, Ex. CAT-713 at 7:24-8:4 (January 18, 2001 Coral trader tape in which Coral supervisor congratulated traders on extraordinary profits from a trade in California and admitted she had no ethical problem causing rolling blackouts);

(continued…)

While Mr. Taylor's *Power Markets Week* plus $75/MWh test,[1860] standing alone, does not establish evidence of duress, fraud, or bad faith in the formation of the contracts; it does provide corroborating evidence that Coral's deceptive trade practices directly affected the subject contracts.

1421. In this regard, Mr. Taylor also provided compelling testimony that Coral's B2B transactions were purposely deceptive with regard to purchase costs to conceal upstream profits. As Mr. Taylor explained in his pre-filed testimony, and reiterated at hearing, there were numerous instances in which Coral's alleged B2Bs with CERS were actually the end of a daisy chain of transactions that Coral initiated with a low-cost purchase, hiding significant profits not captured through a simple comparison between the screen price and the alleged B2B purchase price.[1861]

1422. Thus, the California Parties have successfully established a ***prima facie*** case that certain transactions were tainted by "bad faith." As discussed above, Coral's insufficient production in response precluded the undersigned from analyzing the transactions with the level of granularity necessary to support a contract specific inquiry. As a result, there remain significant questions of fact and law with respect to these transactions that must be resolved in Phase II of this proceeding. In Phase II, Coral may demonstrate that the contracts were not in fact conducted in "bad faith" and/or that the rates charged to CERS with respect to these contracts were nonetheless just and reasonable based on Coral's actual costs and market conditions.

#### (c) The California Parties Failed to Establish that Coral Engaged in Undue Price Discrimination During the CERS Period

1423. The California Parties assert that Coral "unduly discriminated against CERS during the CERS Period" by charging "CERS more than they were charging similarly-situated customers for the very same product in the very same markets …."[1862]

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Tr. 4056:3-5 (Bowman). *See also* Ex. CAT-104 (emails between Coral traders discussing Coral's ability to exploit CERS's concern regarding blackouts to extract large margins); Ex. CAT-360 (on May 8, 2001, an ISO blackout day, Coral arranged with Avista to purchase 25 megawatt-hours for $450 and offered it to CERS for $550; when CERS declined, Coral advised Avista that it would not be making the purchase for resale).

[1860] California Parties Initial Br. at 29, 41-42.

[1861] Tr. 2969:11-2995:16 (Taylor); Ex. CAT-668 through CAT-675.

[1862] California Parties Initial Br. at 42.

The California Parties bear the burden of substantiating their allegation of undue discrimination[1863] by showing that "(1) two classes of customers are treated differently; and (2) that the two classes of customers are similarly situated."[1864] In addition, the Commission has "long recognized" that rate differentials may be justified by cost or other factual differences between customers.[1865] Complainants must address "the threshold issue of whether the rate disparity is nonetheless justified. … [R]ate differences are not, in and of themselves, evidence of undue discrimination."[1866]

1424. The threshold challenge that the California Parties face with an "undue discrimination" theory of unlawful activity is the fact that the evidence of record when considered as a whole strongly supports a finding that CERS was "uniquely situated" as compared to other buyers in the Pacific Northwest market during the relevant time period in a number of material ways including the fact that CERS was required to obtain the energy critical to reliable ISO operation, credit risk issues, and the sheer volume of its energy purchases. In fact, Dr. Fox-Penner admitted that "CERS was a uniquely situated entity in the whole WECC."[1867]

1425. Nevertheless, the California Parties assert that "[u]ndue price discrimination was possible during [the CERS Period] because a limited set of sellers knew that CERS had to buy large amounts of energy in Real Time – in trader parlance, CERS was 'short.'"[1868] Trial Staff correctly points out that there is no citation to the record for this rather surprising statement and, given the rolling blackouts, political uproar, and media coverage surrounding the energy crisis, to assert that such knowledge was only available to a limited number of sellers is simply not credible.[1869] The idea that only a limited set

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[1863] *See Transwestern Pipeline Co.*, 36 FERC ¶ 61,175, at 61,433 (1986).

[1864] *Energy Transfer Partners, L.P.*, 120 FERC ¶ 61,086, at P 169 (2007).

[1865] *Village of Belmont v. Wisc. Power & Light Co.*, 84 FERC ¶ 61,056, at 61,255 (1998) (citations omitted); *see Cities of Newark, New Castle & Seaford v. FERC*, 763 F.2d 533, 546 (3d Cir. 1985).

[1866] *Village of Belmont*, 84 FERC at 61,255 (citations omitted).

[1867] Trial Staff Reply Br. at 17-20. *See also* Tr. 1245:18-1246:4 (Fox-Penner).

[1868] California Parties Initial Br. at 42.

[1869] *See, e.g.*, Ex. CAT-012 at 3:18-4:20 (discussing blackouts and the California Governor's proclamation of a state of emergency); Ex. CAT-022 at 7:7-8 (stating that the Governor's proclamation was "front page news").

of sellers knew that CERS was "short" is also directly contrary to the testimony of California Parties witness Lee, who testified that "[s]ellers knew from the start that CERS was a buyer and that it fell to CERS to go out to try to meet the extremely high demand by purchasing bilaterally" and "of course [this] was obvious to any individual seller."[1870] Moreover, such a claim ignores many other significant factors adversely impacting CERS's buying options other than "undue discrimination" by sellers, including a widespread perception that CERS was highly risky and directives from the CAISO to purchase only at COB.[1871]

1426. Further, as discussed in both Trial Staff's Initial and Reply Briefs, Dr. Fox-Penner's attempt to match CERS transactions with non-CERS transactions does not make the necessary showing that similarly situated customers were treated differently because Dr. Fox-Penner failed to control for critical factors such as the time the agreement between the counterparties was reached and the duration of the transaction.[1872] Moreover, the econometric tests in Dr. Fox-Penner's rebuttal testimony suffers from the same flaws as his matching methodology in that it also fails to properly control for the duration of transactions, the timing of agreements, or credit risk.[1873] Finally, Trial Staff correctly points out that Dr. Fox-Penner's use of long-run and short-run marginal costs as evidence that prices were economically inefficient was discredited by Dr. Savitski, Professor Hogan, and Mr. Cavicchi.[1874]

1427. For the foregoing reasons, the California Parties have failed to establish that Coral engaged in undue price discrimination during the CERS Period.

#### (d) The California Parties Failed to Establish that Coral Exercised Market Power During the CERS Period

1428. The California Parties allege that the "Respondents" exercised market power during the CERS Period or took advantage of market power circumstances that existed by

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[1870] Ex. CAT-022 at 7:14-20.

[1871] California Parties Initial Br. at 24-26.

[1872] Trial Staff Initial Br. at 28-29; Trial Staff Reply Br. at 17-20.

[1873] Trial Staff Initial Br. at 30 (citing Tr. 1275:6-1276:24 (Fox-Penner)); Trial Staff Reply Br. at 17-20.

[1874] Trial Staff Initial Br. at 33-37; Ex. S-13 at 21:12-20, 24:20-22; Ex. PNR-1 at 14:21-15:18; Ex. TAE-8 at 36:15-37:15.

engaging in price discrimination.[1875] The California Parties assert that its witness, Dr. Reynolds, demonstrated, through a variety of econometric and statistical tests (referred to as the "CERS Regressions" and the "TransAlta Regressions"), that market power existed and that larger sellers in general, and TransAlta in particular, exercised market power and charged higher prices to CERS.[1876] In particular as to Coral, the California Parties assert that Dr. Reynolds concluded that Coral's high prices were the result of the exercise of market power.[1877] Dr. Reynolds disputed Coral's contention that peak and off-peak differences explained his results by performing statistical tests, controlling for peak and off-peak differences; and that this additional analysis confirmed that Coral realized higher prices for larger quantities sold.[1878]

1429. First, the California Parties have failed to provide seller specific evidence that Coral had or exercised market power, relying instead on regression analyses that included market participants who never were or who are no longer parties to this proceeding. Further, Dr. Reynolds used a market power test that was not adopted by the Commission during the CERS Period and cannot be applied to Coral retroactively. Trial Staff's Initial Brief explains how the Commission was applying what has been referred to as the "hub-and-spoke" test during the relevant period and that the Commission has long used a twenty percent generation market share as an indicator of potential generation market power.[1879] Moreover, in its order affirming the Initial Decision in the *Lockyer* proceeding, the Commission affirmed its rejection of the California Parties' argument that the twenty percent hub-and-spoke analysis is an inappropriate market power screen for the Commission to use in that proceeding.[1880] The Commission reiterated that it "is required to use the standards for assessing market power of market-based rate sellers …

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[1875] California Parties Initial Br. at 72.

[1876] Ex. CAT-264 at 6-20; Ex. CAT-266; Ex. CAT-631 at 5-25, 33-42.

[1877] Ex. CAT-631 at 35-36.

[1878] *See* California Parties Initial Br. at B-10. *See also* Ex. CAT-264 at 4-8; Ex. CAT-631 at 5, 34-36.

[1879] Trial Staff Initial Br. at 49; Trial Staff Reply Br. at 32-34. *See California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 122 FERC ¶ 61,260, at P35 n.70 (2008).

[1880] *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, Opinion No. 512, 135 FERC ¶ 61,113 (2011).

in effect at the time the transaction took place."[1881] The Commission explained that "doing otherwise would 'violate the requirement that all jurisdictional sellers be on notice as to what test will be applied to them' and would constitute the 'retroactive establishment of agency rules and tests.'"[1882] As Trial Staff correctly points out, the same rationale is applicable to this proceeding.

1430. Because it is undisputed that the hub-and-spoke analysis was the standard for assessing market power of market-based rate sellers during the CERS Period, and it is undisputed that Dr. Reynolds declined to provide an analysis of market power as to Coral using that market power screen, the California Parties have failed to establish that Coral had or exercised market power during the CERS Period.

## VII. The California Parties Issue 1(B) Claims

1431. Issue 1(B) addresses claims that an individual seller engaged in unlawful market activity, without a legitimate business reason, that directly affected the particular contract or contracts to which that seller was a party such that the presumption of just and reasonable rates applicable to bilateral contracts under the *Mobile-Sierra* standard would not apply. The California Parties have asserted Issue 1(B) claims against Shell Energy North America (US), L.P., d/b/a Coral Power, L.L.C. (Shell Energy or Coral) and TransCanada Energy Ltd. (TransCanada). The California Parties' claims concern transactions entered into by CERS between January 17, 2001 and June 20, 2001 (CERS Period). Initial briefs were filed by the parties on December 16, 2013,[1883] and reply briefs were filed on January 28, 2014.[1884]

### A. Summary of the Position of the Parties

#### 1. The California Parties Initial Brief

1432. The California Parties argue that the Western Energy Crisis inflicted real harm on California's consumers, businesses, and government services. The California Parties

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[1881] *Id.* P 39.

[1882] *Id.* (quoting *California ex rel. Lockyer v. British Columbia Power Exch. Corp.*, 125 FERC ¶ 61,016, at P 30 (2008)).

[1883] The California Parties filed errata to their initial brief and the California Respondents filed errata to their reply brief.

[1884] In their post-hearing briefs, Respondents provide substantially similar arguments on numerous issues. Those arguments are not repeated in each summary.

note that Commissioner Florio testified that the crisis was "unprecedented" and the "burden [on the IOUs' customers] was enormous."[1885] The California Parties assert that Commissioner Florio also provided examples of the harm caused by the crisis, such as consumers being forced to choose between buying food or medicine and paying their electric bill and businesses cutting hours, laying off workers, and adding surcharges to their prices to cover the cost of electricity.[1886]

### (a) The *Mobile-Sierra* Standard

1433. The California Parties contend that if the *Mobile-Sierra* presumption bars relief for the sales at issue here, it is almost impossible to imagine how it could ever be avoided or overcome. The California Parties note that the Commission's primary responsibility is to protect consumers,[1887] and the *Mobile-Sierra* Doctrine must be interpreted in way that empowers the Commission to provide relief for the consumers and businesses harmed by the worst electricity crisis in American history.

1434. Next, the California Parties assert that *Mobile-Sierra* and *Morgan Stanley* make clear that the Commission may always modify contracts that harm the public interest. The California Parties state that in *Mobile*, the Court was careful to explain that its holding that gas companies may not "unilaterally" change their contracts "in no way impairs the regulatory powers of the Commission, for the contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest."[1888] In *Sierra*, the Court re-emphasized the Commission's ability to revise contract rates that affect the public interest.[1889]

1435. The California Parties also aver that in *Morgan Stanley*, the Court held that the presumption that contract rates are just and reasonable may be "overcome" if the

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[1885] Ex. CAT-001 at 4, 19.

[1886] *See id*. at 11-12.

[1887] *See, e.g.*, *Atl. Ref. Co. v. Pub. Serv. Comm'n of N. Y.*, 360 U.S. 378, 388 (1959); *accord NAACP v. FPC*, 520 F.2d 432, 438 (D.C. Cir. 1975).

[1888] *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956).

[1889] *See FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956).

Commission "concludes that the contract seriously harms the public interest."[1890] The Court further explained that in cases involving challenges to excessive rates, the issue is whether "any customer" of the wholesale purchaser would be burdened by the rates, and "circumstances exogenous to contract negotiations, including natural disasters and market manipulation by entities not parties to the challenged contract" are relevant to "whether the contracts impose an 'excessive burden' on consumers."[1891] The California Parties contend that the Commission's failure to consider such circumstances was the "precise" reason the Court gave for remanding the case to the Commission.[1892]

1436. The California Parties further assert that court and Commission precedent support modifying the contracts at issue under the public interest standard. For example, in *Mississippi Industries v. FERC*, the D.C. Circuit upheld the Commission's authority to modify an agreement, stating that the Commission "may always reform a contract found to be 'unlawful' or 'contrary to the public interest.'" [1893]

1437. Additionally, in *Northeast Utilities Service Co. v. FERC*, the First Circuit upheld the Commission's application of the public interest standard to modify a wholesale power contract.[1894] The court explained that "the most attractive case for affording additional protection [under the public interest standard], despite the presence of a contract, is where the protection is intended to safeguard the interests of third parties."[1895] The court stated that all that was necessary was that the Commission had given "thoughtful consideration to the public interest" when it modified the contract.[1896] Similarly, in *Texaco Inc. v.*

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[1890] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[1891] *Id*. at 548-49 & n.4 (internal quotation omitted).

[1892] *Id*.

[1893] *Miss. Indus. v. FERC*, 808 F.2d 1525, 1553, *different holding vacated in part on other grounds per curiam*, 822 F.2d 1104 (D.C. Cir. 1987).

[1894] *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686, 687 (1st Cir. 1995).

[1895] *Id*. at 691 (brackets in original) (internal quotations and citations omitted). *See also Ari. Corp. Comm'n v. FERC*, 397 F.3d 952, 952-54 (D.C. Cir. 2005) (upholding the Commission's authority to prevent "the imposition of an excessive burden" on third parties).

[1896] *Ne. Utils. Serv. Co.*, 55 F.3d at 693.

*FERC*, the D.C. Circuit upheld the Commission's modification of gas transportation contracts under the public interest standard because the Commission had determined that, absent contract modification, the public interest would be harmed.[1897]

1438. Next, the California Parties discuss the D.C. Circuits' opinion in *Transmission Access Policy Study Group v. FERC*, which upheld the Commission's determination that "it would be against the public interest to permit a *Mobile-Sierra* clause in an existing wholesale requirements contract to preclude the parties to such a contract from the opportunity to realize the benefits of the competitive wholesale power markets."[1898] The court noted that the Commission believed that "the unprecedented competitive changes that have occurred (and are continuing to occur) in the industry may render [customers'] contracts to be no longer in the public interest."[1899] The court also upheld the Commission's determination that refusing to allow contract modification could harm third parties and thereby harm the public interest.[1900]

1439. The *TAPS* court rejected the argument that the Commission had made generic, rather than particularized, case-by-case, public interest findings, holding that "when intervening circumstances," such as Commission-mandated open transmission access, "affect an entire class of contracts in an identical manner, we find nothing in the *Mobile-Sierra* doctrine to prohibit FERC from responding with a public interest finding applicable to all contracts of that class."[1901] The court also rejected challenges to the Commission's determination that the public interest required it to allow customers to modify their supply contracts, noting that the Commission had found instances of undue discrimination and had relied upon the "harm to third parties (i.e., customers of the wholesale requirements customers) that may result from adherence to uneconomical contracts."[1902]

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[1897] *See Texaco Inc. v. FERC*, 148 F.3d 1091, 1093 (D.C. Cir. 1998).

[1898] *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 710-11 (D.C. Cir. 2000) (*TAPS*), *aff'd*, *New York v. FERC*, 535 U.S. 1 (2002).

[1899] *Id.* at 709-10 (internal quotations and citation omitted).

[1900] *Id.* at 709-11.

[1901] *Id*. at 710-11. *See also Ari. Corp. Comm'n v. FERC*, 397 F.3d 952, 955-56 (D.C. Cir. 2005) (the "*Mobile-Sierra* doctrine permits generalized findings of public interest when intervening circumstances affect a class of contracts in the same manner)

[1902] *TAPS*, 225 F.3d at 712.

1440. Moreover, in *ISO New England Inc.*, the Commission modified a contract under the public interest standard relying on the reasons it gave in Order No. 1000 for eliminating federal rights of first refusal.[1903] The Commission noted that the court had previously upheld the Commission's public interest determination in Order No. 888 based upon the Commission's predictions and estimates.[1904] The Commission also discussed the court's affirmance of contract modification based upon the Commission's generic finding that utilities had engaged in undue discrimination "by denying competitors access to their transmission lines."[1905] Finally, the Commission relied on the Supreme Court's statement that "the *Mobile-Sierra* doctrine does not overlook third-party interests; it is framed with a view to their protection,"[1906] and on the First Circuit's finding that "the 'most attractive case' for contract reformation pursuant to the *Mobile- Sierra* doctrine 'is where the protection is intended to safeguard the interests of third parties.'"[1907]

1441. The California Parties argue that these cases demonstrate that the Commission has ample authority to modify Respondents' contract prices because of the harm that they caused to the public interest.[1908] The California Parties note that the Commission and courts have never hesitated to modify contracts in order to "safeguard the interests of third parties."[1909] The California Parties assert that there is specific evidence documenting actual historic and ongoing harm to consumers and businesses.

1442. Furthermore, the California Parties note that the Commission has modified contracts in order to remedy undue discrimination and courts have approved those

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[1903] *ISO New England Inc.*, 143 FERC ¶ 61,150, at PP 160-98 (2013).

[1904] *See id*. PP 176-180.

[1905] *Id*. P 181 (quoting *TAPS*, 225 F.3d at 712.)

[1906] *Id*. P 194 (quoting *NRG Power Mktg., LLC v. Me. Pub. Serv. Comm'n*, 558 U.S. 165, 175 (2010)).

[1907] *Id*. P 194 (quoting and citing *Ne. Utils. Serv. Co v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993)).

[1908] *See generally, e.g.*, Ex. CAT-001; Ex. CAT-267.

[1909] *See, e.g.*, *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686, 691 (1st Cir. 1995).

modifications.[1910] The California Parties contend that Respondents charged CERS prices significantly above what they charged similarly-situated purchasers, and that there was no legitimate business reason for the difference in prices. Thus, the California Parties conclude that the Respondents' discrimination violated FPA section 205 and meets the *Mobile-Sierra* standard for public interest modification.[1911]

1443. The California Parties also assert that the Commission may apply public interest modifications to an entire class of contracts in cases where intervening circumstances impact all of the contracts.[1912] The California Parties state that all of the relevant contracts were negotiated in emergency conditions of chaos, blackouts, and time pressure during a period when market manipulation was prevalent.[1913] Thus, even the few contracts as to which the California Parties did not allege and prove specific contract formation deficiencies under Issue 1(A) should be modified under Issue 1(B) because they also harmed the public interest and created an excessive burden.

1444. Next, the California Parties contend that unlike the contracts at issue in *Morgan Stanley*, these contracts do not benefit the public interest. The California Parties note that in *Morgan Stanley*, the Court emphasized that the long-term contracts at issue conferred economic benefits, including protection against price volatility and support for capital investment.[1914] The California Parties aver that the spot market contracts do not convey such benefits because they did not yield a secure revenue stream to support capital

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[1910] *See, e.g.*, *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 712 (D.C. Cir. 2000), *aff'd*, *New York v. FERC*, 535 U.S. 1 (2002); *Miss. Indus. v. FERC*, 808 F.2d 1525, 1553, *different holding vacated in part on other grounds per curiam*, 822 F.2d 1104 (D.C. Cir. 1987) (Commission adopted ALJ's finding of profound discrimination).

[1911] *See, e.g.*, *PacifiCorp v. Reliant Energy Servs. Inc.*, 103 FERC ¶ 61,355, at P 66 (2003), *order on reh'g*, 105 FERC ¶ 61,184 (2003).

[1912] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 549 n.4 (2008) (Commission may revise rates when "circumstances exogenous to contract negotiations" result in contracts that "impose an 'excessive burden' on consumers") (internal quotation omitted). *See also TAPS*, 225 F.2d at 709-10.

[1913] *See, e.g.*, *California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1014-15 (9th Cir. 2004) ("the California energy market was subjected to artificial manipulation on a massive scale").

[1914] *Morgan Stanley*, 554 U.S. at 547, 551.

investment and are precisely the volatile prices from which long-term agreements are supposed to offer relief.[1915]

**(b) Evidence of Excessive Burden on Consumers and Harm to the Public Interest**

1445. The California Parties state that Commissioner Florio provided unrefuted evidence of the burden that excessive rates imposed on third parties. The California Parties state that in San Diego, where retail rates were not capped, customers' "monthly energy bills had doubled, tripled or risen even higher, seemingly overnight."[1916] Moreover, the California Parties assert that customers could not protect themselves because they "could not modify their usage quickly enough or dramatically enough to keep their bills under control."[1917] The California Parties state that Commission Florio provide numerous specific examples of the excessive burden placed upon the government, consumers, and businesses.[1918] Commissioner Florio concluded that the increased prices were producing "tragic results" and it was not "realistic – or, frankly, humane – to force customers to bear the full impact of extreme market prices."[1919]

1446. The California Parties assert that no Respondent witness even attempted to rebut Commissioner Florio's testimony.[1920] The California Parties contend that Ms. Radel's criticism that Commissioner Florio's testimony did not link Respondents' contracts to the burden ignores the purpose of Commissioner Florio's testimony. The California Parties state that other witnesses specifically detailed the relationship between Respondents' contracts and harm to the public interest.

1447. The California Parties also state that Mr. Pacheco demonstrated that the contract rates not only burdened the public at the time, but will continue to burden California

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[1915] Ex. CAT-041 at 131-132.

[1916] Ex. CAT-001 at 5.

[1917] *Id*. at 6.

[1918] *Id*. at 8-14.

[1919] *Id*. at 17.

[1920] *See* Tr. 542:13-17 (California Parties Counsel stating that Respondents and Staff have waived cross-examination of Commissioner Florio). *See also* Ex. S-15 at 21 (Ms. Radel stating that she had no basis to disagree with Commission Florio).

consumers into the future. The California Parties assert that CDWR issued bonds to finance CERS's purchases because immediate pass-through of costs would have placed too high of a burden on consumers.[1921] The California Parties state that for twenty years, a Bond Charge is imposed on every customer of the IOUs.[1922] The California Parties note that any refunds ordered in this proceeding will benefit California consumers because the refunds will reduce the bond charges.

1448. Next, the California Parties aver that Professor Berck demonstrated the excessive harm to the public interest that would have been caused had California not financed the costs.[1923] The California Parties state that if California had immediately passed through $4.97 billion to California ratepayers, the total overcharge alleged from all sellers, personal income would have been reduced by $15.19 billion, representing a loss of approximately 105,000 jobs.[1924] Similarly, had California passed through $2.11 billion, the amount of overcharges associated with CERS's total purchases in the Pacific Northwest, personal income would have been reduced by $6.31 billion, representing a loss of approximately 44,300 jobs.[1925] The California Parties note that Professor Berck concluded that these losses "would impose extraordinary burdens on [California] consumers."[1926] For example, Professor Berck explained that a "$4.97 billion overcharge is enough to reduce the competitiveness of California industry."[1927] Professor Berck further testified that "[t]here is an excellent chance that a destabilization of the California economy would [have also] spread to other states."[1928] Lastly, the California Parties aver

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[1921] Ex. CAT-037 at 11-15. *See also* Ex. CAT-001 at 18.

[1922] Ex. CAT-037 at 12.

[1923] Ex. CAT-267 at 3-4. The California Parties aver that Professor Berck's model has been endorsed by courts. *See id*. at 6 (citing *Green Mountain Chrysler Plymouth Dodge Jeep v. Crombie*, 508 F. Supp. 2d 295 (D. Vt. 2007)).

[1924] *See* Ex. CAT-267 at 4-5.

[1925] *See id*.

[1926] *See id.* at 14-15. If costs associated with Powerex's sales are ignored, the damage would still have been hundreds of millions of dollars. *See* Tr. 1585:5-1586:2 (Berck).

[1927] *Id*. at 14. Professor Berck found that the other overcharge scenarios "would also impose extraordinary burdens on California consumers." *Id*. at 15.

[1928] Ex. CAT-267 at 6.

that had there been such decreases in personal income and increases in unemployment, the circumstances in San Diego described by Commissioner Florio would have been found state-wide.[1929]

1449. The California Parties argue that Professor Berck correctly stated that the proper focus is on the "total amount of overcharges" even though numerous parties have settled claims involving their sales to CERS.[1930] The California Parties state that "the cumulative effect on California depends on all the people who contributed."[1931] The California Parties assert that it would be wrong to disaggregate the harm and then say that any one seller's contribution to the harm is too small to consider.[1932]

1450. The California Parties further note that no Respondent witness even attempted to rebut Professor Berck's testimony. The California Parties state that Ms. Radel asserted that Respondents' contracts with CERS did not harm the public interest,[1933] but largely abandoned that claim on cross-examination.[1934]

1451. With respect to Ms. Radel's claim that the revenue bonds rendered the burden to consumers less excessive, the California Parties state using bonds to pay for past energy consumption is not the same as using bonds to pay for a capital asset that will be used in the future.[1935] The California Parties contend that Ms. Radel's approach "incorrectly and

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[1929] Tr. 1579:25-1580:2 (Berck).

[1930] Tr. 1615:6-7 (Berck). *See also* Tr. 2841:2-13 (Taylor) ("[i]f you try to decompose any of these manipulative activities down to a single party in a single transaction in a single point in time, it would be very difficult in a large market to say that one transaction altered the price").

[1931] Tr. 1615:10-11 (Berck).

[1932] Tr. 1609:13-1610:4 (Berck).

[1933] *See* Ex. S-15 at 20-21.

[1934] *See, e.g.*, Tr. 4171:22-4172:4 (Radel) (stating that the burden wouldn't be less just because it's spread over twenty years); Tr. 4178:11-19 (Radel) (stating that immediate pass-through of the costs would have burdened California's economy); Tr. 4181:2-12 (Radel) (stating that measuring the burden based only on the remaining Respondents, rewards the remaining Respondents for not settling).

[1935] Ex. CAT-269 at 5.

naively assumes that the burden of any principal amount, regardless of size, can be rendered reasonable or eliminated altogether if the payment plan is stretched out long enough."[1936] Additionally, the California Parties aver that stretching the payments out over time means that there are "customers who are paying today for electricity consumed in 2001, but who were themselves not electric consumers during that period."[1937] The California Parties further state that consumers now bearing the burden of the excessive prices is the type of "down the line" burden that *Morgan Stanley* held could amount to an "excessive burden."[1938] The California Parties assert that neither ratepayers, nor their state government, are required to choose between the protections of the FPA and avoidance of an economic disaster.

1452. The California Parties also disagree with Ms. Radel's focus on the impact of the overcharges on individual customers. The California Parties first note that a $70 charge is a high amount for an individual consumer.[1939] Furthermore, the California Parties assert that under Ms. Radel's approach, it would be impossible for a challenger to a spot market contract to ever demonstrate an excessive burden.[1940] The California Parties state that Ms. Radel's reasoning leads to the conclusion that "the more people you harm, the lower amount per person the harm equates to and therefore the harm is less."[1941]

1453. Furthermore, the California Parties aver that Ms. Radel's position "ignore[s] standard public finance norms."[1942] The California Parties state that the issuance of bonds to finance a past expense for wholesale electricity is, in itself, extraordinary and a strong signal that the burden of wholesale costs was not reasonable.[1943] The California

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[1936] Ex. CAT-636 at 3-5.

[1937] Ex. CAT-269 at 5.

[1938] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 552-53 (2008).

[1939] *Id*. at 8.

[1940] *Id*.

[1941] Tr. 1595:20-21 (Berck).

[1942] Ex. CAT-636 at 3.

[1943] *Id*.

Parties contend that basic principles of public finance indicate that "payments made over time, no matter how small, have as their economic burden their present value."[1944]

1454. The California Parties also note that because California paid a premium over the market interest rate, financing CERS's costs exceeded the actual expenditures.[1945] Additionally, the California Parties assert that the issuance of the bonds damaged California's credit rating, affecting the state's borrowing rate on all other bonds.[1946] The California Parties state that the resulting downgrade "would have affected as much as $25 billion in existing state debt and anything [that] California borrowed in the future."[1947]

1455. Next, the California Parties contend that Dr. Fox-Penner demonstrated that the blackouts that occurred during the CERS Period imposed excessive burdens on California.[1948] The California Parties state that there were seven blackouts that occurred in the CERS Period, totaling more than 22 hours where some portion of the state was without power.[1949] Additionally, there were hundreds of hours of emergency conditions, where unplanned outages could have occurred.[1950] The California Parties contend that the blackouts occurred not due to a lack of supply, but as a result of Respondents' and other sellers' actions.[1951] The California Parties state that there's no record of physical shortages in the Pacific Northwest and therefore, all shortages were economic.[1952]

1456. The California Parties state that there are direct and indirect costs associated with blackouts, including out-of-pocket expenses, property damage, lost opportunity costs, lost

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[1944] *Id*. at 4; Tr. 1611:18-22, 1612:10-15 (Berck).

[1945] Ex. CAT-289 at 153-54.

[1946] *Id.* at 154.

[1947] *Id*. at 155 (citing Vauhini Vara, *California's Ratings No Longer Lowest*, WALL ST. J., Feb. 1, 2013, at A3, *available at* http://online.wsj.com/article/SB10001424127887324610504578276141612731784.html).

[1948] Ex. CAT-161 at 81-87. *See also* Ex. CAT-269 at 9-10.

[1949] Ex. CAT-161 at 79.

[1950] *Id*. at 79-80 & n.34.

[1951] *See* Tr. 1211:19-1212:21 (Fox-Penner).

[1952] Tr. 1212:19-21 (Fox-Penner).

employee productivity, business relocation, lowered tax revenue, and higher costs for government operations.[1953] Dr. Fox-Penner estimated that the actual direct costs of blackouts during the CERS Period were in excess of $295 million dollars.[1954] The California Parties assert that these direct and indirect costs make the state "less attractive for personal and business investment in both the short and long run and leads to lower levels of economic growth."[1955]

1457. The California Parties note that neither Staff nor Respondents provided any testimony to refute Dr. Fox-Penner's analysis on the cost of blackouts. The California Parties state that Coral witness Mr. Tranen, who was once President and CEO of the CAISO, also testified about the importance of avoiding blackouts and about the costs that they can impose, stating that he considered avoiding blackouts the most important part of his job because the widespread negative effects.[1956]

1458. Next, the California Parties state that Mr. Taylor also discussed the harm to the public interest associated with the contracts with the Respondents. Mr. Taylor testified that Respondents charged unduly discriminatory prices and prices that placed an excessive burden on the California consumers.[1957] The California Parties state that Mr. Taylor also asserts that Respondents' activities threatened the reliability of the power system in the West.[1958]

1459. The California Parties also note that contract modification will serve important public interest considerations, such as not allowing the Respondents to keep gains that were the result of their wrongdoing[1959] and preventing undue discrimination.[1960]

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[1953] Ex. CAT-161 at 77-86.

[1954] *Id.* at 86. *See also* Tr. 1271:4-1272:5 (Fox-Penner).

[1955] Ex. CAT-161 at 86; Tr. 1271:17-1272:5 (Fox-Penner).

[1956] Tr. 3980:8-20 (Tranen).

[1957] Ex. CAT-041 at 134. *See also* Tr. 2765:4-2766:12 (Taylor).

[1958] Ex. CAT-041 at 134. *See also* Tr. 2840:9-15 (Taylor).

[1959] Ex. CAT-041 at 135.

[1960] The California Parties note that *Morgan Stanley* held that rates shown to be "unduly discriminatory" warranted contract modification under the public interest standard. *Id*. at 136 (emphasis in original) (citing *Morgan Stanley*, 554 U.S. at 548-49).

### (c) Respondents' Sales to CERS Are the Same as CERS's Sales to the CAISO

1460. The California Parties assert that Respondents' sales to CERS are identical to CERS's sales to the ISO, which the Commission already held should be modified.[1961] The California Parties state that CERS procured power from Respondents and turned around and sold it to the ISO at cost and "there is no economic basis upon which to justify different prices for these transactions."[1962] The California Parties note that Dr. Berry demonstrated that 99.2 percent Coral's and 99.9 percent of TransCanada's real-time sales to CERS match the date, hour, price, quantity, and location of CERS's sales to the ISO.[1963]

1461. The California Parties aver that the Commission-established MMCP should be used to determine whether rates in the Pacific Northwest were unjust and unreasonable because when the Commission capped prices in June 2001 based on the MMCP methodology, no seller could justify higher prices based on costs.[1964]

1462. Additionally, the California Parties contend that Respondents' claims that the market was competitive or that prices are explained by market fundaments are not credible.[1965] The California Parties note that the Commission has already held that "the markets did not work, that sellers had the ability to exercise market power, and that the

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[1961] *See* Ex. CAT-213 at 18-20 (referring to *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,512 (2001)). The California Parties argue that it is irrelevant that as a government agency, CERS was not subject to the Commission's refund order because it does not change the fact that Respondents' sales to CERS were made at prices that the Commission held were unjust and unreasonable and subject to refund. *See City of Redding v. FERC*, 693 F.3d 828 (9th Cir. 2012).

[1962] Ex. CAT-213 at 21.

[1963] *See id*. at 22-23.

[1964] Tr. 1646:20-1647:4 (Berry). *See generally San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418 (2001). *See also Investigation of Wholesale Rates of Public Utility Sellers of Energy and Ancillary Services in the Western Market Systems Coordinating Council*, 135 FERC ¶ 61,176, at PP 2-4 (2011) (subsequent history omitted).

[1965] *See* Ex. CAT-536 at 8-11.

prices that buyers paid were excessive."[1966] The California Parties also contend that there is substantial evidence of market manipulation during the CERS Period and Respondents ignored this evidence in making their claims. This evidence includes a number of CFTC settlements of market manipulation claims, the Enron Memos and guilty pleas by Enron traders for market manipulation, the Commission's revocation of Enron's market-based rates, a Commission settlement with generators that withheld from the day-ahead market, and a recent finding in Docket No. EL00-95 that there were tens of thousands of tariff violations by during the summer of 2000.[1967] The California Parties further note that the Crisis "ended abruptly when the Commission implemented West-wide price caps in June 2001" and prices have remained low.[1968]

1463. The California Parties conclude that the question this case presents is whether the FPA's "just and reasonable" mandate imposes some limits on Respondents' price demands or whether the FPA offers ratepayers no protection at all under the Commission's market-based rate scheme. The California Parties assert that if there is a zone of reasonableness within which market-based rates must fall, the Respondents' rates would violate the FPA and the Commission's obligation to protect consumers and the public interest.

### 2. <u>The California Respondents Initial Brief</u>

#### (a) The *Mobile-Sierra* Standard

1464. The California Respondents[1969] assert that the *Mobile-Sierra* presumption can only be avoided "where there is unfair dealing at the contract formation stage" or in "extraordinary circumstances" involving "unequivocal public necessity" where the

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[1966] *Id*. at 8. *Cf. San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515 (2001) (the Commission mitigated ISO OOM purchases during the CERS Period because sellers are able to exercise market power when supply is tight, which can result in unjust and unreasonable rates).

[1967] Ex. CAT-536 at 9-10.

[1968] *Id*. at 11, Figure 1.

[1969] The California Respondents are Shell Energy North America (US), L.P. (Shell Energy) (f/k/a Coral Power); TransAlta Energy Marketing (U.S.) Inc. and TransAlta Energy Marketing (California) Inc. (TransAlta); and TransCanada Energy Ltd. (TransCanada).

contract "seriously harms" the public interest or imposes "an excessive burden on consumers."[1970]

1465. The California Respondents state that in *Mobile*, the Court established that the "interest[] of contract stability" is balanced with public regulation as the Commission retains the right to modify the contracts "when necessary in the public interest."[1971] Similarly, in *Sierra*, the Court held that the Commission's sole concern should be "whether the rate … adversely affect[s] the public interest— … cast[ing] upon other consumers an excessive burden, or be unduly discriminatory."[1972]

1466. The California Respondents assert that since the issuance of *Mobile* and *Sierra*, the Court has consistently limited the Commission's authority to abrogate freely negotiated agreements. For example, in *Permian Basin*, the Court ruled that "[t]he regulatory system created by the [NGA] is premised on contractual agreements voluntarily devised by the regulated companies; it contemplates abrogation of these agreements only in circumstances of unequivocal public necessity." [1973] The Court also reiterated its holding in *Sierra* that "the Commission may not, absent evidence of injury to the public interest, relieve a regulated company of 'its improvident bargain.'"[1974] Moreover, the California Respondents note that in *Verizon Communications, Inc. v. FCC*, the Court clarified that its prior pronouncement concerning the impropriety of relieving a party to the contract of an "improvident bargain" did not apply just to the regulated entity.[1975]

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[1970] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530, 534, 547, 549 n.4, 550 (2008). *See also* Order Granting Interlocutory Appeal at P 12.

[1971] *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344 (1956).

[1972] *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956).

[1973] *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968) (*Permian Basin*).

[1974] *Id.* at 821.

[1975] *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002).

1467. Next, the California Respondents discuss the Supreme Court's recent decision in *Morgan Stanley*.[1976] The California Respondents first note that *Morgan Stanley* dealt with the same context as this proceeding – a public utility's market-based rates alleged to be excessive.[1977] The California Respondents assert that the Court rejected arguments that the presumption should not apply because the contracts were entered into at a time of historically high rates.[1978] Rather, the Court applied the *Mobile-Sierra* presumption, stating that "[t]he presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*."[1979] The California Respondents note that the Supreme Court specifically rejected the Ninth Circuit's conclusion that the Commission must determine whether a contract was formed in a dysfunctional market before applying the *Mobile-Sierra* presumption, stating that "one of the reasons that parties enter into wholesale-power contracts is precisely to hedge against the volatility that market imperfections produce …."[1980] The Court also noted that "evaluating market 'dysfunction' is a very difficult and highly speculative task—not one that the FPA would likely require the agency to engage in before holding sophisticated parties to their bargains."[1981]

1468. Notwithstanding its holding that the *Mobile-Sierra* presumption should apply in a dysfunctional market, the Court acknowledged that the presumption would not apply where the illegal action of one of the parties to a contract led to the dysfunctional market conditions that affected contract formation.[1982] However, the Court cautioned that the

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[1976] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008).

[1977] The California Respondents note that this contrasts with earlier cases that involved claims by the public utilities or natural gas companies that negotiated unreasonably low contracts under a cost-based regulatory regime.

[1978] *Morgan Stanley*, 554 U.S. at 530.

[1979] *Id.* (emphasis added).

[1980] *Id*. at 547.

[1981] *Id.* at 548.

[1982] *Id.* at 547.

Commission must find "a causal connection between unlawful activity and the contract rate" before there will be any forfeiture of the presumption.[1983]

1469. The California Respondents state that the Court also rejected the Ninth Circuit's use of a "zone of reasonableness" test to determine whether a rate was so high as to impose an excessive burden on consumers.[1984] Specifically, the Court reasoned that the use of marginal cost as a test of justness and reasonableness "fails to accord an adequate level of protection to contracts."[1985] Moreover, the Court noted that to prove harm to the public interest sufficient to overcome the *Mobile-Sierra* presumption, the harm must be "more than a small dent in the consumer's pocket."[1986]

1470. The California Respondents acknowledge that *Morgan Stanley* involved long-term energy contracts, but state that the Commission has confirmed that the holdings in *Morgan Stanley* apply equally to this case involving spot market transactions.[1987] Thus, the California Respondents contend that to overcome the *Mobile-Sierra* presumption, the California Parties must prove that a contract rate imposed an excessive burden on consumers that seriously harmed the public interest.[1988] The California Respondents note that the D.C. Circuit has characterized the burden imposed by the *Mobile Sierra* doctrine as "practically insurmountable" and "almost

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[1983] *Id.* at 554–55.

[1984] Under its test, the Ninth Circuit had equated rates above marginal costs as exceeding a zone of reasonableness, imposing an excessive burden on consumers. *Id.* at 550.

[1985] *Id.* at 548. *See also Id.* at 550-51 ("A presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract based-regulation. We have said that, under the Mobile-Sierra presumption, setting aside a contract rate requires a finding of 'unequivocal public necessity' or 'extraordinary circumstances'. In no way can these descriptions be thought to refer to the mere exceeding of marginal cost." (citations omitted)).

[1986] *Id*. at 551 n.6.

[1987] Order on Rehearing at P 20; Order on Remand at P 20.

[1988] *See* Order Granting Interlocutory Appeal at P 12.

insurmountable."[1989] The California Respondents further state that the Commission has observed that "[p]reservation of contracts has, if anything, become even more crucial since the policy [expressed in the *Mobile-Sierra* doctrine] was first adopted."[1990]

### (b) The *Mobile-Sierra* Standard for Marketers with Market Based Rates

1471. The California Respondents state that it is undisputed that the Commission had authorized each Respondent to sell electric energy at market-based rates because the Commission found that the Respondent lacked market power. The California Respondents note that the Commission predicated its market-based rate program on the finding that power marketers, such as Respondents, "increase efficiency in power supply markets and in turn ultimately lower the cost of electricity."[1991] The Commission also has recognized that power marketers "assume significant risk" and "cannot survive" without "encourag[ing] exchange efficiency in electric power markets that otherwise might not be attained."[1992]

1472. The California Respondents asserts that supply and demand determine prices in energy markets and can put upward pressure on prices and cause wholesale energy prices to be "notoriously volatile."[1993] In recognizing these conditions, the Commission has explained that pricing flexibility permits sellers "to respond quickly to changing market conditions" and ensures that "prices accurately reflect market conditions of scarcity and abundance," furthering "the Commission's statutory goals of promoting efficiency and coordination."[1994]

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[1989] *Papago Tribal Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (Scalia, J.), *cert. denied*, 467 U.S. 1241 (1984); *Kansas Cities v. FERC*, 723 F. 2d 82, 87-88 (D.C. Cir. 1983).

[1990] *PacifiCorp*, 99 FERC ¶ 61,381, at 62,614 (2002).

[1991] *Citizens Power & Light Corp.*, 48 FERC ¶ 61,210, at 61,776 (1989).

[1992] *Id.* at 61,776-77.

[1993] *Idaho Power Co. v. FERC*, 312 F.3d 454, 461 (D.C. Cir. 2002).

[1994] *Citizens Power & Light Corp.*, 48 FERC ¶ 61,210, at 61,777 (1989).

1473. The California Respondents note that sellers lacking market power cannot obtain prices above those prevailing in the market.[1995] Further, if a seller that lacks market power were to attempt to obtain an excessive price, the buyer would have the option to turn to lower-priced suppliers.[1996]

1474. Next, the California Respondents state that in establishing its regulatory program, the Commission recognized that market-based suppliers need to account for the risk of non-payment in their prices.[1997] The California Respondents contend that when Respondents were negotiating the price of energy for sales to CERS, Respondents fairly took into account the increase in risk they faced.[1998] The California Respondents state that CERS was a new entity created following the collapse of the organized California markets and its purchases were not backed by the full faith and credit of the state of California.[1999] The California Respondents note that this atmosphere led multiple market participants to refuse to make any sales to CERS.[2000] The California Respondents further state that the California Parties' witnesses acknowledged that premiums had to be paid to suppliers "willing to take the risk" of trading with CERS.[2001] The California Respondents also contend that the California Parties did not consider the fact that Respondents could have sold their supplies to parties that were more creditworthy than CERS or could have avoided the risk of selling to CERS altogether.

1475. The California Respondents also aver that Respondents did not acquire market power during the CERS Period. The California Respondents assert that Respondents were marketers with little market share.[2002] The California Respondents argue that the

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[1995] *Elizabethtown Gas Co. v. FERC,* 10 F.3d 866, 870-71 (D.C. Cir. 1993).

[1996] *See, e.g., Louisville Gas & Elec. Co.,* 62 FERC ¶ 61,016, at 61,144 (1993).

[1997] *FirstEnergy Solutions Corp.,* 113 FERC ¶ 61,338, at P 19 (2005).

[1998] Ex. TRC-1at 30:17-18; Ex. SNA-1 at 8-14.

[1999] Ex. TRC-1 (Morris) at 33:15-34:7.

[2000] Ex. PNR-1 at 19:8-23; Ex. CAT-016; Ex. SNA-12; Ex. CAT-041 at 43:23-44:8. *See generally* Ex. TRC-1 at 30-50. *See also* Ex. TRC-29; Ex. TRC-30.

[2001] *See* Ex. TRC-25 at 1; Ex. TRC-26 at 1; Tr. 712:17-715:5 (Hart); Tr. 2495:15-2496:5 (Taylor); Tr. 1551:22-1552:6 (Fox-Penner).

[2002] Ex. SNA-9 at 6:4-6; Ex. TRC-1 at 164:12-13.

California Parties did not perform a valid analysis to determine whether any Respondent *in fact* possessed or exercised market power.[2003] The California Respondents aver that the Commission affirmatively found that each Respondent lacked market power, and the California Parties presented no credible evidence that a Respondent accumulated market power in the Pacific Northwest following the grant of its market-based rate authority.

1476. The California Respondents state that even though some sellers declined to sell to CERS, CERS had forty to fifty potential suppliers.[2004] Moreover, the California Respondents state that trader tapes reveal instances where CERS traders rejected offers from Respondents and cut the quantity of megawatts CERS had initially agreed to purchase.[2005]

1477. Furthermore, the California Respondents assert that CERS could have made purchases at trading hubs other than COB or in markets other than real-time. The California Respondents contend that CERS's decisions to purchase from the Respondents at COB allowed CERS to avoid or reduce purchases from alternatives with higher prices.[2006] Moreover, the California Respondents aver that the California Parties did not study the extent to which CERS chose not to buy supplies that were available to it in the day-ahead market.[2007]

1478. Next, the California Respondents argue that the California Parties request for a market-wide remedy based on the MMCP is inappropriate. The California Respondents state that in the Order on Remand, the Commission specifically discussed the fundamental differences between the California organized markets and the Pacific Northwest bilateral market and rejected the MMCP approach taken in the California refund proceeding.[2008] The Commission further stated that "general allegations of market

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[2003] *See, e.g.*, Ex. TRC-1 at 129:6-9; Ex. TRC-4; Tr. 2696:6-12 (Taylor).

[2004] Tr. 2579:7-21 (Taylor).

[2005] *See, e.g.*, Ex. TRC-77; Ex. TRC-81; Ex. TRC-114; Ex. TRC-118; *see also* Tr. 3837:3-3838:2 (Morris).

[2006] *See* Ex. CAT-414.

[2007] Tr. 2535:25-2536:7 (Taylor).

[2008] Order on Remand at PP 18, 24.

dysfunction in the Pacific Northwest are an insufficient basis for overcoming the *Mobile-Sierra* presumption or finding that it is inapplicable."[2009]

1479. Furthermore, the California Respondents argue that Dr. Berry's analysis is in conflict with the *Mobile-Sierra* doctrine, as explained in *Morgan Stanley*. As discussed above, the California Respondents assert that in *Morgan Stanley*, the Supreme Court rejected the contention that *Mobile-Sierra* would only apply if the contract rates fell within a "zone of reasonableness" or were comparable to the "marginal cost" of the seller.[2010] The California Respondents state that the MMCP, which is used by Dr. Berry to overcome the *Mobile-Sierra* presumption, is a proxy for the marginal costs.

1480. The California Respondents also argue that there is no evidence to support using the MMCP, which was derived for use in the CAISO's organized market, in the Pacific Northwest bilateral market. The California Respondents assert that the MMCP was based upon the marginal costs of California generators and does not bear any relationship to Respondents' costs for sales in the Pacific Northwest.[2011] The California Respondents state that Dr. Berry did not even know what energy sources were used to generate the electric energy Respondents sold to CERS.[2012] Thus, the California Respondents conclude that there is no evidence to establish that the MMCP approximates the marginal costs and the heat rates of the generating units that produced the energy that Respondents sold to CERS in the Pacific Northwest.

1481. Moreover, the California Respondents aver that Dr. Berry failed to account for the significant differences between California's organized markets and the bilateral market in the Pacific Northwest. The California Respondents state that Dr. Berry effectively treats the Pacific Northwest transactions at issue as if they took place in the California ISO.

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[2009] *Id.* P 21.

[2010] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548-50 (2008).

[2011] Dr. Berry admitted that the heat rate data for generators that did not bid into the BEEP Stack would not have been considered in calculating the MMCP. Tr. 1646:5-23 (Berry).

[2012] Tr. 1649:14-18 (Berry). The California Respondents also contend that the California Parties failed to address how the natural gas pricing data used to derive the MMCP might change for transactions in the Pacific Northwest. Tr. 1650:6-1651:24 (Berry).

However, the California Respondents note that in 2001, the California Parties took a different position.[2013]

1482. The California Respondents also argue that Dr. Berry's testimony contains numerous factual errors. For example, Dr. Berry wrongly describes the Pacific Northwest as an "organized market."[2014] Dr. Berry also inaccurately states that Respondents real-time sales to CERS were bilateral OOM sales to the ISO.[2015] The California Respondents contend that Dr. Berry's assertion ignores the fact that there is a specific definition of ISO OOM sales and that definition is inapplicable to the sales made by the Respondents to CERS.[2016]

1483. The California Respondents also contend that the Commission ruled that refunds for the ISO's OOM transactions were appropriate because the ISO OOM purchases were "no different than purchases through [CAISO markets because] [b]oth types of purchases are made by the ISO to procure the resources necessary to reliably operate the grid."[2017] With respect to CERS's purchases, the California Respondents note that the Ninth Circuit stated that "[u]nlike the Cal-ISO OOM transactions … the *CERS transactions occurred in a market that was not directly influenced by the market manipulations in the Cal-ISO and CalPX spot markets*."[2018]

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[2013] *See* California *ex rel.* Bill Lockyer, the California Electric Oversight Board, and the Public Utilities Commission of California, Brief, Docket Nos. EL01-10-000, EL01-10-001, at 8 (filed Sept. 17, 2001) ("CERS' bilateral transactions in the Pacific Northwest are not purchases through the California ISO or California PX markets").

[2014] Tr. 1641:10-19 (Berry).

[2015] Ex. CAT-213 at 19:16-18.

[2016] Tr. 1629:6-13 (Berry); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 97 FERC ¶ 61,275, at 62,195 (2001).

[2017] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515 (2001).

[2018] *Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1063 (9th Cir. 2006) (emphasis added) (ISO OOM transactions were "directly associated with the CalPX and Cal-ISO markets. However, the bilateral CERS transactions occurred in a different market …).

1484. Lastly, the California Respondents aver that Dr. Berry's assertion that the Pacific Northwest market was not competitive is inaccurate. The California Respondents state that Dr. Berry relies on the Commission's determination concerning the OOM sales to the ISO.[2019] However, the California Respondents assert that this is at odds with a primary purpose of this proceeding, which is "to address possible unlawful activity that may have influenced prices in the Pacific Northwest spot market."[2020] The California Respondents also note that Dr. Berry testified that the "prices charged by Respondents have already been found to be unjust and unreasonable,"[2021] even though the purpose of the proceeding is determine whether the prices charged to CERS were unjust and unreasonable or not in the public interest.

### (c) Evidence of Excessive Burden on Consumers

1485. The California Respondents state that in order to overcome the *Mobile-Sierra* presumption, the California Parties must demonstrate on a contract-by-contract basis that a rate in a particular contract so excessively burdened consumers as to require its abrogation as an "unequivocal public necessity."[2022] The California Respondents assert that the California Parties offered no contract-specific proof and as a matter of law, have not overcome the *Mobile-Sierra* presumption.

1486. The California Respondents contend that high prices alone do not demonstrate an undue burden on consumers. The California Respondent state that electricity prices produced by fundamental supply and demand forces may be high or low but are not unduly burdensome for purposes of overcoming the *Mobile-Sierra* presumption. The California Respondents assert that it would be misguided to abrogate a bilateral contract for no other reason than that market forces produced high prices. The California Respondents state that this is underscored by the Supreme Court's rejection of the "zone of reasonableness" test in *Morgan Stanley*.[2023] Furthermore, the California Respondents

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[2019] Ex. CAT-536 at 8:14-17.

[2020] Order on Remand at P 16.

[2021] Ex. CAT-536 at 5:18-19.

[2022] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 534 (2008) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968)).

[2023] *Morgan Stanley*, 554 U.S. at 548.

state that the Commission "refute[d] California's argument that simply identifying high prices should be sufficient to *overcome or avoid* the [*Mobile-Sierra*] presumption."[2024]

1487. The California Respondents also state that the Respondents provided the only comprehensive analysis of the market fundamentals in the Pacific Northwest, which concluded that the high prices are fully explained by those fundamentals.[2025] The California Respondents assert that the reduced availability of hydroelectric generation, coupled with high demand for natural gas-fired generation, nuclear plant and qualifying cogenerator outages, air emission limits, and unprecedented levels of demand, together with other factors caused a supply-and-demand imbalance that resulted in historically high prices.[2026]

1488. Next, the California Respondents contend that even if price alone could create an undue burden sufficient to overcome the *Mobile-Sierra* presumption, the evidence demonstrates that California ratepayers never experienced burdensome prices. The California Respondents state that during the CERS Period, and continuing into 2002, the retail rates of California investor-owned utilities remained subject to a retail rate freeze that kept those rates depressed far below prevailing wholesale market prices.[2027] The California Respondents note that Professor Hogan cited the rate freeze as "one of the critical public policy decisions which served to exacerbate the Western Power Crisis."[2028]

1489. The California Respondents further aver that any possible burden stemming from high wholesale prices pre-dated the creation of CERS. The California Respondents note that the Official Statement that accompanied the issuance of California's first revenue bonds cited the IOU's inability to pay power bills due to the CalPX and CAISO in December 2000, the eventual collapse of the organized California markets, the January 2001 credit rating downgrade for PG&E and SCE, and the reduction of power supply resources bid into the California market due to the credit difficulties.[2029]

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[2024] Order Granting Interlocutory Appeal at P 15 (emphasis added).

[2025] *See generally*, Ex. PNR-1.

[2026] *Id.*

[2027] *See* Ex. CAT-040 at 23; Ex. CAT-037 at 15:9-13. *See also* Ex. PNR-1 at 80.

[2028] Ex. PNR-1 at 77:3-7.

[2029] Ex. CAT-040 at 23.

1490. The California Respondents also state that the California Parties never presented evidence showing that retail ratepayers in California ever paid "burdensome" rates. The California Respondents note that Dr. Morris demonstrated that California's retail rates have been consistent with rates in other states that voluntarily restructured their electric industries and that "price increases that were ultimately passed on to rate-payers [in California] were not atypical of rate changes in other states over a 20-year period."[2030]

1491. With respect to Commissioner Florio's testimony, the California Respondents contend that the evidence is neither credible nor relevant.[2031] The California Respondents state that Commissioner Florio failed to mention that the CPUC retroactively reset the high prices in SDG&E's service area to the same below-market cap that applied to SCE and PG&E and continued that price cap for all three companies throughout the CERS Period.[2032] Moreover, the California Respondents assert that the testimony is irrelevant because it addresses a period preceding CERS's creation[2033] and fails to connect any specific Respondent sale to an alleged price effect or excessive burden.[2034]

1492. Next, the California Respondents argue that the high cost of outages demonstrates that Respondents sales to CERS were beneficial and served the public interest. The California Respondents state that Coral witness Mr. Tranen testified that when he was President and CEO of the ISO he considered avoiding service interruptions to be "the most important part of [his] job" because "the[ir] impacts can be very high."[2035] Additionally, Mr. Hart attested that CERS had the same "primary concern."[2036] The California Respondents note that Dr. Fox-Penner estimated that service interruptions

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[2030] Ex. TRC-1 at 166:1-169:7.

[2031] The California Respondents note that the substance of Commissioner Florio's testimony goes only to his perception, not to the truth of the hearsay testimony that composes the bulk of his testimony. Tr. 544:8-19.

[2032] Ex. CAT-039 at 40.

[2033] Ex. CAT-001 at 3:2-4.

[2034] *See* Ex. S-15 at 21:6-8.

[2035] Tr. 3980:8-15 (Tranen).

[2036] Ex. CAT-012 at 4:22-23, 8:14-15.

typically cost between $10 and $20 per kilowatt-hour,[2037] which is thirty to sixty times more than the average price of Respondents' sales to CERS.[2038]

1493. The California Respondents assert that no Respondent was under any legal obligation to sell to CERS.[2039] Yet, Respondents sold to CERS, despite the risk of nonpayment, at prices below other alternatives. The California Respondents state that Respondents' sales to CERS averted shortages, not caused them. The California Respondents further note that had Respondents not sold to CERS, CERS would have been required to purchase from other, higher priced sellers.[2040]

1494. Next, the California Respondents discuss Professor Berck's economic modeling. The California Respondents contend that Professor Berck's models addresses the question of what could have happened, not what did happen. The California Respondents state that Professor Berck models the effects on income and employment in California based on a simulation reflecting a hypothetical that never occurred: if CDWR did not issue the bonds, if the California PUC unfroze retail rates, and if the cost of CERS's purchases immediately flowed through in retail rates.[2041]

1495. The California Respondents assert that in *Morgan Stanley*, the Supreme Court affirmed a remand to the Commission in part because it could not discern whether the Commission "looked simply to whether consumers' rates increased immediately upon the relevant contracts' going into effect, rather than determining whether the contracts imposed an excessive burden 'down the line.'"[2042] The California Respondents state that on remand, the Commission determined that a buyer attempting to demonstrate a burden "down the line" should compare the rates of its challenged long-term contract with actual market prices of forward contracts that could have provided substitute power.[2043] The

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[2037] Ex. CAT-161 at 84:1-7.

[2038] *See* Ex. SNA-44.

[2039] *See* Ex. SNA-9 at 6:4-6; Tr. 2525:8-11, 2651:6-8 (Taylor).

[2040] *See* Ex. TRC-1 at 126:4-6; Ex. CAT-414.

[2041] Ex. CAT-267 at 3:20-4:2; Tr. 1565:15-18 (Berck).

[2042] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 552 (2008).

[2043] *Nev. Power Co.*, 125 FERC ¶ 61,312, at P 20 (2008).

California Respondents argue that the California Parties failed to present this type evidence, such as a comparison of the rates in the challenged contracts to other offers that CERS rejected in favor of Respondents' contracts.

1496. The California Respondents note that the Commission also cautioned that "the 'down the line' burden should be measured by actual market data … and not speculation or modeling when presenting evidence."[2044] The Commission also emphasized that the "down the line" analysis should focus on consumers' rates.[2045] The California Respondents contend that the California Parties did the exact opposite in this proceeding, submitting only economic simulations about what could have happened, but offering no evidence addressing the actual cost of Respondents' sales to CERS on the retail customers.

1497. Lastly, the California Respondents state that Trial Staff witness Ms. Radel provided testimony on the actual impact of the bond charge on customers of the investor owned utilities. Specifically, Ms. Radel calculated that that each California customer is paying $0.27 per month for what the California Parties allege were overcharges to CERS for spot electricity.[2046] The California Respondents contend that even Ms. Radel's calculation overstates the relevant cost to California customers because it includes sales to CERS by now-settled Respondent Powerex. The California Respondents aver that when Powerex's sales to CERS are removed, the monthly bond charge per customer for *all* alleged Respondent seller overcharges (including the Avista Entities and TransAlta) falls to just $0.069 per month.[2047] On a per contract basis, which is the proper unit of measurement, the California Respondents state that California ratepayers pay just $0.000134 per contract.[2048] The California Respondents contend that such a miniscule

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[2044] *Id.* P 23.

[2045] *Id.* P 21 ("Buyers attempting to demonstrate an excessive burden must submit evidence on: (1) given the contract, what consumers' rates were; (2) what consumers' rates would have been down the line in the absence of the contract; and (3) how the difference imposes an excessive burden on consumers.").

[2046] *See* Ex. S-15 at 21:17-22:8. Ms. Radel concludes that the alleged overcharges "did not cause and is currently not causing an excessive burden on California consumers." *Id.*

[2047] The California Parties allege approximately $266.88 million in overcharges against Coral, TransCanada, the Avista Entities, and TransAlta.

[2048] Mr. Taylor counts 510 contracts, including those by the Avista Entities and TransAlta. *See* Ex. CAT-041 at 126-130, Tables III-8 through III-12.

amount cannot possibly be an excessive burden for purposes of overcoming the *Mobile-Sierra* presumption.

**(d) Respondents' Sales Benefited California and Were in the Public Interest**

1498. The California Respondents argue that Respondent sellers found ways to manage unique risks in a supply-constrained market and provided power to CERS where it sought energy at market prices. The California Respondents assert that Respondent sellers helped California overcome supply shortages that were largely of the state's and its investor-owned utilities' own making.

1499. The California Respondents state that Respondents provided energy when California was experiencing its most severe electric energy shortages at the locations where energy was most needed.[2049] The California Respondents assert that Respondents were able to purchase energy from many sources, including from sellers unwilling to sell directly to CERS, and worked around credit issues in order to supply CERS with power.[2050] Moreover, the California Respondents state that Respondents sought out new sources of energy, purchased transmission service contracts, and paid charges for ancillary services and transmission losses necessary to secure energy supplies for CERS.[2051] The California Respondents argue that greater harm was avoided because Respondents, without any legal requirement to do so, continued to make energy sales to CERS at prices below CERS's supplier of last resort.[2052] The California Respondents note that Dr. Fox-Penner calculated the value of lost load in California at $18,240/MWh, a cost far higher than the Respondents' sales to CERS.[2053]

1500. The California Respondents note that energy in the Desert Southwest was consistently available at lower cost than energy in the Pacific Northwest;[2054] however,

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[2049] Respondents (including the Avista Entities and TransAlta) sold more than 1,000,000 MWh of electric energy to CERS, primarily at COB. Ex. SNA-44.

[2050] *See, e.g.*, Ex. SNA-1 at 10:21-11:5; Ex. TAE-1 at 7:9-10. *See also* Ex. CAT-016 (listing twenty-two sellers refusing to do business with CERS).

[2051] *See* Tr. 3513:5-3515:1 (Harrigan).

[2052] Ex. TRC-1 at 126:4-6.

[2053] Ex. TRC-1 at 126:2-3.

[2054] Ex. TAE-1 at 5:13-20; Tr. 3937:7-13 (Tranen); Tr. 950:23-25 (Lee).

frequent south-to-north congestion on the ISO-controlled transmission system often prevented transmission of the lower-cost energy.[2055] The California Respondents contend that its sales either supplied CERS with energy from northern regions of the Western Interconnection or used transmission rights on transmission facilities not subject to ISO control, such as the DC tie, to move available energy supplies from the Desert Southwest.[2056] The California Respondents aver that the California Parties fail to explain how the public interest would have been better served by leaving energy in Southern California where it was not needed and stranding this available energy when the Pacific Northwest was experiencing scarcity.

1501. The California Respondents further note that the California Parties wrongly claim that Respondents had no reason to perceive that sales to CERS carried a higher than normal risk of nonpayment. The California Respondents argue that this assertion ignores the well-known and documented history that led California to create CERS.[2057] The California Respondents state that Mr. Hart has characterized the situation as the "California problem," with sellers unwilling to deal with any California entity because the CalPX, ISO, and the IOUs had failed to make payments.[2058] The California Respondents aver that Respondents used credit limits and risk premiums to account for the considerable risks of non-payment and regulatory clawback. The California Respondents contend that these methods of managing risk are supported by the circumstances leading up to the CERS Period, including the CalPX bankruptcy and the non-payment by the ISO.[2059]

1502. The California Respondents also assert that there was significant litigation risk in selling to CERS. The California Respondents note that public pronouncements by California policymakers and officeholders leading into 2001, when CERS began operations, were overtly hostile, labeling energy sellers as criminal enterprises[2060] and

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[2055] Ex. CAT-641 at 7:14-19.

[2056] The California Respondents note that the California Parties allege that these transactions are False Exports. However, Mr. Taylor admitted that no rule or tariff ever prohibited bilateral exports out of California. *See* Ex. TRC-4 at 12-13.

[2057] Ex. TRC-19 at 12. *See also* Ex. CAT-014 and Ex. CAT-015 (stating that CERS's purchases are not backed by the full faith and credit of the State of California).

[2058] Ex. SNA-12.

[2059] Ex. PNR-1 at 8:16-19:22.

[2060] *See, e.g.*, Hearing Transcript, Docket No. EL00-95-000, at 9 (Nov. 4, 2000).

threatening to exercise eminent domain to seize generators.[2061] The California Respondents further state that CPUC filed complaints at FERC and the Attorney General unambiguously stated his intent to pursue all available legal actions to claw back any monies paid to sellers over historical levels. The California Respondents argue that this proceeding demonstrates that the litigation risk was not illusory.

1503. Furthermore, the California Respondents assert that the California Parties' claim that litigation risk could have been avoided simply by offering energy at "appropriate" prices is misguided because the California Parties themselves have not consistently suggested the "appropriate" price.[2062] Moreover, the California Respondents state that any "appropriate" price suggested by the California Parties ignores the fact that many sellers were marketers, who were also often paying prices far in excess of historical levels. The California Respondents note that many of its transactions with CERS involved substantial effort (and cost) by the seller to move energy from areas experiencing temporal surpluses to locations that CERS required.[2063]

1504. Next, the California Respondents contend that the California Parties have failed to support their claim that Respondents withheld energy from California.[2064] The California Respondents argue that Respondents did not have any legal obligation to sell any energy to CERS, let alone an obligation to sell in any specific time frame or location. Additionally, the California Respondents assert that the California Parties have arbitrarily dismissed Respondents' business reasons for needing to hold available supplies until real-time. The California Respondents state that there is no evidence that Respondents "backed down" what little uncontracted generation they had under their control. Moreover, the California Respondents contend that by offering more energy in the day-of market, sellers had less ability to demand higher prices in that market.[2065]

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[2061] Tr. 682:2-5 (Hart).

[2062] The California Respondents note that the California Parties have suggested the following standards in this proceeding alone: (1) the MMCP; (2) Mr. Taylor's *Power Markets Week* plus seventy-five dollars screen; and (3) Dr. Fox-Penner's multiple price discrimination benchmarks.

[2063] *See, e.g.*, Ex. TRC-1 at 10:4-6.

[2064] Ex. PNR-1 at 24:1-6.

[2065] Ex. TRC-1 at 119:5-13.

1505. Next, the California Respondents argue that the IOUs and the state's policies exacerbated the tight supply conditions during the energy crisis.[2066] The California Respondents state that the factors that contributed to the Western Energy Crisis include (1) California's historic heavy reliance on imported energy;[2067] (2) decisions by California policymakers that effectively limited additional generating capacity within the state;[2068] (3) an electric restructuring plan that lacked critical safeguards contained in contemporaneously launched organized market designs;[2069] (4) California's persistent refusal to raise retail rates during the Crisis;[2070] (5) energy-limited Western generation resources; and (6) a convergence of high demand and limited supply of electric energy. The California Respondents argue that Respondents' sales to CERS did not intensify the crisis, but helped alleviate the supply shortage and provided time for the market to recover.[2071]

1506. The California Respondents contend that the California Parties wrongly claim that Respondents limited the available supply of energy. The California Respondents state that the forces that produced tight supply conditions in 2000 and 2001 had been building for years, wholly independent of Respondents. The California Respondents note that historically, interregional north-south exchanges were possible through the diverse seasonal demand of the winter peaking Pacific Northwest and the summer peaking Desert Southwest.[2072] However, in order for this relationship to work, policy makers in each region needed to ensure that resources overall were sufficient to meet the projected load of the entire Western Interconnection. The California Respondents assert that the State of

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[2066] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121 (2000), at 61,371-72 (2000) ("the structural defects in the California market [were] created over many years in an environment which relied on regulatory rather than market responses to consumer needs").

[2067] *Id.* at 61,357; *see also* Ex. TRC-14 at 4.

[2068] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,372 (2000).

[2069] *Id.* at 61,354, 61,372.

[2070] Ex. PNR-1 at 77:3-7.

[2071] Ex. PNR-1 at 7:17-8:4.

[2072] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,357 (2000).

California failed to ensure that overall supply was sufficient.[2073] The California Respondents also contend that California policy makers failed to consider potential transmission constraints or the potential for reduced output from energy-limited resources.

1507. The California Respondents note that prior to the crisis, California policymakers reached decisions that made the state vulnerable to adverse supply conditions including: (1) policies making it more difficult to site new generation and transmission;[2074] (2) the CPUC allowing limited transmission capacity between the north and south; (3) incentivizing IOUs to divest large amounts of generation capacity;[2075] (4) preventing IOUs from negotiating forward purchase contracts;[2076] (5) implementing a market structure without the pricing structure necessary to encourage investment in new generation;[2077] (6) using state revenue bonds to reduce retail rates by ten percent at the outset of restructuring in 1996;[2078] (7) capping retail rates until March 2002;[2079] and (8) failing to put into place conservation measures once energy shortages became apparent.[2080]

1508. Additionally, the California Respondents state that during the crisis, policy makers made the following errors that exacerbated the crisis: (1) declining to support CERS's purchases with the full faith and credit of the state; (2) re-freezing retail rates well below prevailing wholesale market prices;[2081] (3) accusing sellers of crimes and threatening

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[2073] *Id.* at 61,360 n.47 (noting that "over the past five years load in California has risen by 5,222 MW while resources have increased only 672 MW").

[2074] *Id.* at 61,372.

[2075] 1996 Cal. Legis. Serv. 854, § 367(b) (West) (AB 1890).

[2076] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,360 (2000)..

[2077] *Id.* at 61,358; Ex. PNR-1 at 153:15-154:20.

[2078] AB 1890 § 1(e).

[2079] *Id.*; *see also* Ex. PNR-1 at 76-80.

[2080] *Id.* at 37:16-38:9, 77:5-7.

[2081] Ex. PNR-1 at 80:1-15.

punitive legislation and litigation;[2082] and (4) limiting NOx emissions from the gas turbine generators that had been designed to supply peak load in California.[2083]

1509. The California Respondents also argue that the IOUs did not adequately protect themselves against the possibility of tight supplies and made poor choices once the tight supply conditions became apparent. For example, the IOUs did not seek to negotiate contracts to hedge their risk, a regular feature of other restructuring efforts.[2084] Additionally, the IOUs stopped payments to Qualifying Facilities (QF), prompting the QFs to terminate electric energy deliveries, a response that further limited already tight supply conditions.[2085]

#### (e) The Equitable Doctrine of Unclean Hands Bars the California Parties' Request for Contract Modification

1510. The California Respondents state that the California Parties seek the equitable remedy of contract modification. The California Respondents assert that only in extreme circumstances does the Commission grant this equitable relief[2086] and that courts and Commission are guided by the equitable maxim that "he who comes into equity must have clean hands."[2087] The California Respondents contend that the California Parties cannot prevail on their 1(B) claims because CERS took unfair advantage of its status as an appendage of the State of California to access non-public ISO information that conferred on it a competitive advantage in the market.

1511. The California Respondents state that the Supreme Court has instructed that "[i]t is one of the fundamental principles upon which equity jurisprudence is founded, that before a complainant can have … standing in court he must first show that not only has

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[2082] *Id.* at 191; JAMES L. SWEENEY, THE CALIFORNIA ELECTRICITY CRISIS 17 (2008).

[2083] Ex. PNR-1 at 126:4-6.

[2084] *See* Ex. TRC-11.

[2085] Ex. PNR-1 at 111, 112 Table 26.

[2086] *See Pub. Utils. Comm'n of the State of Cal. v. Sellers of Long Term Contracts to the Cal. Dept. of Water Res.*, 99 FERC ¶ 61,087, at 61,383 (2002).

[2087] *Precision Instrument Mfr. Co. v. Auto. Maint. Mach. Co.*, 324 U.S. 806, 814 (1945).

he a good and meritorious cause of action, but he must come into court with clean hands."[2088] The California Respondents assert equity requires that any party seeking relief must have acted fairly and without fraud or deceit or employed any unfair means to gain advantage as to the controversy at issue.[2089]

1512. The California Respondents further note that courts may exercise its discretion in barring recovery based upon a complainant's unclean hands.[2090] Moreover, the complainant's misconduct need not be criminal or conduct that would justify legal proceedings.[2091] "Any willful act concerning the cause of action which rightfully can be said to transgress equitable standards of conduct is sufficient cause for the invocation of the maxim."[2092]

1513. The California Respondents assert that to establish unclean hands, "the defendant must demonstrate that the plaintiff's conduct is inequitable and that the conduct relates to the subject matter of its claim."[2093] The California Respondents state that even in the absence of a relationship between the unclean hands act and the relief sought, "[w]here plaintiff's action is condemned by statute, or is against public policy, and the right sought to be vindicated is inimical to public welfare, the defense of unclean hands is available even though there be no relation between the suitor's unclean hands act and the relief sought."[2094] The California Respondents note that in *Packers Trading Co.* the Seventh Circuit reversed the Commodity Futures Trading Commission's (CFTC) decision to order the respondent trading company to pay reparations to the complainant, holding that the CFTC erred by isolating the complainant's trading ban violation from the case and not

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[2088] *Keystone Driller Co. v. Gen. Excavator Co.*, 290 U.S. 240, 244 (1933) (quoting STORY'S EQUITY JURISPRUDENCE, 14th ed., § 98).

[2089] *Precision*, 324 U.S. at 814-15; *Keystone*, 290 U.S. at 245.

[2090] *Keystone*, 290 U.S. at 245-46.

[2091] *Precision*, 324 U.S. at 815.

[2092] *Id.*

[2093] *Fuddruckers, Inc. v. Doc's B.R. Others, Inc.*, 826 F.2d 837, 847 (9th Cir. 1987) (citing *CIBA-GEIGY Corp. v. Bolar Pharm.*, 747 F.2d 844, 855 (3d Cir. 1984), *cert. denied*, 471 U.S. 1137 (1985)).

[2094] *Maltz v. Sax*, 134 F.2d 2, 5 (7th Cir. 1943) (citing *Morton Salt Co. v. G. S. Suppiger Co.*, 314 U.S. 488, 490 (1942)); *see also Precision*, 324 U.S. at 815.

considering the violation in the context of the case, even though the trading ban violation was not directly associated with the transaction in controversy.[2095] The court found that when "improper conduct affects the operation and integrity of the commodities exchange in which the public has substantial interest" and that "the public is injured if the wrongdoer is permitted to profit from his wrong."[2096]

1514. The California Respondents contend that CERS acted inequitably throughout the CERS Period by (1) utilizing confidential and/or non-public information available to CERS to gain a competitive advantage in negotiations with the Respondents and (2) exercising buyer market power.

1515. The California Respondents assert that the Commission has already ruled that by placing its traders inside the ISO control room, CERS obtained an unfair competitive advantage over other market participants.[2097] The California Respondents further note that the Commission stated that "by voluntarily entering into bilateral transactions outside the ISO and PX, [CERS] made a conscious decision to forgo the refund protection that the Commission provided for purchases through the ISO and PX."[2098] The California Respondents state that despite the Commission's ruling, the California Parties continue to deny that being in the ISO control room provided CERS's traders confidential, non-public information that gave them an unfair competitive advantage.[2099]

1516. The California Respondents note that the ISO expressed reservations about CERS's presence on the control room.[2100] Specifically, the California Respondents state that Mr. Hart's notes from February 6, 2001 reveal that senior ISO officials felt that CERS's presence in the ISO control room conflicted with Commission orders that required the separation of market participants from grid operations.[2101] The California

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[2095] *Packers Trading Co. v. CFTC*, 972 F.2d 144, 149-50 (7th Cir. 1992).

[2096] *Id.* at 150.

[2097] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515 (2001).

[2098] *Id.*

[2099] *See, e.g.*, Ex. CAT-272 at 18-22; Ex. CAT-285 at 15-20.

[2100] Ex. TRC-130 at 23.

[2101] *Id.* at 30-31.

Respondents further state that CERS real-time traders inside the ISO control room knew the ISO objected to their presence because the ISO didn't want CERS "to see the full scope of everything that's going on in [the control] room."[2102]

1517. The California Respondents assert that access to the ISO control room facilitated coordination between CERS and the ISO and provided CERS with access to the ISO's "associated written materials, visual observations, and oral statements regarding the ISO's markets, systems, operations and activities."[2103] The California Respondents state that no other market participant had access to observe the "full scope" of ISO operations and the information displayed on monitors and other electronic media on control room walls. The California Respondents contend that access to this information provided a clear competitive advantage to CERS as Mr. Hart recognized at the time.[2104]

1518. The California Respondents state that Mr. McIntosh testified that "[a]ny information that was not provided to all market participants would be deemed confidential," including "details about transmission outages and derates and generation outages."[2105] The California Respondents argue that contrary to Mr. McIntosh's assertion, photographic evidence demonstrates that CERS traders on the ISO control room floor were surrounded by monitors and other electronic media providing confidential non-public information.[2106] The California Respondents assert that CERS traders sat only one desk removed from an electronic map that displayed real-time "actual" and "limit" measurements on transmission lines, such as Path 15, a critical transfer path within the ISO system,[2107] and two desks down from the electronic map that displayed the current state of each of the substations in a large part of the Western Interconnect.[2108] The California Respondents aver that this information could give the observer a real-time understanding of available transmission capacity in the Western

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[2102] Ex. TRC-139 at 2:1-3.

[2103] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515 (2001).

[2104] Ex. TRC-130 at 42.

[2105] Ex. CAT-641 at 9:5-8.

[2106] Ex. TRC-168; Tr. 2332:15-24 (McIntosh).

[2107] Tr. 2322:12-2328:23 (McIntosh).

[2108] Tr. 2333:21-23 (McIntosh).

Interconnection that would not be available to sellers or any other buyer.[2109] The California Respondents further note that the ISO control room also included monitors that could provide unit-specific outage data, EMS alarms, and transmission path monitoring information.[2110]

1519. Moreover, the California Respondents state that a CERS trader admitted that the ISO control room gave CERS traders "the full scope of everything that's going on"[2111] and that Mr. McIntosh acknowledged that access to confidential and/or non-public information would have provided CERS a competitive advantage.[2112]

1520. The California Respondents further assert that Mr. McIntosh incorrectly testified that transmission outages and unit-specific generation outages were commercially available from an entity named Genscape. The California Respondents aver that the California Parties provided no evidence that supports this contention. Furthermore, publicly available documents indicate that Genscape did not offer any product concerning Western electric facilities until the fall of 2001, after the close of the CERS Period.[2113] The California Respondents contend that the suggestion that Genscape could make

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[2109] Tr. 2333:13-20 (McIntosh).

[2110] Ex. TRC-170; Tr. 2337:3-2340:9 (McIntosh).

[2111] Ex. TRC-139 at 2:1-3.

[2112] Tr. 2350:21-2351:5 (McIntosh).

[2113] *See* ASPECTX, INC., *Case Study: Genscape Launches It [sic] New Product Offerings to The Power Market*, http://www.aspectx.com/case-study-genscape-launches-it-new-product-offerings-to-the-power-market/ (last visited Mar. 11, 2014); E-mail from David A. Doctor, Chief Executive Officer, Genscape, Inc. (Sept. 13, 2001, 06:59 PST), *available at* http://www.enron-mail.com/email/skilling-j/inbox/David_Doctor_Genscape_Inc__1.html; Cynthia Eagles, *Genscape Gets $3.55 Million in Venture Capital Funds*, AM. CITY BUS. J. (Nov. 29, 2001), http://www.bizjournals.com/louisville/stories/2001/11/26/daily32.html?page=all; PENNWELL CORP., *Genscape Inc. to Help Federal Agency Monitor Power Grid*, ELEC. POWER & LIGHT (Aug. 20, 2002), http://www.elp.com/articles/2002/08/genscape-inc-to-help-federal-agency-monitor-us-power-grid.html; PR NEWSWIRE ASSOCIATION LLC, *Genscape Enhances Online, Real-Time Power Information Service* (Jan. 24, 2002), http://www.thefreelibrary.com/Genscape+Enhances+Online,+Real-Time+Power+Information+Service.-a082089797.

available on a real-time basis the equivalent information that was displayed on a confidential basis within the ISO control room monitors defies credulity.

1521. Next, the California Respondents argue that Mr. Hart made a concerted effort over the course of the CERS Period to get access to confidential data concerning generator planned outages. For example, Mr. Hart sought this information in a meeting with the ISO's Chairman of the Board and other senior ISO officials and ISO personnel were instructed to provide all information that CERS requested.[2114] The California Respondents note that the ISO made the report highly confidential and confined its use for CERS's activities mandated under AB-1X.[2115] The California Respondents contend that Mr. Hart's explanation, that the information was provided for a group associated with the Governor's office, directly conflicts with the purpose stated in the memorandum.[2116]

1522. The California Respondents further note that Mr. Hart asserted that the unit-specific outage information does not have any useful marketing purpose.[2117] The California Respondents argue that this claim is not credible because utilities plan unit outages well in advance and the document itself demonstrates the high degree of confidentiality. The California Respondents state that the information provides, at the very least, a guide to purchasing energy in the market that no other participant possessed. With respect to Mr. Hart's claim that the information was never shared with CERS staff,[2118] the California Respondents note that the price of power at locations such as COB dropped precipitously within a few days of Mr. Hart receiving the highly confidential Unit Status Report from the ISO.[2119]

1523. Next, the California Respondents argue that CERS exercised buyer market power in two ways: (1) in the day-ahead market, CERS capped its prices and did not reveal the

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[2114] Ex. TRC-130 at 17; Tr. 670:11-673:10 (Hart). *See also* Tr. 2277:10-22 (Alaywan).

[2115] Ex. TRC-138 at 1.

[2116] *Id*.

[2117] Tr. 773:22-774:12 (Hart).

[2118] Tr. 773:21 (Hart).

[2119] *See* Ex. CAT-289 (Taylor) at 107, Figure IV-2. Mr. Hart attributes the price drop to mere coincidence. Tr. 773:21 (Hart).

full scope of its demand[2120] and (2) CERS paid higher prices and bought greater quantities outside California to drive price lower within California.[2121] The California Respondents assert that such strategies can only be successfully implemented if the buyer is exercising market power. Moreover, the California Respondents aver that these strategies directly led to higher real-time market prices at COB and NOB for which the California Parties now seek refunds.

1524. The California Respondents note that Dr. Morris detailed the strategy of paying higher prices and buying greater quantities outside of California and the California Parties have not challenged Dr. Morris's conclusion on this issue.[2122] The California Respondents further state that trader tapes between Sempra and CERS confirm that CERS was willfully choosing to purchase energy at COB for higher prices than the price of available at NP15.[2123] The trader tape further notes that the Sempra trader was considering moving in-state energy, for which Sempra's trader was seeking $200/MWh at NP 15, "out of the ISO and sell[ing] it back to them [at COB] … [for] $400."[2124] The California Respondents note that this demonstrates that CERS's strategy incentivized sellers to export energy out of the ISO and sell it back to CERS at ISO interfaces, which the California Parties now claim is a False Export.

1525. Next, the California Respondents assert that there is documentary evidence of CERS's strategy of capping the price paid for day-ahead purchases. The California Respondents cite a January 20, 2001 CERS document, which provides pricing guidelines to determine the reasonableness of offers to sell.[2125] Additionally, a February 3, 2001 CERS memo states that the original pricing guidelines should continue to be used as a

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[2120] *See* Ex. TRC-62 at 1.

[2121] Ex. TRC-1 at 18:12-14 (citing Ex. TRC-12).

[2122] Ex. TRC-1 at 18:14-15.

[2123] Ex. TRC-143 at 5:10-14.

[2124] *Id.* at 7:9-12.

[2125] Ex. TRC-61 at 1; *see also* Ex. TRC-128. The guidelines originally suggested that the price cap would be at $300/MWh but Mr. Hart acknowledged that he lowered this number to $250/MWh during the approval process. *See* Tr. 579:2-7 (Hart).

reference and purchases should be made at or below pricing guidelines.[2126] The California Respondents further note that the February 3, 2001 memo sets a price cap of ten percent above the day-ahead price for day-of purchases at COB or NOB, but allows CERS to pay the day-of market price if a system emergency is declared.[2127]

1526. The California Respondents state that the effect of CERS's strategy was that CERS did not reflect its expected demand in the day-ahead market, leading to insufficient supplies and ISO declared emergencies.[2128] Additionally, by not revealing its true demand in day-ahead transactions, CERS was able to lower the day-ahead price relative to the day-of price.[2129] The California Respondents note that Mr. Taylor acknowledged that shifting demand to day-of purchases would raise day-of prices.[2130]

1527. The California Respondents contend that without the price cap, CERS would have revealed its true demand to the day-ahead market.[2131] However, because CERS instituted a day-ahead cap, it only covered fifty-seven percent of the net short day-ahead on average.[2132] The California Respondents state that this allowed CERS to purchase day-ahead power at an average price of $237.98/MWh and day-of power at an average price $387.54/MWh of in February 2001.[2133] The California Respondents aver that by depressing prices in the day-ahead market, CERS may have saved as much as $800

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[2126] The memo states that the guidelines are "especially important when considering purchases from in state base load generation." Ex. TRC-12 at 1; Ex. CAT-060 at 2.

[2127] Ex. TRC-12 at 1; Ex. CAT-060 at 2.

[2128] Ex. TRC-1 at 119:6-9.

[2129] *Id.* at 119:9–11.

[2130] *See* Ex. TRC-4 at 87.

[2131] *See* Ex. S-13 at 41:7-9; *see also* Ex. TRC-1 at 122:1-4.

[2132] Ex. TRC-1 at 120:6-10; *see also* Tr. 3809:9-17 (Morris)

[2133] Ex. TRC-1 at 120:5-10.

million.[2134] The California Respondents state that Mr. Hart's March 21, 2001 notes confirm that CERS successfully implemented this day-ahead pricing strategy.[2135]

1528. Furthermore, the California Respondents argue that another factor leading CERS to purchase insufficient amounts of day-ahead energy was the IOUs' net short forecasts.[2136] The California Respondents assert that the IOUs' forecasts were notoriously inaccurate, often under-forecasting load by thousands of megawatts on an hourly basis,[2137] and CERS never went back to check the accuracy of the forecasts.[2138] The California Respondents further note that traders observed that whenever there was a large variance between the IOUs' day-ahead forecast and actual load, the price for energy in the day-of market would rapidly increase.[2139] In another trader tape between a CERS real-time trader and a CERS day-ahead trader, the CERS day-ahead trader acknowledged that CERS was "skewing" the day-of pricing upward through its procurement strategy by choosing to not procure 2,000 to 3,000 MWh on a day-ahead basis.[2140]

1529. Lastly, the California Respondents contend that this inequitable conduct goes directly to the transactions for which the California Parties now seek refunds. First, the California Respondents argue that CERS utilized confidential and/or non-public information to gain an unfair competitive advantage in entering into its bilateral contracts with the Respondents, directly affecting the outcome of negotiations. Second, the California Respondents aver that CERS's exercise of buyer market power raised prices in the Pacific Northwest for day-of transactions, the transactions at issue in this proceeding.

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[2134] *Id.* at 121:4–7.

[2135] Ex. TRC-130 at 48 ("[t]he pricing strategy from yesterday worked extremely well. The hour ahead was a little bit expensive but not horribly worse than normal. The day ahead for tomorrow came back down in the 190 to 220 range. Much better."). *See also* Ex. TRC-144 (CERS trader admitting that CERS "didn't go hunting for too much power" day-ahead).

[2136] Ms. Lee testified that CERS based day-ahead energy procurement on the forecasts that the IOUs provided to CERS. Tr. 826:1-14 (Lee).

[2137] Ex. TRC-143 at 2:1-24.

[2138] Tr. 826:8-11 (Lee).

[2139] Ex. TRC-143 at 3:23-4:1.

[2140] Ex. TRC-145 at 2:19-23.

The California Respondents aver that permitting the California Parties to recover under these circumstances would allow the wrongdoer to enjoy the fruits of his transgression.

### 3. TransCanada Initial Brief

#### (a) The *Mobile-Sierra* Standard and Evidence of Excessive Burden on Consumers

1530. TransCanada states that the California Parties may overcome the *Mobile-Sierra* presumption if they demonstrate "that the contract rate imposes an excessive burden on consumers or seriously harms the public interest."[2141] TransCanada asserts that the Commission and the courts have made clear that the evidence required to make such a showing must be on a contract-specific basis.[2142] Furthermore, the Supreme Court has stated that to overcome the *Mobile-Sierra* presumption, the harm must be "more than a small dent in the consumer's pocket."[2143]

1531. TransCanada asserts that the California Parties failed to present evidence of excessive burden on consumers or serious harm to the public interest arising from any specific contract between CERS and TransCanada. TransCanada notes that Professor Berck admitted that his analysis did not look at any individual seller's sales to CERS, and that he was making no allegations with regard to any specific seller or with regard to any specific contract.[2144]

1532. Next, TransCanada contends that its sales to CERS were actually beneficial to CERS and California consumers. TransCanada avers that the prices of its sales to CERS were below the weighted average price CERS paid other sellers.[2145] Specifically, TransCanada states that its prices were typically below the average price that CERS paid at COB and was the lowest price CERS paid approximately forty-nine percent of the

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[2141] Order Granting Interlocutory Appeal at P 12; *see also* Order on Rehearing at PP 13-14, 30.

[2142] Order on Rehearing at P 30; Order Granting Interlocutory Appeal at PP 12-14.

[2143] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 511, n.6 (2008).

[2144] Tr. 1591:25-1592:7 (Berck).

[2145] Tr. 2502:21-25 (Taylor); *see also* Ex. TRC-194; Ex. TRC-195.

time.[2146] Furthermore, TransCanada notes that it was under no obligation to sell any power to CERS.[2147]

1533. Lastly, TransCanada contends that even if all its sales are aggregated, the sales did not impose and "excessive burden" on consumers. TransCanada states that CERS's acquisition costs were only one half of one percent higher under the actual contracts negotiated with TransCanada than they would have been had the transactions taken place at the MMCP level.[2148] TransCanada notes that the actual rate impact is approximately one one-hundredth of a percent (i.e., 0.01 percent).[2149]

**(b) The California Parties' Claims are Procedurally Infirm**

1534. TransCanada first provides a brief summary of the California Parties' claim history in this proceeding. TransCanada states that the California Parties never filed a complaint in this case alleging wrongdoing on the part of the Respondents; instead, they chose to rely on the August 2000 complaint of Puget Sound Energy, Inc. TransCanada notes that this is prior to any of the alleged fraud, duress, or bad faith on TransCanada's part purportedly occurred.

1535. TransCanada states that the Commission did not initial set the Puget Sound complaint for hearing;[2150] however, the Commission subsequently ordered an evidentiary hearing before an Administrative Law Judge.[2151] TransCanada asserts that the first ALJ who heard this case found that the California Parties "request for refunds … violates the Commission's longstanding policy prohibiting intervenors from expanding complaints initiated by others."[2152] Thus, the ALJ held that "[t]o the extent parties wish to prosecute

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[2146] Ex. TRC-1 at 8:15-19.

[2147] *See* Tr. 2525:8-11 (Taylor); Ex. TRC-1 at 164:12-13.

[2148] *See* Ex. TRC-1 at 165:5-10.

[2149] Ex. TRC-1 at 165:16-17.

[2150] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at P 10 (2003). The original *Puget Sound* complaint encompassed a request for prospective relief in the form of rate caps. *Id*. P 1.

[2151] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120 at 61,499-500 (2001).

[2152] *Puget Sound Energy, Inc.*, 96 FERC ¶ 63,044, at 65,376, 65,383-84 (2001).

claims beyond the scope of a complaint, such parties must initiate a new Section 206 proceeding."[2153] Following the ALJ's order, TransCanada notes that the Commission also acknowledged that "this case could be dismissed solely on procedural grounds,"[2154] because the California Parties had missed the timeframe for filing a Section 206 complaint that would capture the relevant period with its refund effective date.[2155] Nonetheless, the Commission did not dismiss the case.

1536. TransCanada argues that the current procedural posture of this case is legally flawed because the current proceeding does not involve hearing a Section 206 complaint raised by a complainant, or by the Commission *sua sponte*. TransCanada further notes that the Commission did not set a refund effective date in the Order Dismissing Puget Sound Complaint; rather, it identified two dates that *could have* been used for the effective date (i.e., the earliest and latest refund effective dates).[2156] Therefore, TransCanada contends that the proceeding has gone forward based on an attempt, contrary to the observation of the ALJ who initially heard the case, to alleviate the California Parties' failure to file a timely complaint of their own.

1537. TransCanada acknowledges that the Ninth Circuit ultimately ruled that the CERS claims fell within the scope of this proceeding. However, TransCanada argues that had the California Parties filed their own complaint in a timely fashion, Respondents would have been on notice within the time frame set by the FPA of the precise nature of the claims against them. TransCanada states that it was only with the filing of their Direct Testimony,[2157] which occurred more than ten years after the initial complaint was filed, that the California Parties raised a number of the legal claims of misconduct now pending against TransCanada.[2158]

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[2153] *Id.*

[2154] *Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348 at P 25.

[2155] *Id.*

[2156] *Id.* P 30 n.25.

[2157] *See* California Parties September 21, 2012 Direct Testimony.

[2158] TransCanada avers that even the claims asserted in the California Parties' Direct Testimony appear to be a moving target, noting that Mr. Taylor testified that there are unidentified claims "exogenous" to the contracts that the California Parties are raising against TransCanada. Tr. 2438:9-2439:10 (Taylor).

1538. TransCanada states that a party submitting a complaint must "[c]learly identify the action or inaction which is alleged to violate applicable statutory standards or regulatory requirements;" and "[e]xplain how the action or inaction violates applicable statutory standards or regulatory requirements."[2159] TransCanada contends that the California Parties' Direct Testimony, Preliminary Disclosure of Claims,[2160] the Final Joint Statement of Issues, and the Pre-Hearing Brief do not meet this standard, and therefore, violate TransCanada's Due Process rights.

**(c) Statute of Limitations**

1539. Next, TransCanada argues that the California Parties claims are barred by the federal and Utah statutes of limitations. TransCanada avers that the California Parties' claims against TransCanada are being asserted for the first time more than a decade after the actions giving rise to these claims occurred.

1540. TransCanada states that federal and state statutes of limitations implement the principles of repose, which include preventing of the use of stale evidence, providing and protecting settled expectations, reducing uncertainty, and reducing the costs of measures to guard against the risks associated with untimely claims.[2161] TransCanada states that repose is also intended to bring litigation to an end so that the commercial world can base their transactions on established rules.[2162] Additionally, time limits encourage claimants to sharpen claims and diligently pursue litigation at the outset, rather than develop new claims and theories over a prolonged period.[2163]

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[2159] 18 C.F.R. §§ 385.206(b)(1)-(2) (2013).

[2160] California Parties' August 23, 2012 Preliminary Disclosure of Claims. TransCanada asserts that this document only contained a general statement alleging that all Respondents "engaged in unlawful market activity, market manipulation, fraud, duress, price discrimination, unfairness, and/or bad faith" and also alleged that the *Mobile-Sierra* presumption should not apply or that it is "overcome because the contract rate is against the public interest."

[2161] Tyler T. Ochoa & Andrew J. Wistrich, *The Puzzling Purposes of Statutes of Limitation*, 28 PAC. L.J. 453, 458, 460 (1997).

[2162] *Id*. at 466.

[2163] *Id*. at 457.

1541. TransCanada asserts that the Commission has acknowledged that it cannot allow litigation before it to be dragged on indefinitely in the context of a party seeking rehearing of an order denying rehearing.[2164] TransCanada avers that the same principle applies in this proceeding because allowing the California Parties to take yet another bite at the apple based upon new allegations and theories of wrongdoing related to events that occurred twelve years ago should not be tolerated.

1542. With respect to the California Parties' claims of duress, fraud, bad faith, and undue price discrimination, TransCanada argues that those claims are barred by the Utah statute of limitations.[2165] TransCanada states that the Utah statute requires that claims of duress, bad faith, and undue price discrimination be brought, if at all, no later than four years after the cause of action has accrued.[2166] Thus, the California Parties were required to bring claims of duress, fraud, bad faith, and undue price discrimination by June 20, 2005 at the latest. TransCanada states that these allegations were not made by the California Parties until September 21, 2012,[2167] and therefore, are barred by the Utah statute of limitations.

1543. Next, TransCanada argues the California Parties claims under Issue 1(B) are barred by the federal statute of limitations.[2168] TransCanada states that in the Brown Order, the Commission noted that by imposing "market-wide relief in the context of short-term bilateral sales to CERS irrespective of an individual seller's wrongdoing[,] …

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[2164] *California ex rel. Brown v. Powerex Corp.*, 140 FERC ¶ 61,115, at P 12 (2012) ("every response by the Commission to a party's arguments would allow yet another opportunity for rehearing unless presumably that response were word-for-word identical to what the Commission earlier said.").

[2165] The WSPP Agreement includes a Utah choice of law provision. *See* Ex. CAT-124 at 48 (WSPP Agreement § 24).

[2166] UTAH CODE ANN. § 70A-2-725(1); *see also California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at PP 104, n.153, 108 (2011), *reh'g denied*, 139 FERC ¶ 61,210 (2012). For claims of fraud, the statute of limitations under Utah law is only three years. UTAH CODE ANN. § 78B-2-305(3).

[2167] This is the date that the California Parties filed their Direct Testimony. TransCanada asserts that this date constitutes the earliest possible date that these claims of fraud, duress, bad faith, and undue price discrimination were made.

[2168] *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at PP 97-111 (2011), *reh'g denied*, 139 FERC ¶ 61,210 (2012)

the results could be punitive and confiscatory."[2169] TransCanada asserts that the Commission reached this conclusion because an order resetting sales prices would apply to sellers to CERS without regard to whether an individual seller had violated its tariff or engaged in any other wrongdoing.[2170] TransCanada asserts that the Commission rejected, based upon a federal statute that "sets a five-year limit for 'an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise,' " the California Attorney General's request to reset market prices.[2171]

1544. TransCanada states that the California Attorney General, joined by the other California Parties, makes the same argument in Dr. Berry's testimony that the Commission previously rejected. TransCanada argues that the California Parties are relying on a general claim that attempts to blur the distinctions between the Respondents' contracts with CERS and CERS's sales to the ISO to support their contention that the Respondents-CERS contract prices should be reformed to the MMCP levels,[2172] without regard to the culpability of individual sellers. TransCanada asserts that this claim is barred by *res judicata*. TransCanada further avers that even if the California Parties were able to differentiate their current claim from that raised in *Brown*, the claim would be barred for the same reason the Commission refused a market-wide remedy in *Brown* – a grant of the claim would amount to a penalty, making the federal five-year statute of limitations under 28 U.S.C. § 2462 applicable.[2173]

### (d) Equitable Doctrine of Laches

1545. Next, TransCanada argues that the equitable doctrine of laches serves as an additional bar to the claims made by the California Parties. TransCanada states that the

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[2169] *Id. P* 100. In both the Order on Remand and the Order on Rehearing, the Commission reaffirmed the impropriety of imposing a refund without identifying individual wrongdoing of the sellers. *See* Order on Remand at P 2; Order on Rehearing at P 30. *See also Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 553-54 (2008).

[2170] *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 101 (2011).

[2171] *Id*. P 99 (quoting 28 U.S.C. § 2462 (2006)).

[2172] Ex. CAT-536 at 6:1-7:18; Tr. 1630:8-22 (Berry).

[2173] *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 104 (2011).

doctrine of laches is "designed to prevent unfairness to a party caused by a second party's unexcused or unreasonable delay in asserting a claim."[2174] Thus, the doctrine applies when a party is able to show that the delay in asserting rights caused undue prejudice to the party against whom the claims are brought.[2175] As stated above, TransCanada notes that the claims in this case are based on actions or inactions that took place during the CERS Period, January 17, 2001 through June 20, 2001.

1546. TransCanada further argues that the procedural history in this proceeding should not make the doctrine of laches inapplicable. TransCanada states that this proceeding *did not* arise from a complaint filed by the California Parties. TransCanada notes that both the Commission in 2001 and the Ninth Circuit in 2006 instructed the California Parties to file a complaint, stating "if DWR or another party believes that any of its contracts are unjust or unreasonable, it may file a complaint under FPA Section 206 …."[2176] Thus, the California Parties had guidance to assert their claims as early as 2001.

1547. TransCanada notes that the California Attorney General did file a complaint alleging wrongdoing in 2009,[2177] and could have made the claims of duress, fraud, bad faith, and undue price discrimination that are now being asserted. TransCanada asserts that the California Attorney General did not do so, notwithstanding that those claims arise from the same factual circumstances at issue in his 2009 complaint. As noted above, the Commission held that the claims raised in the 2009 complaint were barred by this federal statute of limitations.[2178] TransCanada avers that it would be inequitable and contradictory to allow these new claims to go forward in this proceeding when it is evident that the California Parties failed to make them for all these years, despite having the opportunity and directive to do so multiple times.

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[2174] *Nw. Pipeline Co.*, 56 FERC ¶ 61,231, at 61,890 (1991) (citing *EEOC v. Dresser Indus., Inc.*, 668 F.2d 1199 (11th Cir. 1982)).

[2175] *Id*. at 61,890 (citing *Envtl. Def. Fund, Inc. v. Alexander*, 614 F.2d 474 (5th Cir. 1980)).

[2176] *Pub. Util. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1062 (9th Cir. 2006) (quoting the Commission's statement in *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120 (2001)).

[2177] California Attorney General, Complaint, Docket No. EL09-56-000 (filed May 22, 2009).

[2178] *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 99 (2011).

1548. Moreover, TransCanada contends that the California Parties also should not be rewarded for their strategy of modifying the bases for their claims depending on the scope of a proceeding. For example, TransCanada asserts that the California Parties have reversed their position regarding whether the sales to CERS in the Pacific Northwest market were different than transactions in the California market.[2179]

1549. Lastly, TransCanada notes that the Ninth Circuit has stated that "[u]nlike the Cal-ISO OOM … transactions that we have concluded were properly considered in the Refund Proceedings, the CERS transactions occurred in a market that was not directly influenced by the market manipulations in the Cal-ISO and CalPX spot markets."[2180] TransCanada states that in response to this finding, the California Attorney General filed his complaint in the *Brown* proceeding, arguing that the transactions were the same. However, the Commission, relying on the Ninth Circuit's statement, continued to treat the CAISO purchases as distinct and separate from CERS's purchases.[2181] TransCanada argues that rather than provide evidence that the circumstances in the California markets had an effect on the Pacific Northwest market, the California Parties ignored both their previous assertions and Commission and court precedent, and now assert that "CERS purchased in the same market that the Commission has already found to be dysfunctional."[2182] TransCanada contends that the California Parties' willingness to revise their allegations to accommodate their latest legal theories serves as a perfect example of why rejection of their claims based on the equitable principle of laches is appropriate here.

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[2179] In this case in 2001, the California Attorney General and the California Public Utilities Commission stated that there were differences between the California and the Pacific Northwest markets. California *ex rel.* Bill Lockyer, the California Electric Oversight Board, and the Public Utilities Commission of California, Brief, Docket Nos. EL01-10-000, EL01-10-001, at 3, 8 (filed Sept. 17, 2001) ("CERS' bilateral transactions in the PNW *are not purchases through the California ISO or PX markets* … such purchases are the functional equivalent of other purchases made in the PNW"). However, in this phase of the proceeding, the California Parties have alleged that bilateral sales to CERS were in most respects identical to the previous spot market sales made in the California ISO and CalPX. Tr. 1621:23-1623:7 (Berry).

[2180] *Pub. Util. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1063 (9th Cir. 2006).

[2181] *California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at PP 32-34 (2011).

[2182] Ex. CAT-536 at 9:2-3.

### 4. Commission Trial Staff Initial Brief

1550. Trial Staff states that the *Morgan Stanley* Court held that a contract rate does not impose an excessive burden simply because it is above marginal cost.[2183] Instead, the Commission can set aside a contract rate only in the event of "unequivocal public necessity" or "extraordinary circumstances."[2184]

1551. Trial Staff notes that in its Order Granting Interlocutory Appeal, the Commission found that in attempting to overcome the *Mobile-Sierra* presumption, evidence may be considered "that specific contract rates imposed an excessive burden on consumers."[2185] Furthermore, in the Order on Rehearing, the Commission rejected the California Parties' argument that "the Commission should permit evidence that the rates, as a whole, imposed an undue burden on the public."[2186] Rather, the Commission stated that it "must evaluate each seller's conduct in relation to specific contract negotiations and/or whether the contract imposes an excessive burden on consumers."[2187] The Commission further stated that the "[California] Parties' claims of uniformly higher prices amount to little more than a variation on claims of general market dysfunction, which have been previously rejected by the Supreme Court as a basis for overcoming *Mobile-Sierra*."[2188]

1552. Trial Staff argues that the California Parties failed to provide evidence of an excessive burden or serious harm to the public interest and failed to tie such burden or harm (if any) to the contract rates at issue in this proceeding.

1553. First, Trial Staff states that at hearing, Mr. Taylor testified that "where there is manipulative activity that might affect market prices generally," with no evidence of a price impact on a particular contract, he would "make a 1(B) finding."[2189] Trial Staff

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[2183] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[2184] *Id.*

[2185] Order Granting Interlocutory Appeal at P 15.

[2186] Order on Rehearing at P 28.

[2187] *Id.* P 30.

[2188] *Id.*

[2189] Tr. 2884:6-2885:17 (Taylor); *see also* Ex. CAT-665.

contends that Mr. Taylor confounds the Joint Statement of Issues and disregards the Commission's orders by using allegations of duress, fraud or bad faith, undue price discrimination, False Export, and selling non-firm energy as firm to support claims under Issue 1(B). Trial Staff avers that the California Parties are attempting to avoid the Commission's requirement to link alleged unlawful activity to specific contracts.[2190] Trial Staff further asserts that the California Parties' use of the unlawful activity, without a price impact on a particular contract, under Issue 1(B) is directly contrary to the Commission's directive that "general allegations of market dysfunction in the Pacific Northwest are an insufficient basis for overcoming the *Mobile-Sierra* presumption or finding that it is inapplicable."[2191]

1554. Second, Trial Staff contends that Professor Berck's analysis does not provide evidence of excessive burden or serious harm to the public interest. Trial Staff states that Professor Berck's analysis measures a theoretical harm that may have occurred under a hypothetical scenario. Trial Staff avers that even if the harm actually occurred, the California Parties failed to tie the harm to the specific contract rates at issue in this proceeding, as required by the Commission.[2192]

1555. Trial Staff states that Professor Berck calculated the decrease in real state personal income and increase in unemployment that would have occurred had the State of California immediately passed through to consumers the amount of alleged overcharges by Respondents in this case.[2193] However, Trial Staff notes that California did not immediately pass through the full costs of electricity during the CERS Period, electing instead to issue bonds to finance the costs.[2194] Trial Staff asserts that Professor Berck failed to measure how the actual bond issuance affected real state personal income and unemployment.[2195] Furthermore, Trial Staff notes that Professor Berck assumed various levels of harm, but did not determine if that harm was attributable to any of the Respondents.[2196] Thus, Trial Staff argues that the California Parties provide no evidence

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[2190] Order on Remand at P 21.

[2191] *Id*.

[2192] Order on Rehearing at PP 28, 30.

[2193] Ex. CAT-267 at 3:20-4:2; Tr. 1579:8-15 (Berck).

[2194] Ex. CAT-37 at 11:17-12:4

[2195] Tr. 1580:9-18 (Berck).

[2196] Tr. 1593:1-6 (Berck).

to explain why contract abrogation is an "unequivocal public necessity"[2197] or whether a particular contract rate imposes an excessive burden or seriously harms the public interest.[2198]

1556. Trial Staff further contends that even assuming the California Parties' $1.05 billion in alleged overcharges, such overcharges did not cause and are currently not causing an excessive burden on California consumers.[2199] Trial Staff asserts that this equates to under $70 per California residential customer, or between $0.23 and $0.27 per month over 20 years.[2200] Trial Staff further notes that $1.05 billion includes overcharges from Powerex, who has settled with the California Parties. Trial Staff states that only $266.88 million is attributable to the Avista Entities, TransAlta, TransCanada, and Coral,[2201] which results in a monthly charge of only $0.06 to $0.07 per residential customer.

1557. Trial Staff avers that Professor Berck's claim that payments cannot be rendered reasonable by stretching them out over time ignores Ms. Radel's finding that if the costs had been passed through *immediately*, the average monthly impact per ratepayer would have been approximately $14.[2202] Removing the overcharges attributable to Powerex lowers the monthly payment to just $3.56 per residential customer. Trial Staff states that the California Parties never address how this charge creates an undue burden on consumers or seriously harms the public interest.[2203]

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[2197] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[2198] Order Granting Interlocutory Appeal at P 1.

[2199] Ex. S-15 at 21:17-22:8; Ex. S-25 at 3:4-9.

[2200] Ex. S-15 at 21:21-22:2; Ex. S-25 at 3:4-9. Ms. Radel also calculated an average monthly surcharge between $2.51 and $2.90 for California residential customers based on the full principal amount of the bond ($11.3 billion), which was issued to cover all spot market purchases by CERS, including charges by entities not a party to this case and charges that California does not dispute. Ex. S-25 at 2:8-3:3; Ex. S-26.

[2201] Ex. SNA-34A: Tr. 1585:24-1586:2 (Berck).

[2202] Ex. S-15 at 22:2-4.

[2203] Tr. 1595:16-17 (Berck).

1558. With respect to Professor Berck's assertion that the number of people contributing to the costs should not factor into the calculation of burden,[2204] Trial Staff asserts that ignoring the number of people contributing to a cost defies common sense. Trial Staff notes that CERS was responsible for purchasing energy for over 10 million residential customers.[2205] Thus, the amount of power purchased and the costs incurred were a direct function of the demand placed on the system by those 10 million customers. Moreover, Trial Staff argues that Professor Berck contradicted his own argument when he stated that the "California economy is large, and a million dollars [in overcharges] is too small to discuss" given the size of the California economy.[2206] Trial Staff contends that if burden is a product of the size of the economy, burden is also a product of the number of people contributing to the costs incurred.

1559. Third, Trial Staff asserts that many other factors, such as severe drought conditions, decreased output of hydroelectric generators, high gas prices, and increased demand, could have contributed to the high prices during the CERS Period.[2207] Trial Staff notes that Professor Berck made no attempt to isolate the impacts of these market fundamentals when performing his calculations.[2208]

1560. Fourth, Trial contends that Commissioner Florio's testimony describes events that occurred outside the CERS Period and cannot be evidence of excessive burden caused by the sales to CERS at issue in this proceeding.

### 5. <u>The California Parties Reply Brief</u>

1561. The California Parties argue that Respondents and Trial Staff conflate the standard for avoiding the *Mobile-Sierra* presumption, which requires a showing of bad behavior at the contract formation stage or market manipulation,[2209] with the standard for

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[2204] Tr. 1612:9-15 (Berck).

[2205] *See* Ex. S-26.

[2206] Tr. 1608:16-18, 1613:20-24 (Berck).

[2207] *See, e.g.*, Ex. PNR-1 at 33:6-36:15; Ex. SCL-1 at 11:19-22; Ex. SCL-10 at 10:218-221; Ex. S-1 at 20:10-13.

[2208] Tr. 1602:19-22 (Berck).

[2209] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 554 (2008).

overcoming the *Mobile-Sierra* presumption, which requires only a showing that "any customer" of the purchaser would be burdened.[2210]

### (a) The *Mobile Sierra* Standard

1562. The California Parties contend that Respondents and Trial Staff misrepresent the current state of the law concerning the *Mobile-Sierra* doctrine and this proceeding. The California Parties assert that Respondents and Trial Staff wrongly conclude that the *Mobile-Sierra* presumption may only be overcome on what they call a "contract-specific" basis. The California Parties aver that the D.C. Circuit specifically rejected this argument, and the Commission has relied upon the court's reasoning to support recent contract modification in response to Order No. 1000.[2211]

1563. The California Parties state that in *TAPS*, the D.C. Circuit rejected the argument that it should overturn the Commission's modification of contracts because the Commission had made generic, rather than particularized, case-by-case, public interest findings.[2212] Specifically, the court stated that "when intervening circumstances affect an entire class of contracts in an identical manner, we find nothing in the *Mobile-Sierra* doctrine to prohibit FERC from responding with a public interest finding applicable to all contracts of that class."[2213] Additionally, in *Arizona Corp. Commission v. FERC*, the court explained that the "*Mobile-Sierra* doctrine permits generalized findings of public interest when intervening circumstances affect a class of contracts in the same manner."[2214] The California Parties also note that the Commission relied on this reasoning to justify its modification of a contract pursuant to Order No. 1000.[2215] The California Parties assert that in this proceeding, they have presented overwhelming

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[2210] *Id*. at 548-49.

[2211] *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000, FERC Stats. & Regs. ¶ 31,323 (2011) (subsequent history omitted).

[2212] *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 709-11 (D.C. Cir. 2000), *aff'd*, *New York v. FERC*, 535 U.S. 1 (2002).

[2213] *Id.* at 710. *See also Texaco Inc. v. FERC*, 148 F.3d 1091, 1097 (D.C. Cir. 1998); *ISO New England*, 143 FERC ¶ 61,150, at PP 173-75 (2013).

[2214] *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 955-56 (D.C. Cir. 2005).

[2215] *ISO New England*, 143 FERC ¶ 61,150, at P 181 (2013) (quoting *TAPS*, 225 F.3d at 712).

evidence that the contracts were generically influenced by conditions that resulted in rates that harmed and continue to harm the public.

1564. Next, the California Parties argue that Respondents contention that the Commission "previously ruled that a market-wide remedy would not be appropriate in this case" is irrelevant. The California Parties state that the question of remedies is premature because it was specifically reserved for Phase II.[2216] Additionally, the California Parties aver that they do not seek a market-wide remedy. Rather, the California Parties state that they seek modification only of the Respondent contracts that harmed the public interest, not the contracts of any other entities that may have sold energy in the Pacific Northwest markets. Lastly, the California Parties contend that the Commission has not barred a public interest finding applicable to all contracts at issue in this proceeding, given the California Parties' showings that the energy crisis affected the entire class of contracts in an identical manner and caused aggregated harm to the public.

1565. The California Parties also argue that Respondents misrepresent the *Mobile-Sierra* doctrine. The California Parties note that *Mobile-Sierra* has provided the Commission with all the tools necessary to protect the public interest. Thus, in *Mobile*, the Supreme Court explained that its holding does not impair the Commission's power to modify contracts when necessary in the public interest.[2217]

1566. The California Parties further state that the Court held that "the *Mobile-Sierra* doctrine does not overlook third-party interests; it is framed with a view to their protection."[2218] Similarly, the First Circuit stated that "most attractive case" for contract reformation pursuant to the *Mobile-Sierra* doctrine "is where the protection is intended to safeguard the interests of third parties."[2219]

1567. The California Parties argue that despite the precedent discussed above, Respondents wrongly rely on isolated statements in *Morgan Stanley* that the Commission

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[2216] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085, at PP 1, 15-16 (Sept. 13, 2012) (Order Confirming Rulings from the Sept. 6, 2012 Prehearing Conference).

[2217] *United Gas Pipe Line Co. v. Mobile Gas Services Corp.*, 350 U.S. 332, 344 (1956). *See also FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956).

[2218] *NRG Power Mktg., LLC v. Me. Pub. Utils. Comm'n*, 558 U.S. 165, 175 (2010).

[2219] *Ne. Utils. Serv. Co. v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993) (internal citation omitted). *See also ISO New England*, 143 FERC ¶ 61,150, at P 194 (2013).

may modify contracts in "extraordinary circumstances," or cases of "unequivocal public necessity," or where there is "serious[] harm" to consumers. The California Parties assert that even under these standards, contract modification is appropriate in this proceeding given the circumstances of the Western Energy Crisis.[2220]

1568. With respect to Respondents' contention that the Court has followed a consistent path of limiting the Commission's authority to abrogate freely negotiated agreements, the California Parties argue that the case cited by Respondents affirmed the Commission's modification of contracts in order to preserve the public interest.[2221] The California Parties also aver that Respondents' reliance on the Court's statement that "the principal regulatory responsibility [is] not to relieve a contracting party of an unreasonable rate"[2222] is irrelevant to this proceeding because the California Parties are not asking the Commission to relieve the "contracting party" – CERS – of an unreasonable rate. Rather, the California Parties seek refunds that will flow to California's consumers.[2223]

1569. In addition, the California Parties argue that Respondents' reliance on the D.C. Circuit's characterization of the burden imposed by the *Mobile-Sierra* doctrine as "practically insurmountable" and "almost insurmountable"[2224] is misguided. The California Parties note that the First Circuit rejected these statements, explaining that "[i]t should be noted that neither *Mobile* nor *Sierra* stated or intimated that the 'public interest' doctrine was 'practically insurmountable.'"[2225] Moreover, the California Parties

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[2220] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 553 (2008) (stating that under the circumstances, it was "entirely possible" that the rates charged were so high that they imposed an excessive burden on consumers).

[2221] *See Permian Basin Area Rate Cases*, 390 U.S. 747, 783-84 (1968).

[2222] *Verizon Commc'ns, Inc. v. FCC*, 535 U.S. 467, 479 (2002).

[2223] *See, e.g.*, Ex. CAT-037 at 17.

[2224] *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983); *Kansas Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983).

[2225] *Ne. Utils. Serv. Co. v. FERC*, 993 F.2d 937, 961 (1st Cir. 1993).

note that in *Morgan Stanley*, the Court never described the public interest standard as "practically insurmountable" or "almost insurmountable."[2226]

1570. The California Parties also assert that Respondents mischaracterize the Supreme Court's decision in *Morgan Stanley* when implying that the Court held that there is no zone of reasonableness for contracts involving market-based rates. The California Parties state that the FPA requires all rates to be just, reasonable, and non-discriminatory.[2227] The California Parties aver that *Morgan Stanley* merely rejected the Ninth Circuit's overarching finding that the *Mobile-Sierra* presumption could be overcome simply upon a finding that market-based rates exceed marginal costs.[2228] The Court did not hold that there was no limit to the amount that sellers could charge. The California Parties contend that they proved serious harm to the public and did not rely on the mere exceeding of marginal cost.[2229]

### (b) Respondents Cite Irrelevant Factors

1571. The California Parties argue that Respondents list a number of factors that are either irrelevant to whether contracts that burden consumers may be modified or premature because they address remedies. First, the California Parties assert that the fact that Respondents had authorization to sell at market-based rates is irrelevant. The California Parties note that in both *Mobile* and *Sierra*, the Court made clear that the Commission retained the authority to modify contracts that harm the public interest.[2230] The California Parties also state that Commission-authorization has never immunized a contract from public interest modification.[2231]

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[2226] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527 (2008).

[2227] *See* 16 U.S.C. §§ 824d, 824e(a) (2012).

[2228] *Morgan Stanley*, 554 U.S. at 549-50, 624.

[2229] *See, e.g.*, Ex. CAT-001; Ex. CAT-267.

[2230] *United Gas Pipe Line Co. v. Mobile Gas Services Corp.*, 350 U.S. 332, 335 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956).

[2231] *See Miss. Indus. v. FERC*, 808 F.2d 1525, 1529, *different holding vacated in part on other grounds per curiam*, 822 F.2d 1104 (D.C. Cir. 1987); *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 667 (D.C. Cir. 2000).

1572. Second, the California Parties aver that Respondents' reliance on the volatility of the energy market is irrelevant. The California Parties note that market volatility typically describes day-to-day fluctuations, but the CERS Period is characterized by high prices over a sustained period.[2232] The California Parties also note that they do not rely solely on high prices and market volatility. Rather, the California Parties state that they presented evidence of the harm to the public caused by the Energy Crisis.

1573. Third, the California Parties contend that Respondents' assertions regarding their lack of market power are irrelevant to whether contracts harmed the public. The California Parties note that in *Texaco Inc*., the D.C. Circuit approved Commission modification of a contract even though there was no indication that the pipeline committed any bad act.[2233] The California Parties state that all that was necessary was the Commission's finding that, absent contract modification, the public interest would be harmed.[2234] With respect to Respondents' claim that they were not obligated to sell to CERS, the California Parties state that once the Respondent did in fact make the sale, that contract was subject to the Commission's jurisdiction and may be modified under the *Mobile-Sierra* doctrine.

1574. Fourth, the California Parties assert that Respondents' claim that the California Parties seek a market-wide remedy is both irrelevant to Issue 1(B) and premature. The California Parties note that it only seeks modification of specific contracts with Respondents. The contracts of all other market participants will remain untouched. Additionally, the California Parties aver that the Commission made clear in its Interlocutory Order that it has not ruled out a remedy that all of Respondents' contracts that burdened consumers may be modified.[2235]

1575. With respect to Dr. Berry's testimony, the California Parties argue that Respondents' wrongly characterize it as a request for a market-wide remedy. The

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[2232] Ex. CAT-270.

[2233] *Texaco Inc. v. FERC*, 148 F.3d 1091, 1094 (D.C. Cir. 1998) (citing *Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 636, FERC Stats. & Regs. ¶ 30,939 (1992) (subsequent history omitted)).

[2234] *See Texaco Inc.*, 148 F.3d at 1094-95. *See also TAPS*, 225 F.3d at 683, 710-712; *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 954-56 (D.C. Cir. 2005).

[2235] Order Granting Interlocutory Appeal at P 15.

California Parties state that Dr. Berry merely demonstrates how the Commission already viewed the prices that Respondents charged CERS and determined those prices to be unjust and unreasonable.[2236] Additionally, the California Parties state that Respondents attempt to distinguish CERS's sales to the ISO from Respondents' sales to CERS by noting that Respondents' sales to CERS were not OOM purchases pursuant to the ISO tariff. The California Parties argue that this is irrelevant because CERS was created to purchase the power that the ISO previously had purchased through its centralized auction and OOM purchases.[2237] Thus, the purchases CERS was making and paying for were essentially OOM purchases.[2238] Lastly, the California Parties aver that Respondents' assertions concerning the appropriateness of the MMCP are irrelevant and premature because the MMCP was used to determine an appropriate remedy.

1576. Fifth, the California Parties contend that Respondents wrongly rely on "market fundamentals" to justify the high prices. The California Parties note that they have already demonstrated that the high prices were the result of sellers' market manipulation, illegal behavior, and tariff violations. However, the California Parties argue that even if true, market fundamentals are irrelevant to whether Respondents' contract rates imposed a burden on consumers. The California Parties note that in *Morgan Stanley*, the Supreme Court held that natural disasters could result in rates so high as to impose an excessive burden on the public.[2239] Thus, even if it were the case that Respondents' rates were due, for example, to a historically hot summer or aberrantly-low hydro supplies, that would not immunize their contracts from modification.

1577. Sixth, the California Parties state that the Respondents blame California's retail rate freeze for causing the IOUs to default while also crediting the rate freeze for ensuring that consumers were not burdened by Respondents' contract rates. The California Parties argue that Respondents' claims rely on Professor Hogan's assertion that California should have eliminated the rate freeze to curb electric power demand.[2240] However, the California Parties note that Commissioner Florio testified as to the harm

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[2236] *See* Ex. CAT-213.

[2237] *See id.* at 6.

[2238] Ex. CAT-643 at 6-7.

[2239] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 549 n.4 (2008).

[2240] Ex. PNR-1 at 77:3-7.

that resulted from immediate pass through of costs in San Diego.[2241] Commissioner Florio also concluded that "customers simply could not modify their usage quickly enough or dramatically enough to keep their bills under control."[2242]

1578. Regardless, the California Parties contend that the retail rate freeze is irrelevant to whether the contracts with Respondents should be modified. With respect to Respondents contention that the rate freeze prevented any harm to consumers, the California Parties assert that the rate freeze did not insulate consumers from these rates. Rather, it meant that consumers have been forced to pay these rates over many years.

1579. Seventh, the California Parties assert that Respondents wrongly claim that their sales actually helped California. The California Parties state that the evidence demonstrates that there was no supply shortage that Respondents were helping to avoid.[2243] Rather, Respondents were purchasing energy that was going to be sold to California one way or another. The California Parties argue that the mark-ups on the sales to CERS harmed consumers. Moreover, the California Parties note that most electricity wholesale contract sales help, in some technical sense, to avoid blackouts by providing power, but this fact has not prevented court from holding that contracts that burden consumers may be modified. Lastly, the California Parties assert that Respondents' claim that CERS would have had to make a higher priced purchase is irrelevant to the determination of whether there is a burden on consumers.

1580. Eighth, the California Parties argue that Respondents assertion that the California Parties failed prove withholding by Respondents is another example of conflating the question of whether the *Mobile-Sierra* presumption may be avoided with the question of whether the presumption may be overcome. The California Parties again note that "bad acts" are not a requirement for overcoming the *Mobile-Sierra* presumption.

1581. Ninth, the California Parties argue that Respondents' claims regarding actions by policy makers are also irrelevant. The California Parties state that all contracts are entered into within the context of prior decisions by "policymakers" and conditions that were not created by the contracting parties. Thus, the California Parties contend that these issues are irrelevant in determining if the contract rates imposed a burden on consumers.

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[2241] Ex. CAT-001.

[2242] *Id.* at 6.

[2243] *See, e.g.*, Tr. 1211:19-1212:21 (Fox-Penner).

1582. Lastly, the California Parties aver that access to the ISO Control Room is also irrelevant. The California Parties state that even if CERS had obtained sensitive information and had been able to use it to lower Respondents' rates to a somewhat less extreme level, that would be irrelevant to the question set for hearing under Issue 1(B). The California Parties state that Respondents' "unclean" hands argument ignores the fact that the consumers were harmed by Respondents' rates and those third-party consumers do not have "unclean hands."

#### (c) Evidence of Excessive Burden on Consumers and Harm to the Public Interest

1583. The California Parties state that Respondents wrongly attack Professor Berck's testimony as merely showing "what could have happened, not what did happen" if rates were immediately pass through to consumers.[2244] The California Parties note that courts have upheld Commission modification of contracts based upon similarly "hypothetical" harm. The California Parties also note that this argument ignores the testimony of Commissioner Florio, which did detail the effects of immediate pass through in San Diego.[2245]

1584. Additionally, the California Parties contend that Respondents and Trial Staff wrongly calculate the harm on a per consumer basis "down the line." The California Parties state that this ignores Professor Berck's testimony that the proper focus is on the "total amount of overcharges."[2246] The California Parties note that this is not the equivalent of a market-wide remedy because the California Parties ask only that Respondents' contracts be modified to account for their share of the harm.

#### (d) Mr. Taylor's *Mobile-Sierra* Databases

1585. The California Parties assert that Trial Staff misunderstood Mr. Taylor's 1(A) and 1(B) designations from his *Mobile-Sierra* database. The California Parties explain that a 1(A) designation shows a contract where Mr. Taylor observed that CERS paid a price

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[2244] *See, e.g.*, *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 712 (D.C. Cir. 2000); *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686, 692 (1st Cir. 1995); *Miss. Indus. v. FERC*, 808 F.2d 1525, 1553, *different holding vacated in part on other grounds per curiam*, 822 F.2d 1104 (D.C. Cir. 1987). *See also ISO New England*, 143 FERC ¶ 61,150, at P 188 (2013).

[2245] *See* Ex. CAT-001.

[2246] Tr. 1614-1615 (Berck).

above the measured market price and, therefore, Mr. Taylor presumed the exercise of duress, fraud, or bad faith; a 1(B) designation shows a contract where Mr. Taylor observed other specific forms of unlawful market activity; and a 1(A) and 1(B) designation shows a contract where Mr. Taylor observed both a price impact reflecting duress, fraud, or bad faith and other specific forms of unlawful market activity. Thus, Mr. Taylor's designations are irrelevant to findings of harm to consumers.

**(e) Unclean Hands Doctrine**

1586. Lastly, the California Parties address Respondents' claims that CERS engaged in inequitable conduct by (1) using confidential information to gain an unfair competitive advantage and (2) exercising buyer market power. Respondents argue that the California Parties should be denied relief under the equitable doctrine of unclean hands.

1587. The California Parties state that the doctrine of unclean hands prevents a wrongdoer from enjoying the "fruits of his transgression."[2247] "The ultimate decision is whether the [conduct of the] plaintiff as compared with the [conduct] of the defendant warrant[s] punishment of the plaintiff rather than [] the defendant."[2248] Thus, the California Parties argue that Respondents must prove that CERS "transgressed" in comparison to Respondents' conduct, and also that CERS enjoyed the fruits of that transgression. The California Parties argue that Respondents' wrongdoing far outweighs any technical transgression that Respondents could suggest CERS committed. Moreover, the California Parties reiterate that any refunds ordered in this proceeding would not go to CERS, but to the consumers of California.

1588. The California Parties assert that as a government entity, CERS's actions were in an effort to protect the health and welfare of Californians, the viability of the electricity grid, and California's economy during the Western Energy Crisis. The California Parties aver that although the government is not immune from principles of equity, courts are hesitant to apply the doctrine of unclean hands to a government agency acting in the public interest.[2249] The California Parties contend that Respondents have failed to meet

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[2247] *Packers Trading Co. v. CFTC*, 972 F.2d 144, 149 (7th Cir. 1992) (quoting *Precision Instrument Mfg. Co. v. Auto Maint. Mach. Co.*, 324 U.S. 806, 814 (1945)).

[2248] *Republic Molding Corp. v. B.W. Photo Utils.*, 319 F.2d 347, 350 (9th Cir. 1963).

[2249] *SEC v. Gulf and W. Indus. Inc.*, 502 F. Supp. 343 (D.D.C. 1980) (citing *United States v. Second Nat'l Bank of N. Miami*, 502 F.2d 535, 548 (5th Cir. 1974)); *Second Nat'l Bank of N. Miami*, 502 F.2d at 548 (quoting *Pan Am. Petroleum & Transport Co. v.*

(continued…)

this heavy burden in demonstrating that CERS gained an unfair competitive advantage over any seller through the access of non-public information or that CERS attempted to exercise buyer market power. The California Parties assert that there is no evidence that CERS "did something which in good conscience it should not have done, or failed to do something fair dealing required it to do."[2250]

1589. With respect to claims that CERS received non-public ISO information, the California Parties assert that Mr. Hart and Mr. Alaywan both testified that the only confidential information received was provided during the period April 7, 2001 to June 25, 2001, when the ISO provided gross megawatt and associated gross cost information for hourly BEEP Stack purchases it was planning to make and for which it needed CERS's credit backing.[2251] The California Parties note that Mr. Alaywan explained that the information was necessary for CERS to discharge its fiduciary obligations and could not have provided a competitive advantage to CERS as a purchaser in the market.[2252]

1590. The California Parties also state that Mr. Hart received a single generation unit outage report on April 13, 2001.[2253] However, this report was never provided to anyone at CERS, and even if it had, the information would have been of very limited competitive value.[2254] The California Parties further note that the unit-specific outage information was available through public sources.[2255]

1591. The California Parties aver that Respondents provided no witness and rely only on (1) the fact that CERS real-time traders were in the ISO control room; (2) a single sentence from a prior Commission order; (3) a transcript of an internal CERS conversation about whether CERS personnel would remain in the ISO control room;

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*United States*, 273 U.S. 456, 506 (1927)). *See also Deseret Apartments v. United States*, 250 F.2d 457, 458 (10th Cir. 1957).

[2250] *Second Nat'l Bank of N. Miami*, 502 F.2d at 548.

[2251] Ex. CAT-272 at 21-22; Tr. 652:8-21 (Hart); Ex. CAT-643 at 9.

[2252] Ex. CAT-643 at 11.

[2253] Ex. TRC-138.

[2254] *See* Tr. 773:20-774:15 (Hart).

[2255] Tr. 2351:1-5 (McIntosh).

(4) small portions from Mr. Hart's dictated notes; and (5) photographs of the ISO control room. The California Parties assert that this evidence fails to meet the Respondents' burden.

1592. With respect to the Commission's order,[2256] the California Parties contend that the Respondents wrongly characterize the order as "controlling precedent." The California Parties state that the Commission mentioned CERS's access to the ISO control room as an additional basis for denying refunds, and interpreted the confidentiality agreement between CERS and the ISO to mean that CERS's presence in the ISO control room actually gave CERS "written materials, visual observations, and oral statements regarding the ISO's markets, systems, operations and activities."[2257] Based on this interpretation, the Commission concluded that CERS had "a competitive advantage in entering into its bilateral contracts."[2258] However, the California Parties contend that the evidence, taken for the first time in this proceeding, supports a contrary interpretation of the confidentiality agreement.[2259] The California Parties further note that on appeal, the Ninth Circuit specifically indicated that CERS could seek refunds in other proceedings.[2260]

1593. The California Parties also argue that the trader tape relied on by Respondents does not even imply that CERS was able to obtain confidential information by the presence of its traders on the ISO floor.[2261] Moreover, Mr. McIntosh testified that "CERS traders got no non-public information by virtue of their presence at the ISO."[2262] Similarly, the California Parties assert that Mr. Hart's dictation notes only reflect a desire

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[2256] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,515, *order on reh'g*, 97 FERC ¶ 61,275, at 62,194 (2001).

[2257] *San Diego Gas & Elec. Co.*, 96 FERC at 61,515.

[2258] *Id*.

[2259] The California Parties note that the undersigned Presiding Judge pointed out that nothing in the confidentiality agreement states that confidential information was actually being provided. Tr. 657:6-8 (Hart).

[2260] *See Pub. Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1064 (9th Cir. 2006).

[2261] *See* Ex. TRC-139.

[2262] Ex. CAT-641 at 11.

to have CERS personnel in the ISO control room and do not demonstrate that traders actually received non-public information. The California Parties further contend that the screens in the ISO control room were too hard for the CERS personnel to see and that, even if they could see it, all of the information was available publicly.[2263]

1594. Next, the California Parties address Respondents' claim that CERS exercised buyer market power. The California Parties assert that the extremely high prices that CERS alone was forced to pay throughout the Crisis demonstrate that this was not the case. Additionally, the California Parties note that Respondents argue both that CERS was purposefully limiting its day-ahead purchases and that it was not prepared enough to properly make all its purchases in the day-ahead market. The California Parties state that these two assertions are in directly conflict with each other. The California Parties further note that Mr. Alaywan testified that CERS had no market advantage during the CERS Period and was not in position to dictate price.[2264]

1595. The California Parties argue that had CERS tried to exercise market power, it was extremely unsuccessful. The California Parties state that Dr. Fox-Penner showed, Respondents regularly charged CERS much higher prices than they charged others.[2265] Additionally, Mr. Taylor testified that sellers made billions of dollars in profits.[2266] The California Parties further note that day-ahead prices at COB, where CERS supposedly had a large impact on prices, closely tracked day-ahead prices at Mid-C, where CERS did not trade.[2267] Thus, CERS's presence in the market did not drive down prices.

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[2263] Tr. 2347:10-19 (McIntosh). The California Parties argue that Respondents' citation regarding the availability of the information from Genscape should be rejected because it was offered for the first time in post-hearing briefs. 18 C.F.R. § 385.508(d)(3) (2013). In any event, the California Parties assert the information alleged to be confidential and shown on the walls of the ISO room was available on OASIS during the CERS Period. *See, e.g.*, CAL. INDEP. SYS. OPERATOR, https://web.archive.org/web/20001211194900/http://www.caiso.com/marketops/OASIS/pubmkt.html (last visited Mar. 12, 2014).

[2264] *See* Ex. CAT-643 at 12 (emphasis in original).

[2265] *See* Ex. CAT-413 at 7.

[2266] Ex. CAT-289 at 105.

[2267] *See id.* at 106 Figure IV-1.

Additionally, because CERS purchased far less in the day-ahead market, it was unlikely that lowering day-ahead prices would have led to a serious reduction of overall costs.[2268]

1596. Lastly, with respect to Respondents' argument that CERS failed to reveal its true demand to the day-ahead market, the California Parties state that sellers were well aware of how much power was needed because the day-ahead and day-of markets had been operational for years. Moreover, the California Parties note that as soon as the West-Wide price caps were in effect, prices dropped and remained low regardless of how CERS or the IOUs "reveal demand" or predict load.

**(f) Claims are Procedurally Infirm**

1597. The California Parties contend that TransCanada wrongly asserts that the California Parties claims are procedurally infirm because the California Parties failed to file their own complaint that mirrored Puget Sound Energy's. The California Parties state that the Commission's regulations provide for entities to intervene in cases filed by others and, upon doing so, those entities become full parties.[2269] The California Parties note that it would be inefficient – both for the industry and for the Commission – to require separate entities to file overlapping complaints.

1598. Furthermore, the California Parties assert that this issue was already fully addressed by the Ninth Circuit. Specifically, the Ninth Circuit held that "the Commission's attempt to exclude Respondents' sales to CERS from this proceeding] is arbitrary, capricious, and an abuse of discretion."[2270] The Ninth Circuit explained that the "complaint provides no indication of an intent to exclude refunds for energy purchased in the [PNW] spot market for consumption outside the geographical area. … [and] [t]he complaint is silent as to any constraint on the identity of the buyers or where the energy would be consumed."[2271] The California Parties further contend that TransCanada's notice argument was fully addressed by the Ninth Circuit's finding that Puget's complaint "served to notify <u>all</u> sellers of energy in the respective markets that

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[2268] *See id*. at 108.

[2269] *See* 18 C.F.R. § 385.214 (2013) (providing for interventions). *See also id*. at § 385.214(c)(1) (providing that intervenors become parties to the proceeding).

[2270] *Port of Seattle v. FERC*, 499 F.3d 1016, 1033-34 (9th Cir. 2007).

[2271] *Id. See also id*. at 1034 (explaining that the Commission's restrictive interpretation of the scope of this proceeding was inconsistent with the Commission's interpretation of the scope of the Refund Proceeding in Docket No. EL00-95).

they may be liable for refunds for sales of energy in those markets, regardless of where the energy would be consumed."[2272]

1599. With respect TransCanada's claim that the Commission failed to set a refund effective date in this proceeding, the California Parties note that the Ninth Circuit disposed of this argument as well. Specifically, the Ninth Circuit held that "FERC's [later-reversed] dismissal of Puget's complaint did not disturb FERC's ability to set the refund effective date, and FERC was not required to formally set the refund effective date prior to instituting a § 206 refund proceeding."[2273] The California Parties aver that TransCanada's contentions are an improper collateral attack on the Ninth Circuit's determination that Respondents' sales to CERS are squarely within the scope of this proceeding.

1600. Lastly, the California Parties address TransCanada's claim that it "was only with the filing of their [d]irect [t]estimony that the California Parties raised in this case a number of the legal claims of misconduct now pending against TransCanada."[2274] The California Parties state that it was only on remand from the Ninth Circuit that the Commission held that the California Parties would have to make a showing that either avoided or overcame the *Mobile-Sierra* presumption.[2275] Thus, the California Parties' first opportunity to make such a showing was in their Direct Testimony.

**(g) Statute of Limitations**

1601. First, the California Parties assert that its claims of duress, bad faith, and fraud are not asserted as a state law contract claim to void the contracts at issue; these standards, governed by state law, are asserted to show that the *Mobile-Sierra* presumption is inapplicable to the contracts at issue, as discussed in *Morgan Stanley*.[2276] The California

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[2272] *Id*. at 1034 (emphasis added)

[2273] *Id*. at 1032.

[2274] TransCanada Initial Br. at 76-77.

[2275] *See* Order on Remand at P 20 (explaining that "the Commission has not previously addressed" application of the *Mobile-Sierra* doctrine to the sales at issue in this proceeding).

[2276] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 547 (2008) (recognizing that evidence of unfairness, bad faith, or duress in the original negotiation of a contract is grounds for disregarding the *Mobile-Sierra* presumption).

Parties state that the *Mobile-Sierra* presumption was not brought into play until the Commission's October 3, 2011 Order on Remand;[2277] thus the Utah statute of limitations governing standard contract claims is wholly inapplicable.

1602. Furthermore, the California Parties argue that even if the Utah statute of limitations applied, it was satisfied in 2001, as all parties have been on notice since at least August 31, 2001 that the California Parties were asserting concepts of duress as part of their claims in this case. The California Parties also note that TransCanada has been on notice of claims involving rates charged in the Pacific Northwest since the October 26, 2000 complaint.[2278] Lastly, the California Parties assert that the previous federal court litigation of these contract claims against Powerex shows that the Commission is the proper venue for determination of these issues,[2279] and this hearing was the first opportunity for the California Parties to actually present evidence of these claims.

1603. Next, the California Parties argue that they are not attempting to seek a penalty barred by the federal statute of limitations.[2280] The California Parties state that they do not seek broad, market-wide penalties; instead they request refunds for specific contracts from specific Respondents. The California Parties assert that Dr. Berry did not propose resetting all prices to the MMCP.[2281] Rather, Dr. Berry explained that the MMCP is a proper benchmark to determine the rates that TransCanada and other Respondents should have charged, and pointed out that the Commission has already mitigated to the MMCP

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[2277] Order on Remand at P 20.

[2278] *Port of Seattle v. FERC*, 499 F.3d 1016, 1023-24 (9th Cir. 2007) ("Puget's complaint alleged that the California and Pacific Northwest markets were part of the same integrated market of the Western Interconnection, and that market conditions in California influenced market conditions in the Pacific Northwest.").

[2279] *See Cal. Dep't of Water Res. v. Powerex Corp.*, Order, No. 2:05-CV-00518 (Eastern District of California order granting Powerex's motion to stay proceedings on duress complaint because of parallel proceedings pending at the Commission, including proceedings on remand from *Port of Seattle*, 499 F.3d 1016).

[2280] The California Parties assert that TransCanada attempts to equate the California Parties' Issue 1(B) claims with the market-wide relief "penalties" rejected in *Brown. California ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 101 (2011). The California Parties state that this section also refutes TransCanada's *res judicata* argument.

[2281] Ex. CAT-213 at 4:19-5:5.

the sales that CERS made to the ISO of exactly the same energy that Respondents sold to CERS.[2282]

### (h) Equitable Doctrine of Laches

1604. The California Parties first note that the defense of laches is rarely accepted in Commission proceedings and requires that "in addition to the first party sleeping on its rights there is also a showing that the delay caused undue prejudice on the party against whom the claim is brought."[2283] The California Parties aver that TransCanada has no legitimate basis for claiming surprise or undue prejudice. As noted above, the California Parties state that TransCanada had notice of the claims at issue and has presented contemporaneous records regarding the transactions at issue.

1605. Additionally, the California Parties assert that they have not been "sleeping" on their claims or manipulating the legal process to delay consideration of these claims. Rather, the California Parties have been pursuing their claims against Respondents since the crisis began, and intervened in the present proceeding in the summer of 2001.[2284] The California Parties state that this hearing presented the first necessity for the California Parties to pursue claims beyond whether the rates charged were "just and reasonable."[2285]

1606. With respect to its claims of duress, bad faith, and fraud, the California Parties state that TransCanada was on notice as far back as Mr. Hart's original testimony in this case in 2001. The California Parties assert that these claims took on greater significance after the Commission ruled that Respondents' contracts benefit from the *Mobile-Sierra* presumption.[2286]

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[2282] The California Parties state that this section also refutes TransCanada's *res judicata* argument.

[2283] *Nw. Pipeline Corp.*, 56 FERC ¶ 61,231, at 61,890 (1991) (citing *Envtl. Def. Fund, Inc. v. Alexander*, 614 F.2d 474 (5th Cir. 1980)).

[2284] *Port of Seattle v. FERC*, 499 F.3d 1016, 1025-26 (9th Cir. 2007).

[2285] The Commission's Order on Remand was the first time the Commission required the California Parties to present evidence to either avoid or overcome the *Mobile-Sierra* presumption. Order on Remand at P 20.

[2286] *Id*.

1607. Lastly, the California Parties argue that TransCanada's claim that its due process rights have somehow been violated is offered without citation to legal authority, is entitled to no weight, and should likewise be summarily dismissed. The California Parties assert that if TransCanada had truly been harmed, it should have made its concerns known to the Presiding Judge and the Commission by motion to dismiss or otherwise.

### 6. The California Respondents Reply Brief

#### (a) The *Mobile-Sierra* Standard

1608. The California Respondents contend that the California Parties improperly aggregate contracts in their analyses. The California Respondents state that the Supreme Court and Commission both explained that the *Mobile-Sierra* presumption is contract-specific.[2287] Therefore, the California Parties were required to show that presumption should be avoided or overcome as it relates to a specific contract.

1609. The California Respondents argue that the Commission has already rejected the California Parties claim that general market dysfunction and the alleged role of CERS's contracts with Respondents in perpetuating and exacerbating price instability justify not engaging in a contract-specific analysis. Specifically, the Commission stated that "massive revision of bilateral contracts that would be required to provide a refund remedy for market participants in the Pacific Northwest would create an *unacceptable amount of risk and uncertainty* for future market participants in the region, since *it would set a precedent that the contract price for power may always be subject to change*— without any advanced warning."[2288] The California Respondents also note that in *Morgan Stanley*, the Court explained that "[i]f there were ever a context where long-settled understanding should be honored it is here, where a statutory decision (subject to revision by Congress) has been understood the same way for many years by lower courts, by this Court, by the federal agency the statute governs, and hence surely by the private actors trying to observe the law."[2289]

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[2287] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008); Order Granting Interlocutory Appeal at P 1; Order on Rehearing at PP 14, 30.

[2288] *Puget Sound Energy, Inc. v. All Jurisdictional Sellers*, 105 FERC ¶ 61,183, at P 54 (2003) (emphasis added). The California Respondents argue that the Ninth Circuit's remand did not affect this conclusion. Order on Rehearing at P 3.

[2289] *Morgan Stanley*, 554 U.S. at 551 n.6.

1610. The California Respondent assert that the California Parties only make allegations of collective harms – harms caused by a group of contracts with a group of sellers, many of who are not even in this case. The California Respondents aver that there is no analysis of any specific contract or its formation, no explanation of how the negotiation of any individual contract affected the public interest, or any other grounds for contract modification specific to a single contract.[2290] The California Respondents aver that Mr. Taylor's database includes only conclusory statements drawn from general theories or documents that usually make no mention of any Respondent.[2291] The California Respondents argue that aggregating contracts, whether by seller or by purchaser, as the California Parties do, would eviscerate the *Mobile-Sierra* doctrine.

1611. Next, the California Respondents contend that the California Parties misconstrue precedent. The California Respondents state that reliance *FPC v. Texaco, Inc.*[2292] is misguided because it ignores the Supreme Court's later statement in *Morgan Stanley*. Specifically, the *Morgan Stanley* Court found that public interest of the *Mobile-Sierra* doctrine "refer[s] to something more than a small dent in the consumer's pocket," and noted that this is "why our subsequent cases have described the [public interest] standard as a high one."[2293] The Court distinguished *Texaco*, stating that *Texaco* "had nothing to do with" the *Mobile-Sierra* doctrine and concerned a Commission order exempting small producers of natural gas from direct rate regulation.[2294]

1612. The California Respondents also argue that the California Parties improperly rely on cases from the First Circuit and D.C. Circuit that were issued prior to *Morgan Stanley*. Specifically, the California Parties cite these cases, as well as one Commission order, for the proposition that contracts involving harm to consumers and businesses that were not parties to the contracts can be modified under the public interest standard. The California Respondents contend that the cases relied on by the California Parties are not the precise situation in this proceeding. The California Respondents state that none of the cases

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[2290] *See Morgan Stanley*, 554 U.S. at 552-53 (discussing factors potentially relevant to the public interest, including rates and alternatives available at the time of contract formation); Order Granting Interlocutory Appeal at P 1.

[2291] *See, e.g.*, Tr. 2766:24-2810:6 (Taylor).

[2292] *FPC v. Texaco, Inc.*, 417 U.S. 380, 399 (1974) ("the Commission may not ignore even a 'small dent in the consumer's pocket' when reviewing rates").

[2293] *Morgan Stanley*, 554 U.S. at 551 & n.6.

[2294] *Id.* at 546-47.

involve a buyer's request to unilaterally modify a contract rate based on an after-the-fact showing that the price was high. The cases also do not condone grouping together the sellers to one purchaser and making a generic public interest finding on the basis of the purchaser's overall supply cost. The California Respondents argue that the cases are not analogous to a *Mobile-Sierra* case of the type discussed in *Morgan Stanley* and at issue here, where one unaffiliated party to a bilateral contract unilaterally challenges the contract rate.[2295]

1613. The California Respondents state that each of the cases involved either the Commission's initial review of a contract filing or tariff filing, inter-affiliate dealing, a Commission determination of the "public interest" in the context of a generalized rulemaking proceeding, or efforts by contract parties to implement terms that are contrary to Commission policy. The California Respondents note that none of the cases include the public interest question of when a party to a contract should be relieved of its "improvident bargain."

1614. Furthermore, the California Respondents contend that the California Parties reliance on *Northeast Utilities* fails to understand the logic of that decision.[2296] Specifically, in *Northeast Utilities*, the court upheld the Commission's decision to modify a newly filed intra-affiliate agreement on the grounds that there was no genuine arms-length bargaining and the contract might unduly discriminate against entities not party to the contract.[2297] The California Respondents state that the Commission specifically explained that the public interest review in *Northeastern Utilities* was infused with critical factors not present in the typical *Mobile-Sierra* case like the one at issue in this proceeding.[2298] The California Respondents state that the case essentially involved an agreement with a provision at odds with Commission policy and an attempt to make

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[2295] *See Ne. Utils. Servs. Co.*, 66 FERC ¶ 61,332, at 62,088 (1994); *Ne. Utils. Servs. Co. v. FERC*, 55 F.3d 686, 689-90 (1st Cir. 1995) (*Northeast Utilities*).

[2296] The California Parties cite *Northeast Utilities Service Co. v. FERC* for its rejection of a prior statement by the D.C. Circuit that the public interest standard is "practically insurmountable." *Ne. Utils. Servs. Co. v. FERC*, 55 F.3d 686 (1st Cir. 1995). The California Respondents state that their initial brief discuss the Supreme Court and other precedent that describe the standard as a high one. *See, e.g., Morgan Stanley*, 554 U.S. at 551 n.6.

[2297] *Northeast Utilities*, 55 F.3d at 687.

[2298] *See Ne. Utils. Servs. Co.*, 66 FERC ¶ 61,332, at 62,076, 62,086-89 (1994).

that provision unreviewable by bootstrapping the public interest standard onto that provision.[2299]

1615. Similarly, in *Mississippi Industries v. FERC*, the *Mobile-Sierra* issue arose as a jurisdictional question of whether affiliated parties could agree to allocate costs without making their allocation subject to Commission modification.[2300] The California Respondents assert that precluding review in this fashion presents an issue that is not relevant to the application of the *Mobile-Sierra* presumption as it relates to CERS's contracts with Respondents, contracts entered into by unaffiliated parties at arms-length producing rates that already have been deemed just and reasonable under the Commission-sanctioned market pricing program.

1616. The California Respondents state that *Texaco Inc. v. FERC* also involved Commission modification of an initial contract filing in which the signatories, both proponents of the contract, attempted to adopt a contract provision contrary to Commission ratemaking policy.[2301] The California Respondents assert that the *Texaco* court effectively refuted the notion that the "public interest" is an easy standard to meet in the *Mobile-Sierra* context and confirmed that a contract-specific analysis is required. Specifically the court stated that the Commission's analysis used in rulemaking proceedings would not suffice for the evaluation of a contract; rather, "the public interest necessary to override a private contract ... is significantly *more particularized* and requires analysis of the manner in which *the contract* harms the public interest and of *the extent to which abrogation or reformation mitigates the contract's deleterious effect*."[2302]

1617. Next, the California Respondents address the cases cited by the California Parties for their assertion that *Mobile-Sierra* does not require a particularized public interest finding, but only a generic finding relating to all of CERS's contracts. First, in *TAPS*, the D.C. Circuit upheld the Commission's Order No. 888 open-access rulemaking , recognizing the unique nature of the Order Nos. 888 and 889 and emphasizing that "generic *Mobile-Sierra* findings are appropriate only in rare circumstances" such as "Order No. 888 [which] fundamentally change[d] the regulatory environment in which

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[2299] *See Ne. Utils. Serv. Co.*, 66 FERC at 62,077-78.

[2300] *Miss. Indus. v. FERC*, 808 F.2d 1525, 1534 & n.30 (D.C. Cir. 1987).

[2301] *Texaco Inc. v. FERC*, 148 F.3d 1091, 1093-95 (D.C. Cir. 1998).

[2302] *Id.* at 1097 (emphasis added).

utilities operate."[2303] The California Respondents argue that the modifications sought by the California Parties do not compare with contract modifications required to conform those contracts to an industry-wide rulemaking.

1618. The California Respondents state that in *ISO New England Inc.*, the Commission reinforced the difference between the type of analysis applicable in the context of a rulemaking and the analysis applicable in the context of bilateral contracts.[2304] Specifically, the Commission noted that when the Commission is implementing new regulations that affect existing contracts, the issue is not whether Commission action impermissibly relieves one party of its "improvident bargain," but whether the Commission is properly exercising its "plenary authority to limit or to proscribe contractual arrangements that contravene the relevant public interests."[2305]

1619. Moreover, the California Respondents note that in Order No. 888-A the Commission *rejected* the request for generic reformation of long-term purchases of electricity, explaining that "[i]n the majority of circumstances, such long-term supply contracts are voluntary arrangements in which neither party had market power [and it] would be inappropriate to make generic *Mobile-Sierra* findings as to these types of contracts."[2306] The California Respondents argue that the CERS contracts at issue in this proceeding are similar because CERS purchased energy from multiple suppliers in the Pacific Northwest spot market and had the opportunity to negotiate rates among those suppliers.

1620. Next, the California Respondents assert that the cases cited by the California Parties demonstrate that for "generic" public interest findings, the modified contracts must be affected by the relevant intervening circumstances "in an identical manner,"

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[2303] *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667, 711 (D.C. Cir. 2000) (*TAPS*).

[2304] *ISO New England Inc.*, 143 FERC ¶ 61,150 (2013).

[2305] *Id.* P 175 (footnotes and citations omitted). The Commission further stated that even in a rulemaking context, the *Mobile-Sierra* doctrine requires the Commission to make a "particularized" showing of "the manner in which the contract harms the public interest and … the extent to which abrogation or reformation mitigates the contract's deleterious effect." *Id.* PP 175-76.

[2306] Order No. 888-A, 62 FR at 12274, 12286 (Mar. 14, 1997), FERC Stats. & Regs. ¶ 31,048 (prior and subsequent history omitted).

justifying identical treatment.[2307] The California Respondents note that the Commission has explained that "[i]n *Mobile-Sierra* cases involving bilateral power sales contracts, like *Sierra* and *Morgan Stanley*, the 'intervening circumstances [prompting reexamination of the contract] *are unique to the relationship between contracting parties*.'"[2308]

1621. The California Respondents contend that the California Parties failed to show how the contract terms were affected by some intervening circumstance on a contract by contract basis. Thus, there is no way to determine if the intervening circumstances affected the relevant contracts "in an identical manner." The California Respondents assert that in rejecting a market-wide remedy, the Commission already rejected the argument that all contracts occurred in the Pacific Northwest spot market and that the "intervening" circumstance of market dysfunction serves a basis for a generic public interest finding.[2309]

1622. Next, the California Respondents aver that the California Parties conflate Issues 1(A) and 1(B) by alleging an excessive burden based on aggregated allegations of market manipulation and wrongdoing. Specifically, the California Parties, quoting Mr. Taylor's testimony, state that "[i]t is in the public interest to have markets free of the distortions that occurred during the [Crisis], and it makes no sense to promote wrongdoing by allowing [Respondents] to keep ill-gotten gains."[2310] The California Respondents argue that the California Parties' approach is inconsistent with the *Mobile-Sierra* doctrine and *Morgan Stanley* and has been expressly rejected by the Commission in this proceeding.[2311]

1623. The California Respondents state that Issues 1(A) and 1(B) are distinct and address discrete parts of the *Mobile-Sierra* analysis. The California Respondents assert that Issue 1(B) only arises after Issue 1(A) has been resolved. The California

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[2307] *TAPS*, 225 F.3d at 710.

[2308] *ISO New England Inc.*, 143 FERC ¶ 61,150, at P 175 (quoting *TAPS*, 225 F.3d at 710).

[2309] *See* Order on Remand at P 21.

[2310] California Parties Initial Br. at 167 (quoting Ex. CAT-041 at 135).

[2311] *See, e.g.*, *Morgan Stanley*, 554 U.S. at 547-48, 554-55. *See also California ex rel. Brown*, 135 FERC ¶ 61,178, at P 88 (2011); Order on Rehearing at P 30; Order Granting Interlocutory Appeal at PP 13-15.

Respondents further argue that the California Parties approach is nonsensical because there would be no need to address the "public interest" of preventing Respondents from keeping their "ill-gotten gains" because if proven true, the "ill-gotten gains" would have required contract modification under Issue 1(A).

1624. The California Respondents also contend that the California Parties' attempt to distinguish the importance of long-term and spot-market contracts is also short-sighted. The California Respondents argue that parties to valid long-term and short-term contracts alike must be able to rely on the enforceability of those contracts or neither party will be willing to enter into either type of agreement, particularly in times of scarcity when prices might be volatile and contracts carry greater financial risk. Moreover, the California Respondents state that the spot market itself and the contracts underlying that market are vital because they allow for the final balancing of system demands. The California Respondents aver that the *Mobile-Sierra* presumption is rooted in the idea that parties negotiating at arms-length can be expected to negotiate a contract with a just and reasonable rate, and there is no reason that expectation is any different for the spot contracts than for the long-term contracts. Lastly, the California Respondents aver that were market participants to understand that *Mobile-Sierra* will not protect short-term contracts, then some will refuse to enter into short-term agreements and others will enter into such agreements with an intent to disclaim contract terms whenever it becomes advantageous to do so.

1625. Next, the California Respondents argue that the California Parties wrongly assert that if the evidence of harm they provided is insufficient, then no evidence of harm can overcome the *Mobile-Sierra* presumption. The California Respondents assert that this argument attempts to gloss over the fact that the California Parties simply failed to make the required showings – "that the contract rate imposes an excessive burden on consumers or seriously harms the public interest."[2312]

1626. Furthermore, the California Respondents assert that the California Parties statement implies that its case is an open-and-shut case of contracts clearly adverse to the public interest. However, the California Respondents note that in *Morgan Stanley*, the Court could have issued a finding that the *Mobile-Sierra* presumption had been successfully avoided or overcome, but chose not to and instead remanded the case for additional review.[2313]

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[2312] Order Granting Interlocutory Appeal at P 12; Order on Rehearing at P 14.

[2313] *Morgan Stanley*, 554 U.S. at 552-53.

1627. Next, the California Respondents aver that the California Parties mischaracterize the Supreme Court's interpretation of the *Mobile-Sierra* doctrine in footnote 4 of its *Morgan-Stanley* decision.[2314] The California Respondents argue that the "exogenous" circumstances alluded to in footnote 4 are relevant, if at all, only to Issue 1(B). That is, according to footnote 4, "circumstances exogenous to contract negotiations" can be "relevant to whether the contracts impose an 'excessive burden' on consumers relative to what they would have paid absent the contracts."[2315] The California Respondents argue that footnote 4 has no relevance to Issue 1(A), which examines whether a contract party's own misconduct prevented *ab initio* contract formation.

1628. The California Respondents state that the Court later instructed the Commission to consider circumstances "exogenous" to contract formation that could have an impact "down the line" following contract formation. However, the California Respondents note that neither the Commission nor any court has ever found that a spot-market sale excessively burdened consumers in violation of the public interest regardless of whether burden was immediate or "down the line." In this case, the California Respondents contend that the California Parties failed to offer any evidence that any Respondent spot sale to CERS imposed an "excessive burden" relative to what consumers would have paid absent the contracts.

1629. Furthermore, the California Respondents acknowledge that the Court instructed that "natural disasters" could be an "exogenous factor" affecting the burden on consumers "down the line." However, the California Respondents assert that the California Parties have not argued that any natural disaster is part of their case for a finding of excessive burden on consumers sufficient to overcome the *Mobile-Sierra* presumption. The California Respondents note that the California Parties disputed

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[2314] Footnote 4 states: "The dissent criticizes the Commission's decision because it took into account under the heading 'totality of the circumstances' only the circumstances of the contract formation, not 'circumstances exogenous to contract negotiations, including natural disasters and market manipulation by entities not parties to the challenged contract.' … Those considerations are relevant to whether the contracts impose an "excessive burden" on consumers relative to what they would have paid absent the contracts. It is precisely our uncertainty whether the Commission considered those 'circumstances exogenous to contract negotiations'" discussed in Part III of our opinion, that causes us to approve the remand to FERC." *Id*. at 549 n.4 (citation omitted).

[2315] *Id*.

whether the "natural disaster" of the drought *per se* had any effect at all on power supply availability and prices during the CERS Period.[2316]

1630. With respect to the Court's reference to "market manipulation by entities not parties to the challenged contract," the California Respondents assert that the California Parties did not introduce evidence showing that third-party market manipulation caused Respondents' contracts to impose an "excessive burden" on consumers relative to what they would have paid absent the Respondents' contracts. Moreover, the California Respondents state that the California Parties provided no evidence to show whether or how any of the acts in California of which they complain influenced prices in the Pacific Northwest.

1631. To the extent that the California Parties are arguing that the activities of third parties are relevant under Issue 1(A), the California Respondents argue that this is inconsistent with the narrow focus of footnote 4 and Commission precedent holding that only a party's own misconduct can be a ground for preventing the *Mobile-Sierra* presumption from applying to its contract.[2317]

### (b) Evidentiary Standard and *Prima Facie* Case

1632. The California Respondents argue that the California Parties confuse their burden of production with the burden of proof. The California Respondents state that a complainant must produce a *prima facie* case in order to prevent the Commission from dismissing its claims or a judge from granting summary disposition against it.[2318] Establishment of a *prima facie* case shifts to the respondent the burden of producing contrary evidence, but does not change the burden of persuasion, which remains with the complainant. The California Respondents assert that once the respondent has raised a factual dispute as to at least one element of the complainant's claim, then the evidentiary value of the complainant's *prima facie* case disappears and all record evidence that bears on each disputed issue of material fact and law must be weighed.[2319]

1633. With respect to the burden of proof, the California Respondents state that a preponderance of the evidence requires assessment of all of the evidence to determine

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[2316] *See* California Parties Initial Br. at 93-94 (citing Ex. CAT-289 at 14).

[2317] *Morgan Stanley*, 554 U.S. 547-48, 554; Order on Remand at PP 20-21.

[2318] *Columbia Gulf Transmission Co.*, 79 FERC ¶ 61,351, at 61,501 (1997).

[2319] *Phillips Petroleum Co. v. FERC*, 902 F.2d 795, 802 (10th Cir. 1990).

whether the complainants have carried their ultimate burden of persuasion on every element of their case.[2320] The California Respondents aver that the California Parties' notion of an "overwhelming" *prima facie* case is a transparent attempt to confuse a *prima facie* case with the much-more-demanding standard of proof that complainants must meet.

1634. Next, the California Respondents argue that the California Parties failed to present a *prima facie* case with regard to Issue 1(B). The California Respondents state that the California Parties failed to provide the necessary contract-specific evidence that any Respondent contract imposed on consumers an excessive burden that seriously harmed the public interest.

1635. The California Respondents further note that in order to establish an excessive burden, the California Parties must analyze the price consumers would have paid but for the contracts.[2321] The California Respondents state that the Commission has held that the appropriate measure of the cost of substitute power at a particular point in time in the duration of a contract is the actual market prices available at that time …."[2322] The California Respondents argue that the California Parties provided no evidence concerning the rates that customers would have paid (but for the contracts) further down the line or what impact exogenous factors had on those rates.

1636. The California Respondents contend that the California Parties only rely on evidence that is irrelevant to the appropriate inquiry, including accounts of harm that occurred outside the CERS Period,[2323] an analysis of hypothetical harm to consumers that did not occur,[2324] generalized allegations of market manipulation by non-parties,[2325] and the suggestion that rates higher than the MMCP imposed an excessive burden in the Pacific Northwest.[2326] The California Respondents assert that this is insufficient to

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[2320] *Harvey v. Merit Sys. Protection Bd.*, 802 F.2d 537, 544 (D.C. Cir. 1986).

[2321] *Morgan Stanley*, 554 U.S. at 549 n. 4, 552-53.

[2322] *Nev. Power Co. & Sierra Pac. Power Co.*, 125 FERC ¶ 61,312, at P 20 (2008).

[2323] Ex. CAT-001 at 3:2-4; Ex. CAT-037 at 15.

[2324] Ex. CAT-267 at 3:20-4:2; Tr. 1565:15-18 (Berck).

[2325] California Parties Initial Br. at 130, 142, 173-75.

[2326] Ex. CAT-536.

establish a *prima facie* case that a specific contract rate imposed on consumers an excessive burden that seriously harmed the public interest.

1637. The California Respondents also contend that the California Parties confuse the law by assuming that there are two separate legal standards under section 205 of the Federal Power Act: a "public interest standard" and the "just and reasonable standard." The California Respondents state that the *Morgan Stanley* Court rejected that notion and explained that the "public interest standard" is merely a differing application of the just and reasonable standard that requires bilateral contract rates to be presumed just and reasonable.[2327] The California Respondents assert that the California Parties provide only generalized claims that are unrelated to the Respondents' contracts, and make no contribution to the required *prima facie* showing of whether these contracts imposed an excessive burden that seriously harmed the public interest.

**(c) Legitimate Business Activity by Respondents**

1638. The California Respondents argue that identifying price separations across points in time or locations and opportunistically capturing those price spreads is what a marketer is supposed to do and, in fact, must do if it wants to stay in business.[2328] The California Respondents state that bringing supplies from lower priced markets to expand choices and enhance competition in higher priced markets is a highly desirable outcome for consumers. The California Respondents assert that the California Parties' characterization of marketers as shameless opportunists demonstrates that they do not understand the Commission's market-based rate program, how it interfaces with the *Mobile-Sierra* presumption, and how competitive power markets operate.

1639. The California Respondents state that the California Parties allege that the prices negotiated by CERS are improper because they exceed the Commission's MMCP, and thus, must be the product of market manipulation. The California Respondents argue that the California Parties position that CERS's prices should be reset to a level based on marginal energy costs directly contradicts *Morgan Stanley's* explicit rejection of a cost-based zone of reasonableness.[2329]

1640. The California Respondents state that prices in bilateral markets are set through negotiations between the two contracting parties, and a rational seller seeks to negotiate a

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[2327] *Morgan Stanley*, 554 U.S. at 535.

[2328] Ex. SNA-1 at 4:13-17.

[2329] *Morgan Stanley*, 554 U.S. at 550.

competitive price – not a price reflective of the seller's cost, but a price based on the seller's expectation of what the prevailing market price will be for comparable transactions.[2330] The California Respondents assert that the expectation of reselling at a prevailing price in the higher priced market motivated the marketer to purchase energy in the lower priced market.

1641. The California Respondents state that the Commission's regulations governing who may obtain market-based pricing authority screens out applicants who may be able to exercise market power in order to obtain non-competitive rates.[2331] The California Respondents state that no Respondent had control of assets sufficient to permit an exercise of market power.[2332] The California Respondents state that market conditions dictated the margins that resellers collected.

1642. With respect to the Pacific Northwest market, the California Respondents state that prices in a given hour were dictated by the demand that existed. Moreover, the California Respondents state that the record demonstrates that there was a persistent premium for energy delivered in the Pacific Northwest as compared to prices in other markets during the CERS Period.[2333] The California Respondents attribute this premium to the result of supply and demand conditions in the Western Interconnection generally and the Pacific Northwest specifically.[2334]

1643. Next, the California Respondents contend that the MMCP is not a valid measure of marginal cost in the relevant period because marginal cost is defined in economic theory as the higher of the incremental cost of additional energy or the seller's opportunity cost.[2335] The California Respondents state that it is economically illogical for a market participant to sell below the best-priced sales opportunity—its opportunity cost—as doing so will forego available profit. Moreover, the California Respondents

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[2330] Ex. PNR-1 at 15:1-18.

[2331] *See Analysis of Horizontal Market Power under the Federal Power Act*, 138 FERC ¶ 61,109, at PP 6, 57 (2012).

[2332] Coral owned or controlled only 28 MW of generation inside the California ISO. Ex. SNA-1 at 3:16-17.

[2333] *See* Ex. TAE-1 at 17:8-18:2.

[2334] Ex. PNR-1 at 12:1-4.

[2335] *Id.* at 13:18-19.

assert that the MMCP is particularly inappropriate for sales in the Pacific Northwest because it was designed for the California organized markets and did not include opportunity costs.[2336]

1644. Similarly, the California Respondents state that it is illogical to presume that marketers should limit their price to close to the acquisition cost. The California Respondents note that marketers, such as the Respondents in this proceeding, incurred expenses and risks by entering into transactions with the expectation they would be able to resell their energy to a purchaser offering a price equal to or better than the Respondent's alternatives. Additionally, no Respondent could expect to negotiate a sale to CERS unless CERS concluded that the negotiated price represented CERS's best alternative. The California Respondents note that Respondents were not the supplier of last resort in the Pacific Northwest, but instead consistently underpriced in relation to the supplier of last resort.[2337] The California Respondents assert that absent evidence that a Respondent had unduly influenced the prices that others offered to CERS, there is no reason for the Commission to overturn CERS's presumptively beneficial transactions.

1645. Lastly, the California Respondents argue that there is no basis for the California Parties' general claim of withholding. The California Respondents state that commodity markets, such as the Pacific Northwest electricity market, have temporal segments that allow parties to transact in forward markets, where sales are negotiated one day or more before delivery, or in real-time markets, in which sales are negotiated on the same day as delivery. The California Respondents assert that the California Parties' claim of withholding from the day-ahead market is only relevant if the California Parties can demonstrate that prices, as a result of that decision, moved to non-competitive levels.[2338] The California Respondents aver that no such evidence was submitted.

#### (d) Various Arguments Raised by the California Parties

1646. First, the California Respondents argue that the California Parties wrongly assert that the WSCC market was not workably competitive. The California Respondents note that Professor Hogan testified extensively regarding the causes for the high prices in the Pacific Northwest.[2339] Furthermore, the California Respondents assert that Mr. Taylor's

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[2336] *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418, at 62,564 (2001).

[2337] *See* Ex. TRC-1 at 126:4-6.

[2338] Ex. PNR-1 at 24:1-6, 32:9-33:4.

[2339] *See id.* at 82-153.

contention that reductions in hydro supply were the result of strategic decision-making ignores the statistics showing the sharp decline in energy produced by hydro facilities.[2340] Moreover, the California Respondents note that the Court in *Morgan Stanley* also stated that reduced hydro production was one of a number of factors contributing to a very tight market for energy in 2001.[2341] The California Respondents also state that Mr. Taylor even conceded that the drought did adversely affect market fundamentals during the relevant period.[2342] Lastly, the California Respondents aver that the California Parties ignore the Commission's finding that the market in the Pacific Northwest was competitive during the CERS Period.[2343]

1647. Second, the California Respondents contend that there is no evidence proving that Respondents engaged in withholding, gas market manipulation, Enron-style gaming, or committed tariff violations. The California Respondents assert that the California Parties' witnesses rely on findings made in staff reports never adopted by the Commission, CFTC findings, and pleas by persons not employed by or working for Respondents. With respect to alleged tariff violations, the California Respondents note that the evidence offered to support the statement about thousands of tariff violations does not even purport to assert any finding that Respondents committed tariff violations.

1648. Third, the California Respondents address the California Parties claim that the high prices were the result of high margins, not scarcity. The California Respondents state that the Commission has repeatedly recognized that competition among purchasers will drive up prices when resources are scarce.[2344] The Commission has also found that

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[2340] *See* Ex. TRC-1 at 15:9-14.

[2341] *See Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 540 (2008).

[2342] Ex. CAT-289 at 14.

[2343] *See Puget Sound Energy, Inc.*, 103 FERC ¶ 61,348, at PP 13, 15, 32, 41, *reh'g denied*, 105 FERC ¶ 61,183 (2003), *remanded sub nom., Port of Seattle v. FERC*, 499 F.3d 1016 (9th Cir. 2007).

[2344] *Tenn. Gas Pipeline Co.*, 94 FERC ¶ 61,097, at 61,398 (2001); *Regulation of Short-Term Natural Gas Transportation Services and Regulation of Interstate Natural Gas Transportation Services*, Order No. 637, 65 Fed. Reg. 10,156, at 10,181 (2000) (subsequent history omitted). *See also Citizens Power & Light Corp.*, 48 FERC ¶ 61,210, at 61,177 (1989).

the collection of scarcity rents is consistent with competitive markets.[2345] The California Respondents state that scarcity rents are, by definition, escalations in price that occur independent of production costs and signal the need for new capacity by demonstrating that prices will justify investment in the construction of new capacity.[2346] The California Respondents note that Dr. Fox-Penner conceded that price signals were effective in signaling the need for new capacity during the energy crisis, as evidenced by capacity additions of 2,982 MW in 2001, 1,990 MW in 2002, and 2,513 MW in 2003.[2347] Moreover, the California Respondents aver that scarcity prompts bidders to increase offer prices in order to obtain scarce capacity. Thus, higher margins do not cause scarcity, higher margins result from scarcity.

1649. Fourth, the California Respondents contend that Dr. Fox-Penner's price discrimination analysis does not demonstrate that prices to CERS exceeded market prices. The California Respondents state that Dr. Fox-Penner's analysis has been thoroughly rebutted. Moreover, the California Respondents assert that Dr. Fox-Penner ignored the incentive for CERS voluntarily to have offered to pay higher prices to insure its access to the limited supply.

1650. Fifth, the California Respondents aver that the California Parties wrongly claim that Respondents overstated credit and litigation risk. The California Respondents state that Respondents' prices to CERS were reflective of competitive prices collected for contemporaneous transactions with similarly situated counterparties, and credit and litigation risk is relevant to the degree to which other buyers from Respondents were similarly situated to CERS.

1651. Sixth, the California Respondents address the California Parties claim that sales to CERS did not help California because Respondents refused to sell in the day-ahead market. The California Respondents argue that this ignores the reasons why Respondents

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[2345] *See, e.g., Edison Mission Energy, Inc. v. FERC*, 394 F.3d 964, 967 (D.C. Cir. 2005); *Tenn. Gas Pipeline Co.*, 94 FERC at 61,398.

[2346] *See, e.g., Blumenthal v. FERC*, 552 F.3d 875, 883 (D.C. Cir. 2009); *PacifiCorp v. Reliant Energy Servs., Inc.*, 102 FERC ¶ 63,030, at P 32 (2003).

[2347] Ex. CAT-161 at 41:6-8. *See also* Ex. TAE-8 at 40:14-17.

sold only in the day-of market, such as temporal arbitrage,[2348] reliance on non-firm transmission,[2349] volatility in the PPoA,[2350] and Coral's back-to-back transactions.[2351]

1652. Seventh, the California Respondents argue that the California Parties wrongly ignore evidence comparing Respondents' prices to CERS with other sellers' prices to CERS.[2352] The California Respondents contend that the fact that CERS was paying other suppliers more than it paid Respondents disproves the allegation that Respondents were withholding energy to exact the highest prices or that Respondents had market power and used market power to raise prices.[2353]

### 7. TransCanada Reply Brief

#### (a) The *Mobil-Sierra* Standard

1653. TransCanada states that the *Mobile-Sierra* presumption's emphasis on honoring bilateral contracts is the rule, not the exception. TransCanada avers that the California Parties wrongly imply that that abrogation of private bilateral contracts is not unusual. TransCanada argues that the California Parties failed to meet their burden of demonstrating that "specific contract rates imposed an excessive burden on consumers."[2354]

1654. TransCanada also states that because its contracts were entered into pursuant to TransCanada's market-based rate authority, and therefore deemed just and reasonable, it need not demonstrate after-the-fact that the rates are reasonable based upon the traditional

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[2348] Ex. PNR-1 at 24:1-6.

[2349] *See, e.g.*, Ex. TRC-77 at 9:7-10.

[2350] Ex. TRC-77 at 7:1-6; Tr. 3547:7-12, 3587:15-22, 3653:10–12 (Kunz).

[2351] Ex. SNA-1 at 15:18-16:4.

[2352] *See* Ex. TRC-195.

[2353] Ex. TRC-1 at 126:4-6.

[2354] Order Granting Interlocutory Appeal at P 15.

"cost-of-service" or that the rates are reasonable based upon the seller's own marginal cost.[2355]

1655. TransCanada further argues that the California Parties avoid the language from *Mobile* and *Sierra* highlighting the necessary balance that exists between the need for contract stability and public regulation, and the necessary restraint on the part of the Commission when faced with calls for contract reformation.[2356] TransCanada asserts that the California Parties fail to recognize that the preservation of contracts benefits customers in the long run and is fully consistent with the Commission's responsibility to protect consumers.

1656. TransCanada avers that the California Parties wrongly assert that the issue is whether any customer would be burdened by the rates and that "the Commission may not ignore even 'a small dent in the consumer's pocket' when reviewing rates."[2357] TransCanada argues that this assertion ignores the Supreme Court's directive that the Commission should only reform contracts under "extraordinary circumstances where the public will be severely harmed."[2358] Moreover, TransCanada notes that in *Morgan Stanley* the Court explicitly stated that the harm to the public interest referred to in *Sierra* "refer[s] to something more than a small dent in the consumer's pocket, which is why our subsequent cases have described the standard [for overcoming *Mobile-Sierra*] as a high one."[2359]

1657. Next, TransCanada contends that the California Parties wrongly use footnote four in *Morgan Stanley* to allege that Respondents face liability because of the market manipulation during the Crisis. TransCanada asserts that the California Parties' interpretation of footnote four would weaken prior *Mobile-Sierra* case law stating that the

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[2355] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[2356] *United Gas Pipe Line Co. v. Mobile Gas Servs. Corp.*, 350 U.S. 332, 338, 344 (1956).

[2357] California Parties Initial Br. at 130 n.580 (quoting *FPC v Texaco, Inc.*, 417 U.S. 380, 399 (1974)).

[2358] *Morgan Stanley*, 554 U.S. at 551.

[2359] *Morgan Stanley*, 554 U.S. at 551 n.6.

*Mobile-Sierra* presumption is "practically insurmountable."[2360] TransCanada states that the majority in *Morgan Stanley* rejected the dissent's broad assertion that "nothing in the FPA or this Court's cases precludes FERC from considering circumstances exogenous to contract negotiations, including natural disasters and market manipulation by entities not parties to the challenged contract."[2361] Rather, the *Morgan Stanley* opinion held that "circumstances exogenous to contract negotiations, including natural disasters and market manipulation by entities not parties to the challenged contract … are relevant to whether the contracts impose an 'excessive burden' on consumers relative to what they would have paid absent the contracts."[2362] Thus, exogenous circumstances cannot be an independent ground for vitiating the application of *Mobile-Sierra*, as the dissent advocated. TransCanada concludes that circumstances exogenous to contract formation, such as market manipulation of third parties and natural disasters, would be relevant only to the determination of what the rates would have been without the contracts at issue "further down the line, when the open market was no longer dysfunctional" because accounting for such factors would enable the Commission to determine the appropriate baseline from which to measure the rate disparity.[2363] TransCanada contends that the California Parties made no attempt to quantify rate impacts they would have experienced without the contracts at issue, separate and apart from the impact of exogenous circumstances

1658. TransCanada argues that the California Parties' interpretation of *Morgan Stanley* would punish sellers who do nothing wrong, which the courts and Commission have found would undermine the reliance on bilateral contracts that the *Mobile-Sierra* presumption is intended to protect.[2364] TransCanada asserts that sellers would be deterred from dealing with entities that present risks, such as CERS, in the future.

1659. Next, TransCanada avers that the case law cited by the California Parties does not support their conclusion that the *Mobile-Sierra* presumption should be overcome in this proceeding. TransCanada states that the cases cited by the California Parties generally

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[2360] *Papago Tribal Util. Auth. v. FERC*, 723 F.2d 950, 954 (D.C. Cir. 1983) (Scalia, J.); *see also Kansas Cities v. FERC*, 723 F.2d 82, 87-88 (D.C. Cir. 1983).

[2361] *Morgan Stanley*, 554 U.S. at 567 (Stevens, J., dissenting).

[2362] *Id.* at 549 n.4 (citation omitted).

[2363] *Id.* at 552-53.

[2364] *Id.* at 547-48.

fall into three categories: (1) cases involving affiliates;[2365] (2) cases presented following industry-wide reform and/or concurrent with Commission rulemakings;[2366] and (3) cases that pre-date *Morgan Stanley* or are otherwise facially distinguishable.

1660. TransCanada also contends that the California Parties improperly rely on language in *Northeast Utilities* stating that the D.C. Circuit's statement that the public interest standard is "practically insurmountable" may not apply in all circumstances.[2367] TransCanada states that the First Circuit's entire analysis in *Northeast Utilities* is based upon a proposition that there is a "public interest standard" that is separate and apart from the "just and reasonable standard."[2368] TransCanada notes that the Supreme Court stated unequivocally in *Morgan Stanley* that the public interest standard is not an exception to the just and reasonable standard and is not a standard independent of the just and reasonable standard.[2369]

1661. With respect to *Public Service Co. of New Hampshire*, TransCanada states that the California Parties cite to this order for the proposition that the Commission can modify the terms of a contract if "third parties may be harmed."[2370] However, TransCanada asserts that the language is mere *dicta* given that the Commission determined that it would amend the contract at issue "[r]egardless of whether the Commission is bound by a public interest standard of review, or by a just and reasonable standard of review."[2371]

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[2365] *Miss. Indus. v. FERC*, 808 F.2d 1525, *different holding vacated in part on other grounds per curiam*, 822 F.2d 1104 (D.C. Cir. 1987); *Ne. Util. Serv. Co. v. FERC*, 55 F.3d 686 (1st Cir. 1995) (*Northeast Utilities*).

[2366] *Texaco Inc. v. FERC*, 148 F.3d 1091 (D.C. Cir. 1998) (the application of Order No. 636); *Transmission Access Policy Study Grp. v. FERC*, 225 F.3d 667 (D.C. Cir. 2000) (involving Commission orders issued in the context of a rulemaking); *ISO New England Inc.*, 143 FERC ¶ 61,150 (2013) (concerning Order No. 1000).

[2367] *Northeast Utilities*, 55 F.3d at 691.

[2368] *Id*.

[2369] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 535 (2008); *see also NRG Power Mktg., LLC v. Me. Pub. Util. Comm.*, 558 U.S. 165, 168, 174-75 (2010).

[2370] *Pub. Serv. Co. of N.H. v. N.H. Elec. Coop., Inc.*, 83 FERC ¶ 61,223 (1998).

[2371] *Id.* at 61,993.

Additionally, TransCanada notes that the order predates *Morgan Stanley* and *NRG Power Marketing* which make clear that the public interest standard is not independent of the just and reasonable standard.

1662. Further, TransCanada states that the California Parties rely on *Arizona Corporation Commission* for the proposition that "generalized findings of public interest [are sufficient] when intervening circumstances affect a class of contracts *in the same manner*."[2372] TransCanada argues that the California Parties ignore that the harm to the public interest was that continued enforcement of the terms of the settlements at issue jeopardized service to customers on the system. Lastly, TransCanada notes that the D.C. Circuit in *TAPS* and the Commission in *ISO New England* later dismissed the proposition that it is appropriate to rely on generic public interest allegations in challenging individual bilateral contracts.

**(b) Evidence of Excessive Burden on Consumers**

1663. TransCanada argues that the California Parties improperly seek to overcome the *Mobile-Sierra* presumption through broad pronouncements concerning the California Energy Crisis and the alleged burden the high prices imposed on consumers. TransCanada contends that the California Parties ignored the direction by the Commission and the Supreme Court that the *Mobile-Sierra* analysis is to be conducted on a contract-by-contract basis and instead rely on aggregated harm.

1664. With respect to the California Parties' reliance on $5 billion of aggregate harm, TransCanada asserts that this figure includes the prices paid to sellers that had settled and sellers who have never been subject to legal claims of unlawful activity by the California Parties. TransCanada avers that accepting the California Parties' arguments based on this aggregated figure would punish TransCanada based upon the impact of others' sales, a result the Commission has rejected.[2373] TransCanada also notes that some of the $5 billion was paid to California municipalities, and the benefits of those revenues enjoyed by California's citizens is not considered or quantified by the California Parties.

1665. Additionally, TransCanada contends that the California Parties did not quantify the amount of harm attributable to any misconduct by any specific party. TransCanada avers that the California Parties argument ignores the Commission's and the Supreme Court's holdings that high prices alone are neither evidence of market manipulation nor

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[2372] *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 955-56 (D.C. Cir. 2005).

[2373] *See* Order on Rehearing at PP 26, 30.

sufficient to overcome the *Mobile-Sierra* presumption.[2374] Additionally, TransCanada asserts that it is unreasonable to presume that all high prices in the Pacific Northwest were the consequence of alleged market manipulation.[2375]

1666. Next, TransCanada argues that the California Parties' argument of aggregated harm also fails to distinguish the impact of exogenous circumstances from any alleged impact attributable to a specific contract.[2376] TransCanada notes that despite admitting that scarcity factored into the Pacific Northwest prices, the California Parties failed to demonstrate an "excessive burden" associated with any particular contract independent of exogenous circumstances.

1667. TransCanada avers that allowing exogenous factors to trump *Mobile-Sierra* protection would mean that *Morgan Stanley's* focus on individual contracting parties' conduct and the specific pricing of a contract would be swallowed by the exogenous circumstances exception. TransCanada asserts that this would also dissuade smaller suppliers from attempting to remedy scarcity conditions. For example, although claims against TransCanada contribute less than one percent to the California Parties' total claim amount, the California Parties allege TransCanada is liable on the basis of the sales made by much large participants.

1668. TransCanada also contends that the California Parties generalize market manipulation argument ignores instances where the alleged manipulation may have lowered prices.[2377] For example, the Commission has recognized that some trading schemes may involve depressing prices in one product or market in order to increase prices and profits in another product or market.[2378]

1669. Next, TransCanada argues that the California Parties improperly rely on the testimony of Commissioner Florio. TransCanada states that Commissioner Florio's

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[2374] *Morgan Stanley*, 554 U.S. at 548; Order Granting Interlocutory Appeal at P 15.

[2375] *Morgan Stanley*, 554 U.S. at 540 (quoting *Cal. for Renewable Energy, Inc. v. Sellers of Energy & Ancillary Servs.*, 119 FERC ¶ 61,058, at 61,243, 61,246 (2007)).

[2376] *Morgan Stanley*, 554 U.S. at 549 n.4.

[2377] Tr. 3736:7-12 (Morris).

[2378] *See Brian Hunter*, 135 FERC ¶ 61,054, at P 11 (2011).

testimony involving a different time period, when TransCanada was not selling energy in the Western United States.

1670. TransCanada also asserts that it has demonstrated that its transactions with CERS benefited California's consumers. TransCanada notes that the average price that TransCanada charged was lower than the weighted average price that CERS paid to other sellers, which reduced the average price that CERS paid for power during the CERS Period.[2379] Furthermore, TransCanada notes that even using the MMCP as a benchmark, CERS's acquisition costs were only *one half of one percent higher* (i.e., 0.5 percent) under all actual contracts negotiated with TransCanada than they would have been using the MMCPs, resulting in an actual rate impact of approximately one one-hundredth of a percent (i.e., 0.01 percent).[2380]

1671. Lastly, TransCanada argues that if the contracts are abrogated, the result would be unfavorable to consumer interests in the long-run. TransCanada notes that because sellers have no obligation to transact with CERS, suppliers may withdraw from the market under similar circumstances, resulting in more scarcity and even higher prices.

### (c) Response to Dr. Berry's Testimony

1672. TransCanada contends that the California Parties improperly rely on Dr. Berry's testimony and exhibits to overcome the *Mobile-Sierra* presumption. TransCanada asserts that the California Parties ignore the actual contractual arrangements between CERS and TransCanada. TransCanada states that it did not transact with the CAISO, it did not sell firm energy,[2381] and its contracts with CERS did not impose the same standard of review as contracts under the ISO tariff.[2382] TransCanada also notes that Dr. Berry's contentions ignore the fact that the State of California created CERS as an entity separate and apart

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[2379] Tr. 2503:1-5 (Taylor); s*ee also* Tr. 2502:21-25 (Taylor); Ex. TRC-1 at 8:17-19; Ex. TRC-195.

[2380] Ex. TRC-1 at 165:5-17.

[2381] The ISO had tariff requirements during the CERS Period directing that all power sold to it be firm. *See* Ex. CAT-147 at 69.

[2382] The ISO tariff, which incorporated a *Memphis* clause, results in materially different commercial arrangements than that the WSPP Agreement. Thus, the *Mobile-Sierra* presumption did not apply to the OOM transactions with the ISO. *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 142 FERC ¶ 63,011, at PP 104-112.

from the ISO. TransCanada concludes that there is no basis to claim that the mitigated ISO OOM purchases were the "exact same" as TransCanada's sales to CERS.

1673. TransCanada also contends that Dr. Berry's assertion that no seller justified costs above the MMCP is misleading. TransCanada states that the case that the California Parties cite applied the mitigation to sales from June 20, 2001 forward, making this cap inapplicable to the sales by TransCanada at issue here.[2383] Additionally, the order gave "sellers other than marketers the opportunity to justify prices above the market clearing price."[2384] Thus, TransCanada, as a marketer, would not even have had an opportunity to "cost-justify higher prices" as suggested by the California Parties.

### (d) Evidence of Third Party Manipulation

1674. TransCanada states that the California Parties also relied on material sponsored by Dr. Berry regarding various consent agreements and other documents relating to third parties' behavior in an attempt to show that the market was not competitive, and that therefore, the *Mobile-Sierra* presumption should not apply. As noted above, TransCanada states that the bad acts of third parties are insufficient to overcome the *Mobile-Sierra* presumption.[2385] Additionally, TransCanada notes that the Commission stated that an "analysis of a general link between the dysfunctional spot market in California and the Pacific Northwest spot market is not adequate to establish a causal connection between a particular seller's alleged unlawful activities and the specific contract negotiations."[2386]

1675. Furthermore, TransCanada argues that the California Parties provided no evidence as to what the "but for" contract rates would have been, absent the contracts of TransCanada and the other Respondents. TransCanada states that the only evidence in the record as to what prices CERS would have obtained if they had rejected all of the Respondents' contracts is $500/MWh from their supplier of last resort,[2387] or as much as

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[2383] *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 95 FERC ¶ 61,418, at 62,548.

[2384] *Id.* at 62,547.

[2385] *See* Order on Rehearing at P 26.

[2386] Order on Remand at P 21.

[2387] Ex. TRC-1 at 126:4-6 (citing Ex. CAT-12 at 19:18).

$3,300 in the Pacific Northwest,[2388] or as much as $1,294/MWh from municipalities within the State of California itself.[2389] TransCanada asserts that the evidence of bad acts by third parties would be relevant to an argument involving what prices would have been "but for" the challenged contract, but the California Parties failed to actually provide any relevant information.

1676. Lastly, TransCanada contends that even if bad acts of third parties were legally cognizable, the evidence submitted is unpersuasive and largely inapplicable to the Pacific Northwest spot market. TransCanada states that the California Parties' evidence generally falls into three categories: (1) activity that did not take place during the CERS Period; (2) activity that took place outside of the Pacific Northwest electric energy spot market; and (3) activity that was alleged in settlements that had no precedential effect and in which the parties admitted to no wrongdoing.

### 8. Commission Trial Staff Reply Brief

1677. Trial Staff states that the California Parties ignore the legal standards mandated by the Commission and fail to demonstrate that the contracts at issue impose an excessive burden on consumers or seriously harm the public interest. Trial Staff asserts the California Parties make broad and general claims about high prices and market dysfunction despite the Commission's clear directives otherwise.[2390]

1678. Trial Staff notes that the Supreme Court also stated that "the mere fact that the market is imperfect, or even chaotic, is no reason to undermine the stabilizing force of contracts that the FPA embraced as an alternative to purely tariff-based regulation."[2391] Lastly, Trial Staff states that in the Order on Rehearing, the Commission rejected an argument that it "should permit evidence that the rates, as a whole, imposed an undue burden on the public," finding that "Cal[ifornia] Parties' claims of uniformly higher prices amount to little more than a variation on claims of general market dysfunction,

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[2388] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 541 (2008).

[2389] Ex. TRC-157; *see also* Ex. TRC-158 through TRC-160.

[2390] Order on Remand at P 21; Order Granting Interlocutory Appeal at P 15.

[2391] *Morgan Stanley*, 554 U.S. at 547-48.

which have been previously rejected by the Supreme Court as a basis for overcoming *Mobile-Sierra*."[2392]

1679. Trial Staff also contends that the Professor Berck's analysis does not measure any actual harm or address the circumstances in California as they actually exist. Instead, Professor Berck measured the hypothetical harm that would have occurred had the State of California immediately passed through to consumers the amount of alleged overcharges. Trial Staff avers that because Professor Berck does not measure the impact of this reality, the California Parties have failed to provide any evidence explaining why contract abrogation is an "unequivocal public necessity."[2393]

1680. Next, Trial Staff argues that the California Parties inappropriately expand the scope of the excessive burden inquiry to general allegations of market dysfunction. Trial Staff states that the California Parties examine "the Crisis" rather than address the specific contracts at issue. Trial Staff asserts that the California Parties cite to testimony covering events in San Diego that occurred prior to the CERS Period. Trial Staff notes that this period, involving different circumstances, was already subject to litigation in Docket No. EL00-95-248. Trial Staff contends that expanding the scope in this manner is directly contrary to the Commission's orders rejecting claims based on general market dysfunction and high prices.

1681. Trial Staff further notes that the California Parties assert that Commissioner Florio's testimony went unchallenged. However, Trial Staff avers that the reason why the testimony was unchallenged was because it is entirely irrelevant to the standard mandated by the Commission – whether specific contract rates at issue impose an excessive burden on consumers or seriously harm the public interest.[2394]

1682. Next, Trial Staff asserts that the cases cited by the California Parties are not analogous to the current proceeding. Trial Staff states that the cases cited demonstrate that the Commission has authority to abrogate contracts under the public interest standard when there is evidence linking an excessive burden or public harm to a particular contract. Trial Staff argues that the California Parties provided no evidence showing actual harm or linking such harm to the contracts at issue.

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[2392] Order on Rehearing at PP 28, 30 (citing *Morgan Stanley* 554 U.S. at 548).

[2393] *Morgan Stanley* 554 U.S. at 550.

[2394] *See* Order Granting Interlocutory Appeal at P 15.

1683. Trial Staff states that in *Mississippi Industries v. FERC*, the Commission reformed a System Agreement and a United Power Sales Agreement (UPSA) that created an unequal allocation of costs among the operating companies, and as a result, harmed consumers.[2395] Trial Staff asserts that unlike the evidence in this proceeding, in *Mississippi Industries* the Commission identified a harm and directly linked that harm to two clearly identifiable contracts. Trial Staff also avers that the California Parties have made no effort to isolate other possible causes of the harm in this proceeding, such as supply and demand conditions.[2396] Additionally, Trial Staff notes that *Mississippi Industries* involved an allocation issue, which is not related to this proceeding.

1684. Next, Trial Staff states that in *Northeast Utilities Service Co. v. FERC*, the First Circuit upheld the Commission's modification of a singular wholesale electric power contract, which it was presented with for the first time, to protect the interests of non-parties.[2397] Trial Staff asserts that the Commission identified particular provisions of the contract that were overly favorable to the company due to a lack of arms-length negotiations because the parties that negotiated the contract were about to merge and assume identical interests.[2398] Trial Staff notes that these circumstances are clearly distinguishable to the contracts at issue here.

1685. Trial Staff also maintains that *Transmission Access Policy Study Group v. FERC* (*TAPS*) involved a Commission determination that where "intervening circumstances" affect an entire class of contracts in an identical manner, the Commission can make a public interest finding applicable to all contracts of that class.[2399] In *TAPS*, the D.C. Circuit upheld the Commission's finding that open access transmission reform implemented by Order No. 888 could result in stranded costs for utilities that entered into contracts with an expectation of continued service to a particular customer, and therefore, it was appropriate to reform contracts that fell into that class.

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[2395] *Miss. Indus. v. FERC*, 808 F.2d 1525, 1528-1529, 1533 (D.C. Cir. 1987), *different holding vacated in part on other grounds*, 822 F.2d 1104 (D.C. Cir. 1987).

[2396] Ex. S-15 at 20:7-15.

[2397] *Ne. Utils. Serv. Co. v. FERC*, 55 F.3d 686, 692 (1st Cir. 1995).

[2398] *Id.*

[2399] *Transmission Access Policy Grp. v. FERC*, 225 F.3d 667, 710 (D.C. Cir. 2000).

1686. Trial Staff argues that the California Parties wrongly attempt to equate the intervening circumstances in *TAPS* to the market conditions that caused high prices during the CERS Period. Trial Staff first notes that market conditions are not an "intervening circumstance" as that term is used in *TAPS* because the market conditions predate the contracts. Additionally, as noted above, the Supreme Court and the Commission have made clear that a showing of uniformly high rates or general market dysfunction is not enough to abrogate contracts.[2400] Lastly, Trial Staff asserts that in *TAPS*, the Commission required parties seeking relief to show actual harm and link that harm to the contract involved.[2401]

1687. Trial Staff contends that the remaining cases cited by the California Parties involve circumstances not present in this proceeding, such as modifications to contracts necessary to enforce specific policy initiatives issued by the Commission after the contracts were formed[2402] or a challenge to a specific provision of a contract due to intervening circumstances.[2403]

1688. Next, Trial Staff avers that the California Parties misunderstand the testimony of Trial Staff witness Ms. Radel and fail to refute her central conclusions. Trial Staff argues that contrary to the California Parties statements, Ms. Radel never suggested that the issuance of bonds rendered the burden on consumers less excessive. Trial Staff states that Ms. Radel's testimony concerning the issuance of bonds was in response to the California Parties' assertion that the issuance of bonds in and of themselves indicated an excessive burden on consumers.[2404] Trial Staff states that Ms. Radel in the only witness in this proceeding that calculates what the California ratepayers would have paid if the rates had been passed through immediately, and still finds that the burden is not excessive.[2405]

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[2400] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548 (2008); Order on Rehearing at PP 28, 30.

[2401] *TAPS*, 225 F.3d at 683.

[2402] *Texaco Inc. v. FERC*, 148 F.3d 1091, 1094-95 (D.C. Cir. 1998); *ISO New England, Inc.*, 143 FERC ¶ 61,150, at PP 160-98 (2013).

[2403] *Ariz. Corp. Comm'n v. FERC*, 397 F.3d 952, 954-55 (D.C. Cir. 2005).

[2404] Ex. S-15 at 20:16-18.

[2405] *Id.* at 21:17-22:8.

1689. Trial Staff asserts that this misunderstanding of Ms. Radel's testimony led to the California Parties' claim that Ms. Radel "backtracked" on her position that spreading the cost over twenty years decreased the burden. Rather, as explained above, Trial Staff states that Ms. Radel never made such an assertion.

1690. With respect to the California Parties' contention that Ms. Radel admitted that immediate pass-through of $5 billion would have burdened California's economy, Trial Staff argues that, as explained by Ms. Radel on redirect, in order to find that $5 billion would have created an undue burden, one must assume that the $5 billion were "overcharges" and that "there was something wrong in the market"—two assumptions that Ms. Radel took issue with.[2406]

1691. Trial Staff argues that the California Parties attempt to shift the burden to Trial Staff to prove the absence of an undue burden. Trial Staff asserts that the purpose of Ms. Radel's testimony was to point out the fact that the California Parties' case does not even attempt to measure actual harm caused by the contracts at issue.[2407]

1692. Lastly, Trial Staff contends that the contracts at issue benefited the public interest. Trial Staff states that California needed energy during the CERS Period to avoid blackouts and the Respondents provided that energy despite no legal obligation to do so.[2408] Trial Staff states that Respondents provided CERS power at the locations where it was need most despite the fact that it would have been far less risky to do nothing.[2409] Trial Staff avers that if the California Parties' allegations regarding high prices and market dysfunction are enough to demonstrate an excessive burden and trigger refunds, then parties would be discouraged from participating in the market when prices reach a certain threshold due to high demand and low supply, which is precisely the time when market participation is most needed. Thus, Trial Staff concludes that upholding the contracts in this case would be consistent with the Supreme Court's reasoning in *Morgan Stanley*, which recognized the "important role of contracts in the FPA" as a "key source of stability."[2410]

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[2406] Tr. 4184:9-20 (Radel).

[2407] Ex. S-15 at 22:5-8.

[2408] Ex. CAT-161 at 85:14-86:2; Ex. TRC-1 at 126:1-19.

[2409] *See, e.g.*, Tr. 3513:3-3514:16 (Harrigan).

[2410] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 551 (2008).

## B. Findings and Conclusion

### 1. The California Failed to Demonstrate that TransCanada's Sales to CERS Imposed an Excessive Burden on Consumers or Seriously Harmed the Public Interest

1693. The sales made by TransCanada to CERS were individually negotiated bilateral transactions governed under the Western Systems Power Pool (WSPP) Agreement.[2411] Numerous buyers and sellers transacted under the WSPP Agreement, as demonstrated by the list of approximately 200 signatories included with the WSPP Agreement.[2412] Further, the Commission has specifically held that the WSPP Agreement demonstrates the "intent that neither seller nor buyer be able to seek changes under section 205 or 206 of the FPA other than under the 'public interest' standard of review."[2413] As previously explained, absent probative evidence of specific seller unlawful market activity at the contract formation stage, as discussed under Issue1(A) *supra*, "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law."[2414] The presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*.[2415]

1694. *Morgan Stanley* requires that the California Parties demonstrate "*extraordinary circumstances*" involving "*unequivocal public necessity*" because the contract "*seriously harms*" the public interest in order to overcome *Mobile-Sierra*,[2416] but the California Parties fail to make any effort to quantify the alleged "harm" imposed by any contract between TransCanada and CERS under the standards required by *Morgan Stanley*. Instead, they claim that the *Mobile-Sierra* presumption should be overcome based upon

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[2411] Ex. TRC-77 at 13:8; Ex. CAT-041 at 111:1-4.

[2412] Ex. CAT-124 at 108-10 (attachment to WSPP Agreement listing members). *See also* Tr. 3173:2 (Morter) (agreeing that there were "a lot" of WSPP members).

[2413] *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at P 36 (2003). *See also* Order on Remand at P 20; Order on Rehearing at P 13.

[2414] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[2415] *Id.*

[2416] *Id*. at 530, 534, 547, 550 (emphasis added).

their allegations that "the extremely high rates that the contracts imposed on consumers seriously harmed the public interest."[2417] They also seek to lump TransCanada in with all Respondents claiming that "Respondents' rates … burdened consumers during the CERS Period" and that the "additional charges on each consumer's electric bill that continue to this day" serve as "evidence" of the "serious harm" imposed by all Respondents.[2418]

1695. Specifically, the California Parties rely on an aggregated estimate that the cost of supplies CERS purchased was too high by $5 billion.[2419] Reliance on the $5 billion aggregate number is insufficient standing alone to support abrogation of the subject bilateral contracts between CERS and TransCanada for a number of reasons. First, the $5 billion figure includes the prices paid to other sellers that have settled and are no longer one of the two remaining Respondents in this phase of the proceeding. Many of those sellers have entered into significant monetary settlements with the California Parties and yet there has been no attempt to offset or recognize the benefits of those settlements by means of an adjustment to its $5 billion aggregate number. Further, this aggregate figure includes prices paid to sellers who have never been subject to legal claims of unlawful activity by the California Parties, such as municipalities within California and Seattle City Light.

1696. Acceptance of the California Parties' arguments based on this aggregated figure would result in the abrogation of TransCanada's contracts with CERS based upon the impact of *others'* sales, a result the Commission has clearly rejected.[2420] Thus, in order to demonstrate an undue burden, the California Parties must demonstrate that the contracts from a *particular seller* impose an undue burden on consumers or seriously harm the public interest.[2421]

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[2417] California Parties Initial Br. at 18.

[2418] California Parties Initial Br. at 18-19.

[2419] *See, e.g.*, California Parties Initial Br. at 150 (citing Ex. CAT-267 at 4). The California Parties also introduced evidence concerning the alleged overcharges by all Respondents in this case as of September 21, 2012. Ex. CAT-267 at 4. However, as with the $5 billion aggregate number, this figure also includes alleged overcharges by settled parties, specifically, Powerex, TransAlta and the Avista Entities.

[2420] *See* Order on Rehearing at PP 26, 30.

[2421] Respondents argue that *Morgan Stanley* requires that a single contract impose an excessive burden on consumers in order to overcome the *Mobile-Sierra* presumption. However, given the fact that spot-market contracts are for such a short duration, it would

(continued…)

### (a) TransCanada's Rates to CERS Were In Line with Those of Other Customers

1697. First it must be noted that TransCanada's hourly sales volume to CERS typically ranged between 17 MWh to 50 MWh[2422] in an hourly market in which total volume could exceed 3,900 MWh.[2423] Given this record evidence, TransCanada's sales cannot be considered "enormous in volume" relative to other purchasers[2424] and do not support allegations that TransCanada had or exercised market power to obtain or maintain extremely high non-competitive market rates. This finding is supported by the fact that Dr. Fox-Penner takes issue with only 26 hours of the 2,610 hourly sales transactions between TransCanada and CERS during the CERS Period.[2425] As Dr. Fox-Penner showed in Exhibit CAT-163, TransCanada made spot sales in the Pacific Northwest to parties other than CERS in just 14 of the 2,610 hourly sales during the CERS Period.[2426] There are only four hours when CERS paid at least $50/MWh *more* than other TransCanada customers, but these sales occurred for what Dr. Fox-Penner admitted were not comparable durations.[2427] However, there were also four hours when CERS paid

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be essentially impossible to overcome the *Mobile-Sierra* presumption with respect to an individual spot market contract. Thus, Respondents' interpretation of *Morgan Stanley* would effectively eliminate the Commission's ability to ensure that spot market contracts do not seriously harm the public interest. Such an interpretation would be in direct conflict with the Court's statement in *Morgan Stanley* that "the FPA intended to reserve the Commission's contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 551 (2008); *see also United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344 (1956) ("contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest").

[2422] Ex. TRC-77 at 49:15-17; *see also* Ex. TRC-221.

[2423] *See* Ex. TRC-82 at 136 (total of 3,965 MWh in hour ending 24).

[2424] The California Parties improperly characterize TransCanada's sales to CERS as "enormous in volume" relative to other purchasers. California Parties Initial Br. at 39, n.143.

[2425] California Parties Initial Br. at 54.

[2426] Ex. CAT-163 at 121 ("Total Matched Transactions: 14").

[2427] Ex. CAT-163 at 87, 113; *see* TransCanada Initial Br. at 48-49.

$50/MWh *less* than other TransCanada customers.[2428] Of the remaining six hours, CERS paid essentially the same price ($0.47/MWh) less than other TransCanada customers in five of the hours.[2429] These findings are relevant to the issue of "excessive burden" inasmuch as they demonstrate that TransCanada's rates to CERS were in line with those of other customers. In fact, the record evidence shows that "TransCanada's prices were typically below the average price that CERS paid at COB and about 49 percent of the time the lowest price that CERS paid at COB."[2430]

**(b) Profit Margins, Standing Alone, Do Not Equate to a Showing that Contract Rates Impose an Excessive Burden on Consumers or Seriously Harm the Public Interest**

1698. While the record reflects that TransCanada's contract prices with CERS were often well below the average prices CERS paid in the spot market at COB during the CERS Period,[2431] the California Parties continue to assert that TransCanada was earning "unconscionable margins" in its sales to CERS.[2432] More specifically, relying primarily on Mr. Taylor's testimony, the California Parties assert that TransCanada was buying low in the PPoA Canadian market and then realizing unconscionably high profit margins by selling that energy to CERS.[2433]

1699. Mr. Taylor asserts that settled energy prices in the PPoA over the entire course of the CERS Period averaged approximately $80/MWh.[2434] Based upon that estimate,

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[2428] Ex. CAT-163 at 110.

[2429] *Id*.

[2430] Ex. TRC-1 at 8:15-19.

[2431] Tr. 2503:1-5 (Taylor)

[2432] California Parties Initial Br. at 40.

[2433] *See* California Parties Initial Br. at 21 ("[t]he essence of the California Parties' 'duress, fraud, or bad faith' claim is that each Respondent exploited CERS by charging a price far above the competitive market levels and well above the prices that Respondents charged other buyers, because Respondents knew that CERS, which was required to obtain the energy critical to reliable ISO operation, lacked reasonable alternatives.").

[2434] California Parties Initial Br. at 38 n.139 (citing Tr. 2922:1-8 (Taylor)).

which TransCanada observes cannot be replicated from data in the record,[2435] the California Parties make an assumption that TransCanada earned excessive margins based on the difference between their estimated $80/MWh average PPoA price and TransCanada's sales prices to CERS. However, Mr. Taylor's estimate of, and reliance on, an average settled price of energy in the PPoA is highly speculative and fundamentally flawed in that it ignores critical factual circumstances surrounding the transactions between CERS and TransCanada.[2436] Furthermore, an analysis based on average prices fails to reflect the volatility of the PPoA market and the price risk associated with purchases in the PPoA.[2437] By their very nature, average prices diminish or hide the minute-by-minute volatility of prices that occurred in the PPoA market during the CERS Period, where prices ultimately are set on an hourly basis. As a result, (1) there were instances in which TransCanada sold at a loss[2438] and (2) other instances in which forecasted PPoA pricing that was available to TransCanada at the time it agreed to a sales price with CERS reflected prices substantially in excess of the levels estimated by Mr. Taylor.[2439]

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[2435] The $80/MWh figure that the California Parties rely upon is only found in the testimony of Mr. Taylor when presenting Exhibit CAT-662 on redirect. The $80/MWh figure, however, was a rough estimate that Mr. Taylor provided by eyeballing the graph lines on Exhibit CAT-662, stating "you can pretty well estimate the average price in the Alberta Power Pool was something on the order of maybe $80." Tr. 2922:6-8 (Taylor). Mr. Taylor's rough estimate of $80/MWh cannot be replicated from the available data in the record.

[2436] For example, Mr. Taylor admitted that he was not familiar with the rules of the PPoA, did not do any assessment of the risks the parties may have encountered as a result of transacting in the PPoA, and had no evidence to support his allegation that the price in the PPoA at the time of the transactions was around $100 or $200 as he claimed. *See* Tr. 2371:13-2372:3, 2406:15-2407:13 (Taylor). *See also* Ex. TRC-225 (showing PPoA hourly prices as high as approximately $568 for hour ending 13); Ex. TRC-226; Ex. TRC-231 (showing PPoA hourly prices as high as approximately $490 for hour ending 10). *See also* Tr. 2444:16-2445:10 (Taylor). Further, Mr. Taylor made no attempt to investigate TransCanada's overhead expenses or opportunity costs. Tr. 2494:24-2495:14, 2496:6-2497:5 (Taylor).

[2437] Ex. TRC-77 at 7:1-6.

[2438] Ex. TRC-225; Ex. TRC-231.

[2439] Ex. TRC-226; *see also* Ex. TRC-225; Ex. TRC-231. The forecasted price is shown by the yellow line in these exhibits.

1700. Moreover, and more importantly, simply comparing the price TransCanada paid for energy to the ultimate sales price to CERS, even assuming that such a comparison demonstrates that TransCanada earned substantial profits from its sales to CERS, is insufficient, standing alone, to abrogate the subject contracts. *Morgan Stanley* makes clear that bilateral, market-based contracts should not be voided on the basis of gross margins as that would be "a reinstitution of cost-based rather than contract-based regulation."[2440]

1701. Further, absent evidence of unlawful market activity at the contract formation stage, assertions by the California Parties that TransCanada should have refused to sell energy to CERS at prices comparable to other market participants simply because they may have been able to buy that energy at lower prices in the Canadian market are nonsensical. While the record reflects that many sellers did refuse to do business with CERS even at very high market prices, they did so primarily because of concerns associated with being paid, not out of concern that high prices were creating an excessive burden on consumers.[2441] Presumably, CERS agreed to buy energy from TransCanada because TransCanada's prices were equal to or less than other sellers in the market at the time and to prevent the greater burden to consumers associated with blackouts.

1702. The correct inquiry to *overcome* the *Mobile-Sierra* presumption of just and reasonable rates applicable to the wholesale bilateral Pacific Northwest spot market energy contracts between TransCanada and CERS that the California Partis now seek to abrogate in this proceeding is not whether TransCanada optimized an opportunity to maximize its profits during the Western Energy Crisis, but whether the contract rates arising from those transactions impose "an excessive burden on consumers" or "seriously harm[] the public interest." Absent evidence of unlawful market activity during the contract formation stage, as discussed under Issue 1(A), factors such as contract rates relative to other market participants at the time, contract volumes, and duration of the contracts must also be considered. The evidence of record reflects that TransCanada prices to CERS were below the weighted average price CERS paid to its other sellers.[2442]

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[2440] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 550 (2008).

[2441] Some sellers would not accept the possibility of future appropriations as sufficient security and assurance of payment. Ex. CAT-016 (including an April 1, 2001 email from Pete Garris to Ray Hart, listing twenty-two sellers refusing to do business with CERS); Ex. SNA-12 (Hart discovery response); *see also* Ex. CAT-415 (chart showing which sellers were not selling to CERS).

[2442] Tr. 2502:21-25 (Taylor); *see also* Ex. TRC-194; Ex. TRC-195.

Specifically, "TransCanada's prices were typically below the average price that CERS paid at COB and about 49 percent of the time the lowest price that CERS paid at COB."[2443] Further, the record reflects that TransCanada was typically selling between 13 MWh and 50 MWh in an hourly market in which total volume could exceed 3,900 MWh.[2444] Most importantly, even if all TransCanada sales are aggregated, the record reflects that CERS's acquisition costs were only one half of one percent higher under the actual contracts negotiated with TransCanada than they would have been had the transactions taken place at the MMCP level advocated as a benchmark by the California Parties.[2445] Based on these findings, the subject contract rates do not impose "an excessive burden on consumers" or "seriously harm the public interest."

**(c) The MMCP Is Not an Appropriate Benchmark for Use in the Pacific Northwest**

1703. The California Parties argued in their Initial Brief that the prices of TransCanada's (and all other Respondents') sales across the market should be reset to the MMCP levels established in Docket No. EL00-95.[2446] However, for the reasons discussed *supra*, the MMCP is not an appropriate benchmark for use in this proceeding.[2447] As explained in the California Respondents' Initial Brief:

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[2443] Ex. TRC-1 at 8:15-19.

[2444] *See* Ex. TRC-82 at 136 (total of 3,965 MWh in hour ending 24).

[2445] *See* Ex. TRC-1 at 165:5-10. *See also* Ex. TRC-1 at 165:16-17. TransCanada notes that the actual rate impact is approximately one one-hundredth of a percent (i.e., 0.01 percent).

[2446] California Parties Initial Br. at 169-72.

[2447] Specifically, the MMCP was an equitable relief remedy construct and not developed to measure undue burden on consumers or harm to the public interest. Further, the MMCP was calculated based on the marginal costs of the last unit dispatched to meet load in the CAISO's real-time market. The Commission explained that the reason why the CAISO's OOM purchases were being mitigated to the MMCP level was because the OOM purchases were inextricably linked to the sales from the California organized markets. *See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 96 FERC ¶ 61,120, at 61,516 (2001). The Commission has made no such finding with respect to the sales to CERS in the Pacific Northwest.

> (1) [T]here is no evidence that the MMCP levels based upon the marginal costs of *California generators* bear any relationship to Respondents' costs for sales in the Pacific Northwest; (2) the California Complainants themselves have previously argued that the Pacific Northwest is a different market than California; and (3) Dr. Berry failed to account for any of the differences between the two markets, including those that the Commission has repeatedly recognized.[2448]

1704. In the Order on Remand, the Commission specifically discussed the fundamental differences between the California organized markets and the Pacific Northwest bilateral market.[2449] Specifically, the Commission noted that "short-term bilateral contract sales to CERS are unlike sales in an organized auction market, such as the CAISO or CalPX, where a tariff violation by any party that produces an unlawful rate for that party also causes all sellers to receive that unlawful rate."[2450] Thus, in the Order on Remand, the Commission concluded that "*the [MMCP] approach taken in the California refund proceeding would not be appropriate here*."[2451]

1705. Furthermore, TransCanada's contracts with CERS did not impose an excessive burden on consumers even under the California Parties' theory of the case. This point is evidenced ironically by reference to the MMCP approach California Parties Witness Berry erroneously posits. The evidence shows that CERS's acquisition costs were only *one half of one percent higher* (i.e., 0.5 percent) under all actual contracts negotiated with TransCanada than they would have been using the MMCPs Dr. Berry advocates.[2452] Furthermore, when the actual rate impact is calculated, the rate impact of TransCanada's sales to CERS presuming MMCPs is approximately one one-hundredth of a percent (i.e., 0.01 percent).[2453] Thus, a calculation of burden caused by TransCanada's contracts with CERS even using the pricing the California Parties allege is appropriate is insufficient to overcome the *Mobile-Sierra* presumption for the purpose of abrogating the subject contracts.

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[2448] California Respondents Initial Br. at 31; *see id.* at 31-36.

[2449] Order on Remand at PP 18, 24.

[2450] *California ex rel. Brown*, 135 FERC ¶ 61,178, at P 77 n.116 (2011).

[2451] Order on Remand at P 24 (emphasis added). *See also id*. at n.56.

[2452] Ex. TRC-1 at 165:5-10.

[2453] *Id.* at 165:15-17.

#### (d) The California Parties' Claims Are Not Barred by Laches or Statute of Limitations

1706. TransCanada, alone among the parties and Trial Staff, argues that the California Parties' claims are time barred by statutes of limitations and the doctrine of laches.[2454] These arguments are meritless and are hereby rejected for the reasons advanced by the California Parties in their Reply Brief.[2455]

#### (e) The California Parties' Claims Are Not Barred by the Unclean Hands Doctrine

1707. Lastly, allegations that CERS engaged in inequitable conduct by (1) using confidential information to gain an unfair competitive advantage and/or (2) exercising buyer market power are unsupported and are hereby rejected for the reasons advanced by the California Parties in their Reply Brief.[2456] Rather, the evidence of record reflects that CERS made every effort to protect the health and welfare of Californians, the viability of the electricity grid, and California's economy during the Western Energy Crisis. In particular, the testimony of Mr. Hart demonstrates the extraordinary measures that he and others took to perform their duties on behalf of California consumers in a responsible and professional manner during an extremely unstable and volatile period.[2457]

1708. In conclusion, although the California Parties have successfully demonstrated that the Western Energy Crisis was "unprecedented" and imposed an "enormous burden" upon consumers,[2458] the California Parties have failed to meet their burden of demonstrating that the bilateral contracts entered into between TransCanada and CERS "imposed an excessive burden on consumers"[2459] as required to overcome the *Mobile-Sierra* presumption that those contracts are just and reasonable.

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[2454] TransCanada Initial Br. at 78-85.

[2455] California Parties Reply Br. at 198-203.

[2456] California Parties Reply Br. at 184-198.

[2457] Ex. CAT-012; Ex. CAT-272.

[2458] California Parties Initial Br. at 127.

[2459] Order Granting Interlocutory Appeal at P 15.

### 2. The California Have Not Demonstrated that Coral's Sales to CERS Imposed an Excessive Burden on Consumers or Seriously Harmed the Public Interest

1709. Because the presumption of just and reasonable rates applicable to bilateral contracts under the *Mobile-Sierra* standard would not apply to the subject contracts, the analysis for *overcoming* the *Mobile-Sierra* standard under Issue 1(B) is not applicable to those contracts tainted by False Export and "bad faith." Rather, those contracts must be assessed under the "just and reasonable" standard of the FPA without the benefit of the *Mobile-Sierra* presumption to determine if modification of the contracts is necessary and if so, in what manner.[2460] The subject contracts should be referred to "Phase II" of this adjudication process for that purpose.

1710. However, with respect to those remaining contracts, i.e. those contracts not determined to have been tainted by False Export or "bad faith" under Issue 1(A) *supra*, for the same reasons discussed regarding TransCanada's contracts, the California Parties have failed to demonstrate that those remaining contracts with Coral imposed an excessive burden on consumers or seriously harmed the public interest.

## VIII. Summary and Conclusion

### A. Claims Asserted by the City of Seattle

#### 1. Seattle's Claims Pursuant to Section 206 of the FPA

##### (a) Seattle Failed to Demonstrate that Any of the Subject Respondents Engaged in Unlawful Market Activity or that Specific Contract Rates Were Directly Affected

1711. The Commission's Order on Remand makes clear that to abrogate contracts otherwise presumed to be just and reasonable under the *Mobile-Sierra* doctrine for the purpose of obtaining refunds under section 206, parties must "demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract."[2461] Mr. Philip Q Hanser, the sole witness Seattle presented in its Section 206

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[2460] The California Parties argued that the prices of Coral's (and all other Respondents') sales across the market should be reset to the MMCP levels established in Docket No. EL00-95. However, for the reasons discussed *supra* regarding Seattle, the MMCP is not an appropriate benchmark for use in this proceeding.

[2461] Order on Remand at P 21 (citing *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 554 (2008); *California ex rel. Brown*,

(continued…)

direct case covering the period of December 25, 2000 through June 20, 2001, and one of only two witnesses Seattle presented in this proceeding, clarified in response to questioning from the undersigned Presiding Judge that he was "not alleging any illegal conduct by any of the Respondents in this case."[2462] Mr. Wayne L. Morter, Seattle's only other witness, stated that he too was "not making any allegations regarding unlawful activity or misconduct by El Paso … or any other Respondent."[2463] These admissions are fatal to Seattle's Section 206 claims under Issue 1(A) because they demonstrate that Seattle has not made the central evidentiary showing of unlawful market activity by any Respondent as required by the Commission to abrogate the subject contracts or to obtain refunds.[2464]

**(b) Seattle Failed to Demonstrate that the Subject Spot Market Contract Rates Imposed an Excessive Burden On Consumers or Seriously Harmed the Public Interest**

1712. In a subsequent order in this proceeding, the Commission clarified that a party to a contract could also overcome the *Mobile-Sierra* presumption by presenting evidence that a particular contract or contracts impose an excessive burden or seriously harm the public interest.[2465] With regard to its Section 206 claims, Seattle relied on the testimony of Mr. Hanser to present the 2001 testimony of Ms. Paula Green and other public documents to assert excessive burden or harm to the public interest.[2466] The most obvious and fundamental failure of Ms. Green's testimony, as presented by Mr. Hanser, is that, contrary to the direction of the Commission, it does not tie any alleged burden or harm to

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135 FERC ¶ 61,178, at P 77 (2011); *Nev. Power Co. v. Enron Power Mktg. Inc.*, 125 FERC ¶ 61,312, at P 28 (2008)).

[2462] Tr. 2074:10-15, 2116:24-2117:1 (Hanser).

[2463] Tr. 3278:7-20 (Morter).

[2464] Order on Remand at P 21 ("parties seeking refunds must submit evidence not only on whether unlawful market activity occurred, but must also demonstrate a connection between unlawful activity by a seller and unjust and unreasonable rates under a specific contract.").

[2465] Order Granting Interlocutory Appeal at PP 12-15.

[2466] Tr. 1897:18-20 (Hanser) ("Q: You're not providing the facts. You're opining on the facts? A: Yes, that's correct.").

specific contracts or Respondents.[2467] Mr. Hanser did not review any transaction data at all as part of his testimony covering the Section 206 Period, and there is no indication in the record that Ms. Green ever did so either.[2468] Without evidence identifying individual contracts or transactions,[2469] it is impossible to evaluate whether particular contracts or transactions between a Respondent and Seattle imposed an excessive burden or seriously harmed the public interest.

1713. Mr. Hanser adopted Ms. Green's reference to rate increases totaling fifty-eight percent that Seattle instituted at or about this time, alleging that these rate increases were the result of "increased costs for wholesale power that Seattle was forced to pay."[2470] However, these rate increases were not tied to any specific wholesale energy costs, much less any costs that resulted from Respondents' contracts or behavior. In fact, the evidence of record reflects that these rate increases were a result of a myriad of factors including many having nothing to do with wholesale energy costs at all. For example, nearly twenty percent of the increase came from increases in transmission costs having nothing to do with wholesale energy costs.[2471] Seattle's increased wholesale power costs also reflect the consequence of Seattle's business decisions to reduce its long-term purchases, sell its share of the Centralia coal plant, and increase reliance on the wholesale spot market,[2472] which then coincided *with the lowest water year on record in sixty years*

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[2467] *See* Order on Rehearing at P 30 ("the Commission must evaluate each seller's conduct in relation to specific contract negotiations and/or whether the contract imposes an excessive burden on consumers").

[2468] Tr. 1901:2-25 (Hanser).

[2469] As discussed above, the definition of spot market transaction is sales with durations of twenty-four hours or less, prescheduled no more than twenty-four hours in advance of delivery, consistent with the Western Electricity Coordinating Council's (WECC) prescheduling calendar and hourly scheduling practices and timelines. *See supra* Section V.B.2.

[2470] Ex. SCL-1 at 5:20, 34:5.

[2471] Tr. 1981:3-1983:4 (Hanser).

[2472] Tr. 1911:5-13 (Hanser) ("PRESIDING JUDGE: I'm sorry. I thought the thrust of the question was if the BPA contract had continued, would those contract rates have been lower at that point in 2000 and 2001 than the spot market rates that they were exposed to. THE WITNESS: Yes. They would have been for the period of time -- the period of time, the month basically from the summer of June of 2000 -- summer of 2000 through basically the beginning of the summer of 2001."); Ex. SCL-40 at 2 (Seattle City

(continued…)

that limited hydroelectric generation output.[2473] In fact, compelling and well supported expert testimony analysis of market fundamentals by Professor Hogan concluded that reduced hydro generation was the "single most important factor contributing directly and indirectly to the high power prices during the Western Power Crisis."[2474]

1714. Mr. Hanser also provided excerpts of bond offerings from 2001 and 2003 to support Seattle's claim that increased wholesale power costs incurred by Seattle led to an excessive burden.[2475] Again, however, none of these documents analyze how any increased amounts for wholesale energy contracts translated into specific rate increases, much less how those amounts were connected to the Respondents or harmed the public interest. To the contrary, the documents showed that Seattle maintained its AAA credit rating during and after the period at issue.[2476] Further, the undersigned concurs with the Respondents' that the bond offering documents actually support their position that the higher wholesale power prices Seattle incurred were the result of market fundamentals of supply and demand and to a lesser degree Seattle's own business decisions. Seattle's statements at the time thus confirm that any burden Seattle faced was the result of unanticipated market forces and its own decisions and do not support any claim of excessive burden or harm to the public interest as a result of the Respondents' sales to Seattle during the relevant period.

1715. Further, while supply and demand market fundamentals are critical components in establishing market-based prices for wholesale sales of energy, Seattle failed to account for those market forces during the relevant period. Mr. Hanser acknowledged on cross-examination that he "never tried to analyze the Pacific Northwest demand" or

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Light Issues Brief stating that for 2000 and 2001, Seattle is "more dependent on the market than we have been historically because of the sale of our share of the Centralia coal plant").

[2473] Ex. SCL-10 at 10 ("Since late 2000, SCL's ability to use hydroelectric resources to restrict market purchases to off-peak periods has been greatly limited because of water conditions that are among the lowest in sixty years of record").

[2474] Ex. PNR-1 at 83:4-7.

[2475] Ex. SCL-1 at 32-35. *See also* Ex. SCL-38 and SCL-39.

[2476] Ex. SCL-39 at 1. Mr. Hanser was unable at hearing to reconcile this AAA rating with the testimony he purported to adopt from Ms. Green that Seattle's credit rating was harmed. Tr. 2226:1-17 (Hanser).

overall supply during the relevant period,[2477] and that he failed to analyze the effects of supply and demand fundamentals on price.[2478] Mr. Hanser's lack of any such analysis stands in stark contrast to Professor Hogan's careful and detailed analysis of the supply and demand fundamentals. Professor Hogan explained that on the supply side, the large reduction in hydro generation was particularly critical because Pacific Northwest purchasers rely heavily on hydro generation.[2479] While Professor Hogan analyzed and discussed the inextricably intertwined nature of many other complex and variable market fundamentals, he concluded that reduced hydro generation was the "single most important factor contributing directly and indirectly to the high power prices during the Western Power Crisis."[2480]

1716. None of these factors are consistent with the kind of excessive burden that courts and the Commission have held, in exceptional cases, might justify the reformation of contract rates. In fact, Seattle's average electric rates remained the lowest of the twenty-five largest cities in the United States in 2001.[2481] For residential rates in particular, Seattle's average rate was 5.99 cents/kWh, well below the U.S. average of 8.48 cents/kWh.[2482] These rate levels are inconsistent with any claim by Seattle of excessive burden.

### 2. Seattle's Claims Pursuant to Section 309 of the FPA

#### (a) Seattle Failed to Demonstrate that Any Respondent Engaged in a Specific Violation of a Substantive Provision of the FPA or Its Filed Tariff or Rate Schedule

1717. In its Order on Rehearing, the Commission determined that it may order refunds, if appropriate, for transactions between January 1, 2000 and December 24, 2000 (Section

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[2477] Tr. 1949:10-23 (Hanser).

[2478] Tr. 1960:13-1969:24 (Hanser).

[2479] Ex. PNR-1 at 83-100.

[2480] Ex. PNR-1 at 83:4-7.

[2481] Ex. PRX-260 at 3 (Seattle City Light 2001 Annual Report). *See also* Tr. 2208:6-14 (Hanser) (agreeing that Seattle's rates were the lowest out of the 25 largest cities).

[2482] Ex. PRX-260 at 3.

309 Period) under its FPA section 309 authority.[2483] While Seattle initially conceded that its testimony pertaining to the Section 309 Period does not pertain to the period from December 25, 2000 to June 20, 2001,[2484] Seattle has apparently renewed its argument that the Order on Rehearing permits Seattle to submit claims for refunds under section 309 for the entire period of January 1, 2000 through June 20, 2001.[2485] Regardless, this argument is moot given that Seattle has not demonstrated a basis for abrogating the subject contracts or for refunds for any period.

1718. The Commission's Order on Rehearing explained that "refund claimants may attain … relief under FPA section 309 … by demonstrating a seller's specific violation of a substantive provision of the FPA or tariff, compliance with which the Commission can enforce by taking actions 'necessary and appropriate.'"[2486] Reliance on evidence consisting of high prices alone was firmly rejected.[2487] Nevertheless, Seattle declined to address individual contracts and the conduct of these nine Respondents as it relates to the formation of their contracts with Seattle. Instead, Seattle asserts that each Respondent repeatedly violated its market-based tariff and section 205 of the FPA, which requires all prices for wholesale power to be "just and reasonable," by charging Seattle prices that were outside of a "zone of reasonableness determined by the seller's marginal cost of producing power."[2488] Seattle's expert witness, Mr. Hanser, uses two benchmark analyses to support his conclusions: (1) the Mitigated Market Clearing Price (MMCP) that the Commission used to calculate refunds in the California Refund Case and (2) the Pivotal Unit Benchmark, a surrogate for the marginal cost of a pivotal unit in the Pacific Northwest.

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[2483] *See* Order on Rehearing at P 32.

[2484] City of Seattle, Washington June 14, 2013 Answer in Opposition to the Indicated Respondents' Expedited Motion to Strike, at 6 ("Mr. Hanser's [June 3, 2013] testimony asserts Section 309 claims only for the period January 1, 2000 through December 24, 2000."); *see also* Tr. at 1901:23-25 (Hanser) ("Q: You did not do a benchmark analysis in your 206 testimony, either direct or rebuttal; is that correct? A: No, I did not.").

[2485] Seattle Initial Br. at 40.

[2486] Order on Rehearing at P 32.

[2487] *Id.* P 30.

[2488] Ex. SCL-110 at 34:22-24, 44:19-23.

1719. While there are deficiencies in using the MMCP or Pivotal Unit Benchmarks as a basis to abrogate the subject contracts or to support refunds in this proceeding in any event for the reasons discussed herein, it must be noted that Seattle's argument is basically the same argument made to the Commission on rehearing by the California Parties and rejected by the Order on Rehearing: "Cal[ifornia] Parties' claims of uniformly higher prices amount to little more than a variation on claims of general market dysfunction, which have been previously rejected by the Supreme Court as a basis for overcoming *Mobile-Sierra*."[2489] Moreover, in *Morgan Stanley*, the Supreme Court also rejected categorically the use of marginal cost as a test of reasonableness because it "fails to accord an adequate level of protection to contracts."[2490] The Court further stated:

> A presumption of validity that disappears when the rate is above marginal cost is no presumption of validity at all, but a reinstitution of cost-based rather than contract based-regulation. We have said that, under the *Mobile-Sierra* presumption, setting aside a contract rate requires a finding of '*unequivocal public necessity*' or '*extraordinary circumstances*'. *In no way can these descriptions be thought to refer to the mere exceeding of marginal cost*.[2491]

1720. Furthermore, for the many reasons discussed above, the MMCP benchmark is specific to the organized California energy markets and not appropriate for use in the Pacific Northwest. The Commission has rejected the use of the MMCP market-wide remedy adopted for the organized California markets as inappropriate for the bilateral Pacific Northwest spot market where "each seller receives only what a specific buyer agrees to pay for a given transaction and each buyer has the opportunity to negotiate a lower price."[2492] The Commission's determination that the California and Pacific Northwest markets are fundamentally different for purposes of its consideration of the use of the MMCP as a remedial construct is fully explained in and supported by the record in the 2001 proceeding in which the Commission created the MMCP proxy and, for the reasons explained in this Initial Decision, the record in this proceeding also fully supports that determination.

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[2489] Order on Rehearing at P 30.

[2490] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 548 (2008).

[2491] *Id.* at 550-51 (emphasis added) (citations omitted).

[2492] Order on Remand at P 24.

1721. Moreover, Seattle's Pivotal Unit Benchmark analysis suffers from a number of deficiencies that render it of limited usefulness in support of Seattle's attempt to abrogate the subject contracts or to obtain refunds. Among other things, the Pivotal Unit Benchmark is fatally flawed from the outset because it ignores *individual* sellers' actual marginal costs.[2493] The benchmark calculations do not even take into consideration whether the cost of energy incurred by a Respondent exceeds the benchmark even before the Respondent may have resold it to Seattle.[2494] The failure to confront individual marginal costs is a fatal error for every respondent given the Respondent-specific nature of this case as, perhaps most dramatically, illustrated by reference to the power marketer respondents, whose marginal costs were tied to the prices available in the market, not generation costs. Further, the marginal cost estimates utilized in the Pivotal Unit Benchmark do not include the recovery of fixed costs, a reasonable profit, opportunity costs, or transmission costs.[2495] Nor do they account for scarcity rents, which are the "additional increment above marginal running cost" by which competitive prices will rise in times of limited supply.[2496]

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[2493] Tr. 2016:1-7 (Hanser) (admitting that the benchmarks are "based on estimates of seller costs"); Tr. 2086:15-18 (Hanser) (admitting that he did not calculate Respondent's specific marginal cost).

[2494] Tr. 2083:20-2084:7 ("PRESIDING JUDGE: Let me just ask a follow-up question about that. So I'm struggling with trying to understand the record with respect to the costs associated with this energy that was being sold by the City of Seattle and the Respondents. Is it possible that the cost of the energy to the City of Seattle exceeded the MMCP benchmark even before they resold it? THE WITNESS: Well, I mean, if it was -- I don't know. PRESIDING JUDGE: You didn't look at that, did you? THE WITNESS: No.").

[2495] Mr. Hanser's Pivotal Unit Benchmark for units actually in the Pacific Northwest does not contain any adders and is determined solely by multiplying hourly plant heat rates by gas prices. Ex. SCL-110 at 41:1-9; Ex. SCL-115 at 21:18-23; Tr. 2125:18-20, 2031:13-15 (Hanser) (opportunity cost is not a component of marginal cost; Pivotal Unit Benchmark does not account for seller's opportunity costs).

[2496] Ex. SCL-111 at 95 ("This is not to say that competitive prices should never rise above the marginal running cost of generation. When supply is scarce relative to demand, competitive prices will rise to a level that reflects the value that the marginal consumer places on additional consumption. This additional increment above marginal running cost is referred to as the 'scarcity rent.'").

1722. Perhaps most compelling is the fact that when adjusted for *actual* natural gas costs and the inclusion of sales both *below* and *above* the benchmarks,[2497] many of the "premiums" Mr. Hanser identifies in his Pivotal Unit Benchmark analysis actually turn negative.[2498] This result is graphically demonstrated by Exhibit JDG-11, which reflects that the total alleged "premiums" turn negative for Avista Energy, Constellation, El Paso, PPL, and PSCo and are dramatically reduced as to the remaining Respondents when appropriately adjusted for these two variables. These findings are inconsistent with any claim of "excessive burden" and are inconsistent with Seattle's basic theory of liability – that these sellers charged Seattle rates that greatly exceeded the rates they could have charged if the market had been competitive.

1723. Seattle acknowledges that all of the transactions for which it is seeking refunds were conducted under the Western Systems Power Pool (WSPP) Agreement.[2499] The Commission has specifically held that the WSPP Agreement demonstrates the "intent that neither seller nor buyer be able to seek changes under Section 205 or 206 of the FPA other than under the 'public interest' standard of review."[2500] Further, each of the subject transactions were bilateral and individually negotiated.[2501] Numerous buyers and sellers transacted under the WSPP Agreement, as demonstrated by the list of approximately 200 signatories included with the WSPP Agreement.[2502] The Respondents and Seattle were both actively engaged as sellers and buyers in the Pacific Northwest and freely negotiated

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[2497] Tr. 2033:1-7 (Hanser) ("Q: So the conclusions that you reach as to whether sellers were above or below the benchmark just take account of the hours above the benchmark? A: Yes, that is correct. Q: Without any offset for sales below the benchmark? A: Yes, that is correct.").

[2498] *See* Ex. JDG-11

[2499] Ex. SCL-1 at 8:20-22 ("All of the transactions from January 1, 2000 through June 20, 2001, which includes the period for which Seattle is seeking refunds, were conducted under the WSPP Agreement"); Ex. SCL-110 at 9:5-9.

[2500] *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at P 36 (2003). *See also* Order on Remand at P 20; Order on Rehearing at P 13.

[2501] *See, e.g.*, Ex. PPL-1 at 7:2-4 (explaining all of PPL's sales in the Pacific Northwest were made under negotiated, bilateral agreements); Ex. EP-1 at 10:15-18 (same for El Paso); Ex. AVE-1 at 13:17-19 (same for Avista Energy).

[2502] Ex. CAT-124 at 108-110 (attachment to WSPP Agreement listing members). *See also* Tr. 3173:2 (Morter).

under the WSPP Agreement to get the best price available.[2503] Like Seattle, many Respondents also had load-serving obligations that required them to buy power to match load.[2504]

1724. Yet, despite clear direction from the Commission, in support of its efforts to have the Commission abrogate the subject bilaterally negotiated contracts and order refunds from the remaining nine Respondents, Seattle has continued to assert a generic market-wide theory that *all* sellers violated their tariffs and the FPA to the extent that they sold power to Seattle above the MMCP and Pivotal Unit benchmarks.[2505] The incongruity of this argument is underscored by the fact that as a market participant Seattle also sold energy above these benchmarks. Mr. Cavicchi testified without contradiction that throughout the relevant period Seattle, itself an active market participant, was selling at prices comparable to those at which Respondents sold to Seattle.[2506] Additionally, Seattle's own witness, Mr. Hanser, confirmed that Seattle sold at prices above the MMCP, the lower of his two benchmarks.[2507]

1725. Further, as previously explained, "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law. The presumption may be overcome *only if* FERC

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[2503] *See, e.g.*, Tr. 3181:18-3182:10 (Morter) (admitting that Seattle sold power at prevailing market prices and that Seattle would not be acting prudently to sell below that price).

[2504] Tr. 3259:23-3260:5 (Morter) (admitting that PSCo and Avista Utilities are load-serving entities). *See also* Ex. PPL-1 at 4:9-5:2 (describing PPL's full requirements contract with Montana Power Company under which PPL was obligated to meet fluctuations in load, much like a load-serving entity).

[2505] *See* Ex. SCL-110 at 34:22-28, 44:17-23.

[2506] Ex. JDG-1 at 19:10-21 ; *see also* Ex. TAE-23 at 11:10-21 (TransAlta witness Wes Harrigan referencing Exhibits TAE-27 and TAE-28 and stating that "TransAlta bought power from and sold power to Seattle at similar price levels during the Section 309 Period").

[2507] Tr. 2018:25-2019:6 (Hanser) ("PRESIDING JUDGE: What I want to know is whether there was any time, to your knowledge, that the City of Seattle sold surplus energy at higher than the MMCP during the relevant time period? THE WITNESS: I believe there was power sold above MMCP by Seattle, but I would have to go back and check my data.").

concludes that the contract *seriously harms the public interest*."[2508] Seattle has failed to demonstrate the kind of excessive burden that courts and the Commission have held, in exceptional cases, might justify the reformation of contract rates. In fact, despite the many complex and inextricably intertwined market force challenges that Seattle and other market participants were facing in the Pacific Northwest, including a large reduction in hydro generation coinciding with one of the lowest water years on record in sixty years, Seattle's average electric rates remained the lowest of the twenty-five largest cities in the United States in 2001.[2509]

1726. For the reasons discussed above, Seattle's claims under both section 206 and section 309 of the FPA must be denied.

### B. Claims Asserted by the California Parties

1727. The California Parties have clearly demonstrated that the Western Energy Crisis inflicted real harm on California's consumers, businesses and government services; that the energy crisis was "unprecedented"[2510] and that the "burden [on the IOUs' customers] was enormous."[2511] Examples of the harm caused to consumers by the energy crisis, such as consumers being forced to choose between buying food or medicine and paying their electric bill[2512] and businesses cutting hours, laying off workers, and adding surcharges to their prices to cover the cost of electricity,[2513] were compelling and mostly unrebutted. Commissioner Florio testified that the rates charged during the Western Energy Crisis "placed an excessive burden on the customers"[2514] and "impaired the

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[2508] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008) (emphasis added).

[2509] Ex. PRX-260 at 3 (Seattle City Light 2001 Annual Report). *See also* Tr. 2208:6-14 (Hanser) (agreeing that Seattle's rates were the lowest out of the twenty-five largest cities).

[2510] Ex. CAT-001 at 19.

[2511] *Id*. at 4.

[2512] *See id*. at 11-12.

[2513] *See id*.

[2514] *Id*. at 19.

State's finances,"[2515] and that California consumers – third parties to the contracts – "continue to bear [that burden] to this day."[2516] Professor Berck's testimony confirmed that to avoid the extreme adverse economic consequences of immediately passing through to consumers the full cost of energy under the CERS contracts during the Western Energy Crisis, it was necessary to implement a twenty year bond program.[2517] The undersigned concurs with the position of the California Parties that the fact that the economic burden to consumers was spread out over time (twenty years) did not eliminate the economic burden to consumers, it merely mitigated it.

1728. Moreover, the record reflects that there were seven blackouts that occurred in the CERS Period, totaling more than twenty-two hours where some portion of the state was without power.[2518] Additionally, there were hundreds of hours of emergency conditions during the CERS Period, where unplanned outages could have occurred.[2519] Dr. Fox-Penner's testimony provided clear and convincing arguments that the blackouts that occurred during the CERS Period imposed significant burdens on California.[2520]

1729. However, as compelling as this testimony is, it must be considered in the context of the relief sought in this proceeding – the California Parties seek abrogation of specific bilateral contracts between CERS and the two remaining Respondents, TransCanada and Coral, the contracts of all other market participants will remain untouched by this litigation.

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[2515] *Id*. at 3.

[2516] *Id*. at 19.

[2517] Ex. CAT-267.

[2518] Ex. CAT-161 at 79.

[2519] *Id*. at 79-80 & n.34.

[2520] *See, e.g*., Ex. CAT-161 at 81-87. *Cf.* Ex. CAT-269 at 9-10 (explaining that the "impacts of blackouts, both direct and indirect, were substantial and placed a further burden on California consumers … . Indeed, the image of the Golden State was severely tarnished, which resulted in collateral impacts such as reduced business investment in the state and reduced tourism.").

### 1. The California Parties Claims Under Issue 1(A)

1730. The sales made by TransCanada and Coral to CERS were individually negotiated bilateral transactions governed under the Western Systems Power Pool (WSPP) Agreement.[2521] Numerous buyers and sellers transacted under the WSPP Agreement, as demonstrated by the list of approximately 200 signatories included with the WSPP Agreement.[2522] Further, the Commission has specifically held that the WSPP Agreement demonstrates the "intent that neither seller nor buyer be able to seek changes under section 205 or 206 of the FPA other than under the 'public interest' standard of review."[2523] As previously explained, absent probative evidence of specific seller unlawful market activity at the contract formation stage, as discussed under Issue 1(A) *supra*, "[t]he [Commission] *must* presume that the rate set out in a freely negotiated wholesale-energy contract meets the 'just and reasonable' requirement imposed by law."[2524] The presumption may be overcome *only if* FERC concludes that the contract *seriously harms the public interest*."[2525]

1731. To *avoid* the *Mobile-Sierra* presumption that the subject contract rates were "just and reasonable" for the purpose of abrogation of specific contracts with Respondents under Issue 1(A), the California Parties bear the burden of demonstrating that the Respondent engaged in "unfair dealing at the contract formation stage,"[2526] which "alter[ed] the playing field for contract negotiations,"[2527] and had "a causal connection … [to] the contract rate."[2528] In other words, the Respondent must have "engaged in

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[2521] Ex. TRC-77 at 13:8; Ex. CAT-041 at 111:1-4.

[2522] Ex. CAT-124 at 108-10 (attachment to WSPP Agreement listing members). *See also* Tr. 3173:2 (Morter) (agreeing that there were "a lot" of WSPP members).

[2523] *Nev. Power Co. v. Enron Power Mktg., Inc.*, 103 FERC ¶ 61,353, at P 36 (2003). *See also* Order on Remand at P 20; Order on Rehearing at P 13.

[2524] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

[2525] *Id.*

[2526] *Id.* at 547.

[2527] *Id.* at 554; Order on Remand at P 20.

[2528] *Morgan Stanley*, 554 U.S. at 555.

unlawful market activity in the spot market and … such unlawful activity directly affected the particular contract or contracts to which it was a party."[2529]

**(a) The California Parties Failed to Demonstrate that TransCanada Engaged In Unlawful Market Activity**

1732. For the reasons discussed *supra*, the evidence proffered by the California Parties fails to demonstrate that any actions attributable to TransCanada caused or even exacerbated the harm suffered by the California ratepayers during the Western Energy Crisis such that their contracts with CERS should be abrogated.

1733. The California Parties aver that they have demonstrated that the high prices during the Western Energy Crisis were the result of sellers' market manipulation, illegal behavior, and tariff violations.[2530] This argument is disingenuous however given that the California Parties are well aware that only a party's *own* misconduct can be a ground for preventing the *Mobile-Sierra* presumption from applying to *its* contract.[2531] While the unrefuted evidence of record supports a finding that the California Parties often found themselves in a position of either suffering the significant direct and indirect costs and disruptions associated with a blackout or paying the high rates necessary to purchase energy on the spot markets during the relevant time period, the record is wholly insufficient to establish that the high prices were the result of unlawful activity by TransCanada.

1734. First, the California Respondents have identified defects in the California markets that clearly contributed to the Western Energy Crisis including: (1) California's historic heavy reliance on imported energy;[2532] (2) decisions by California policymakers that

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[2529] Order on Remand at P 21.

[2530] *See, e.g.*, California Parties Initial Br. at 173-75.

[2531] Order on Remand at P 21 (Parties seeking refunds "must demonstrate that *a particular seller* engaged in unlawful market activity in the spot market and that such unlawful activity directly affected the particular contract or contracts to which *the seller was a party*.") (emphasis added).

[2532] At the time, the Commission noted "[o]ver time, California utilities have increasingly relied on imports from generation located in neighboring states to meet their load requirements and have constructed significant transmission capacity interties to import electricity for California consumers." *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC ¶ 61,121, at 61,357 (2000); *see also* Ex. TRC-14 at 4 (executive summary of California Energy Commission Staff Report on California

(continued…)

effectively limited additional generating capacity within the state;[2533] (3) an electric restructuring plan that lacked critical safeguards contained in contemporaneously launched organized market designs;[2534] (4) energy-limited Western generation resources; and (5) a convergence of high demand and limited supply of electric energy.[2535]

1735. Moreover, Respondents provided the only comprehensive analysis of the market fundamentals in the Pacific Northwest which identified and discussed many other factors contributing to the Western Energy Crisis, including: (1) the reduced availability of hydroelectric generation, coupled with high demand for natural gas-fired generation;[2536] (2) nuclear plant and qualifying cogenerator outages;[2537] (3) air emission limits;[2538] and (4) unprecedented levels of demand,[2539] which, together with other factors, caused a

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Natural Gas Analysis and Issues, stating "[g]rowth in demand for power generation in California's neighboring states has consumed much of the surplus generating capacity that once provided high levels of cheap imports of electricity").

[2533] The Commission's Remedy Order noted that "[t]he Staff Report underscores inadequate siting of generation and transmission as a key structural defect in California," and called upon the CPUC to address delays in siting of new generation and transmission facilities. *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 93 FERC at 61,372.

[2534] The Commission's Remedy Order criticized the California market design provision precluding the IOUs from making forward purchases of energy, a requirement the Commission found to cause the IOUs to have excessive exposure to the price volatility of spot markets. *Id.* at 61,354. The Commission encouraged the CPUC to eliminate restrictions on the utilities' ability to use long term products. *Id.* at 61,372.

[2535] Ex. PNR-1 at 77:3-7 ("During 2000, the CPUC did not allow retail prices to rise in response to shortage conditions, high costs, and increased wholesale price volatility in the Cal ISO and Cal PX bid-based spot markets. This failure of the CPUC, and the State of California more generally, to take prompt actions to curb electric power demand is one of the critical public policy decisions which served to exacerbate the Western Power Crisis.").

[2536] *Id.* at 114:19-120:14 & Appendix III.

[2537] *Id.* at 101-114.

[2538] *Id.* at 120-132 & Appendix II.

[2539] *Id.* at 65-82.

supply-demand imbalance that resulted in historically high prices.[2540] The evidence of record does not demonstrate that actions attributable to TransCanada caused the Western Energy Crisis or even exacerbated it. Further, and more importantly, for the reasons discussed above, the California Parties have failed to demonstrate that TransCanada engaged in any unlawful market activity that directly affected the particular contracts to which it was a party such that the presumption of just and reasonable rates applicable to those contracts under the *Mobile-Sierra* standard would not apply.

**(b) <u>The California Parties Have Demonstrated that Coral Engaged In Unlawful Market Activity</u>**

1736. There were clearly defects in the California markets that contributed to the Western Energy Crisis that were not caused by Coral,[2541] as well as significant market fundamentals in the Pacific Northwest contributing to the Western Energy Crisis which, together with other factors, caused a supply-demand imbalance that resulted in historically high prices independent of Coral's actions.[2542] However, the record also reflects that, unlike TransCanada, unlawful activity by Coral at the contract formation stage may have contributed to or exacerbated the situation the California Parties often found themselves in of either suffering the significant direct and indirect costs and disruptions associated with a blackout or paying the high rates necessary to purchase energy on the spot markets during the relevant time period. Blackouts, a phenomenon

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[2540] *Id.* at 64:12-65:15 (summarizing the contributing factors to the supply-demand imbalance); *see also id.* at 10:14-16 ("scale of shortage … alone could explain the high prices and other market outcomes during the CERS period"); *id.* at 11:14 ("scale of the impact of the fundamentals is sufficient to explain the price impacts"). *See also* Ex. TRC-1 at 12-23; Ex. CAT-038 at 2 ("a shortage of electric power and available energy, combined with a rapid rise in the price of natural gas to fuel generating plants in the State, resulted in a rapid and substantial increase in wholesale energy costs"); *id.* at 3 ("The establishment of long-term contracts, conservation, new generation and reduced natural gas costs have all been factors in the downward trending of costs."); Ex. CAT-039 at 40 ("As supply decreased, the price of electricity offered within the California wholesale market increased further."); *id.* at 46 ("Even before the June 19, 2001 FERC market mitigation order … spot market prices had dropped to below $100 per MWh … due to a combination of conservation and the Department's contracts."); Ex. CAT 40 at 23 ("By the summer of 2000 … insufficient power supply was being bid into the PX and CAISO to satisfy all required load at prices within historic ranges.").

[2541] *See supra* notes 2532 through 2534 and accompanying text.

[2542] *See supra* notes 2536 through 2540 and accompanying text.

that even Respondents' own expert, Mr. Tranen, readily conceded had to be avoided at all costs,[2543] occurred as late as May 7 and 8, 2001, towards the end of the CERS Period.[2544] In fact, virtually all of the Stage 3 Emergencies that the ISO called occurred during the CERS Period.[2545] Sellers were aware that CERS had to buy large amounts of energy in real-time to avoid blackouts, in trader parlance, that CERS was "short."[2546]

1737. Moreover, and perhaps more importantly, Coral was aware that CERS was in a vulnerable position and ready to pay high prices if necessary to avoid blackouts.[2547] Accordingly, for the reasons discussed in this Initial Decision, the California Parties have established a ***prima facie*** case that at least 47 of the subject contracts were tainted by deceptive False Export activities.[2548] Mr. Taylor reported that Coral engaged in 139 hours of False Export involving 2,798 MW; however, Mr. Taylor testified that his analysis may understate actual violations as it does not include cases where the exporting party was different from the party selling to CERS.[2549]

1738. The California Parties have also established a ***prima facie*** case that as many as 119 of the subject contracts may have been tainted by "bad faith," i.e. that Coral was

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[2543] Tr. 3980:8-23 (Tranen).

[2544] Ex. CAT-041 at 30 n.49.

[2545] *See* Ex. CAT-134 (ISO Alert, Warning, and Emergency Record); Ex. CAT-041 at 30 n.49; Ex. CAT-289 at 110 n.223.

[2546] *See, e.g.*, CAT-012 at 3:18-4:20 (discussing blackouts and the California Governor's proclamation of a state of emergency); Ex. CAT-022 at 7:7-8 (stating that the Governor's proclamation was "front page news"). *See also* Ex. CAT-022 at 7:14-20.

[2547] *See, e.g.*, Ex. CAT-713 at 7:24-8:4 (January 18, 2001 Coral trader tape in which Coral supervisor congratulated traders on extraordinary profits from a trade in California and admitted she had no ethical problem causing rolling blackouts); Tr. 4056:3-5 (Bowman). *See also* Ex. CAT-104 (emails between Coral traders discussing Coral's ability to exploit CERS's concern regarding blackouts to extract large margins); Ex. CAT-360 (on May 8, 2001, an ISO blackout day, Coral arranged with Avista to purchase 25 megawatt-hours for $450 and offered it to CERS for $550; when CERS declined, Coral advised Avista that it would not be making the purchase for resale).

[2548] *See supra* Section VI.B.2(a).

[2549] Ex. CAT-041 at 95.

aware that CERS was working under significant distress and used that information in an unlawful manner at the contract formation stage to maximize its profits from CERS.[2550] While Mr. Taylor's *Power Markets Week* plus $75/MWh test,[2551] standing alone, does not establish evidence of duress, fraud, or bad faith in the formation of the contracts, it does provide corroborating evidence that Coral's deceptive trade practices directly affected the subject contracts.

1739. For the reasons discussed *supra*, the California Parties have established a ***prima facie*** case that, during the December 25, 2000 through June 20, 2001 period, with respect to the wholesale bilateral Pacific Northwest spot market energy contracts at issue in this case, Coral engaged in unlawful market activity without a legitimate business reason, i.e. False Exports and "bad faith" negotiations at the contract formation stage, that directly affected the particular contract or contracts to which Coral was a party. There remain significant questions of fact and law with respect to those transactions that must be resolved in Phase II of this proceeding.[2552] In Phase II, Coral may demonstrate that the contracts were not in fact False Exports or tainted by "bad faith" and/or that the rates charged to CERS with respect to these contracts were nonetheless just and reasonable based on Coral's actual costs and market conditions.

### 2. <u>The California Parties Claims Under Issue 1(B)</u>

1740. Absent evidence sufficient to *avoid* the *Mobile-Sierra* presumption that the subject contract rates were "just and reasonable" as discussed under Issue 1(A), to *overcome* the *Mobile-Sierra* presumption that the wholesale bilateral Pacific Northwest spot market energy contracts between Respondents and CERS were "just and reasonable," as discussed under Issue 1(B), the inquiry that must be addressed is not simply whether Respondents optimized an opportunity to maximize their profits during the Western Energy Crisis, but whether the contract rates arising from those transactions impose "an excessive burden on consumers" or "seriously harms the public interest." Factors such as contract rates relative to other market participants at the time, contract volumes, and duration of the contracts must also be considered.

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[2550] *See supra* Section VI.B.2(b).

[2551] California Parties Initial Br. at 29, 41-42.

[2552] *See Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 13, 2012) (Order Confirming Rulings from the September 6, 2012 Prehearing Conference); *Puget Sound Energy, Inc.*, Docket No. EL01-10-085 (Sep. 14, 2012) (Order of Chief Judge Phasing Proceeding and Suspending Procedural Timelines for Phase II).

1741. *Morgan Stanley* requires that the California Parties demonstrate "*extraordinary circumstances*" involving "*unequivocal public necessity*" because the contract "*seriously harms*" the public interest in order to overcome *Mobile-Sierra*,[2553] but the California Parties fail to make any effort to quantify the alleged "harm" imposed by any contract between Respondents and CERS under the standards required by *Morgan Stanley*. Instead, they claim that the *Mobile-Sierra* presumption should be overcome based upon their allegations that "the extremely high rates that the contracts imposed on consumers seriously harmed the public interest."[2554]

1742. Specifically, the California Parties rely on an aggregated estimate that the cost of supplies CERS purchased was too high by $5 billion.[2555] Reliance on the $5 billion aggregate number is insufficient standing alone to support abrogation of the subject bilateral contracts between CERS and Respondents for a number of reasons. First, the $5 billion figure includes the prices paid to other sellers that have settled and are no longer one of the two remaining Respondents in this phase of the proceeding. Many of those sellers have entered into significant monetary settlements with the California Parties and yet there has been no attempt to offset or recognize the benefits of those settlements by means of an adjustment to its $5 billion aggregate number. Further, this aggregate figure includes prices paid to sellers who have never been subject to legal claims of unlawful activity by the California Parties, such as municipalities within California and Seattle City Light.

1743. Acceptance of the California Parties' arguments based on this aggregated figure would result in the abrogation of Respondents' contracts with CERS based upon the impact of *others'* sales, a result the Commission has clearly rejected.[2556] Thus, in order to demonstrate an undue burden, the California Parties must demonstrate that the

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[2553] *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530, 534, 547, 550 (2008) (emphasis added).

[2554] California Parties Initial Br. at 18.

[2555] *See, e.g.*, California Parties Initial Br. at 150 (citing Ex. CAT-267 at 4). The California Parties also introduced evidence concerning the alleged overcharges by all Respondents in this case as of September 21, 2012. Ex. CAT-267 at 4. However, as with the $5 billion aggregate number, this figure also includes alleged overcharges by settled parties, specifically, Powerex, TransAlta and the Avista Entities.

[2556] *See* Order on Rehearing at PP 26, 30.

contracts from a *particular seller* impose an undue burden on consumers or seriously harm the public interest.[2557]

1744. With respect to TransCanada specifically, the evidence of record reflects that TransCanada's prices to CERS were below the weighted average price CERS paid to its other sellers.[2558] Specifically, "TransCanada's prices were typically below the average price that CERS paid at COB and about forty-nine percent of the time, the lowest price that CERS paid at COB."[2559] Further, the record reflects that TransCanada was typically selling between 13 MWh and 50 MWh in an hourly market in which total volume could exceed 3,900 MWh.[2560] Most importantly, even if all TransCanada sales are aggregated, the record reflects that CERS's acquisition costs were only one half of one percent higher under the actual contracts negotiated with TransCanada than they would have been had the transactions taken place at the MMCP level advocated as a benchmark by the California Parties.[2561] Based on these findings, the subject contract rates do not impose "an excessive burden on consumers" or "seriously harm the public interest."

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[2557] Respondents argue that *Morgan Stanley* requires that a single contract impose an excessive burden on consumers in order to overcome the *Mobile-Sierra* presumption. However, given the fact that spot-market contracts are for such a short duration, it would be essentially impossible to overcome the *Mobile-Sierra* presumption with respect to an individual spot market contract. Thus, Respondents' interpretation of *Morgan Stanley* would effectively eliminate the Commission's ability to ensure that spot market contracts do not seriously harm the public interest. Such an interpretation would be in direct conflict with the Court's statement in *Morgan Stanley* that "the FPA intended to reserve the Commission's contract-abrogation power for those extraordinary circumstances where the public will be severely harmed." *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 551 (2008); *see also United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344 (1956) ("contracts remain fully subject to the paramount power of the Commission to modify them when necessary in the public interest").

[2558] Tr. 2502:21-25 (Taylor); *see also* Ex. TRC-194; Ex. TRC-195.

[2559] Ex. TRC-1 at 8:15-19.

[2560] *See* Ex. TRC-82 at 136 (total of 3,965 MWh in hour ending 24).

[2561] *See* Ex. TRC-1 at 165:5-10. *See also* Ex. TRC-1 at 165:16-17. TransCanada notes that the actual rate impact is approximately one one-hundredth of a percent (i.e., 0.01 percent).

1745. Because the presumption of just and reasonable rates applicable to bilateral contracts under the *Mobile-Sierra* standard would not apply to those Coral contracts tainted by False Export and "bad faith," the analysis for *overcoming* the *Mobile-Sierra* standard under Issue 1(B) is not applicable to Coral's contracts tainted by False Export and "bad faith." Rather, those contracts must be assessed under the "just and reasonable" standard of the FPA without the benefit of the *Mobile-Sierra* presumption to determine if modification of the contracts is necessary and if so, in what manner.[2562]

1746. As previously explained, the California Parties fail to make any effort to quantify the alleged "harm" imposed by any contract between Respondents and CERS under the standards required by *Morgan Stanley*. Accordingly, with respect to those remaining Coral contracts not determined to have been tainted by False Export or "bad faith" under Issue 1(A) *supra*, the California Parties have failed to demonstrate that those remaining contracts imposed an excessive burden on consumers or seriously harmed the public interest.

1747. The Supreme Court in *Mobile* and *Sierra* has defined the necessary balance that must exist between the need for contract stability and public regulation, and the necessary restraint on the part of the Commission when faced with calls for contract reformation.[2563] Except as to those Coral contracts which have been determined to have been tainted by False Export or "bad faith" under Issue 1(A) *supra*, the California Parties have failed to meet the burden necessary to avoid or overcome the *Mobile-Sierra* presumption as applied to Respondents' contracts with CERS; therefore, those contract cannot be abrogated.

## IX. <u>Order</u>

1748. The omission from this Initial Decision of any argument raised by the Participants at the hearing or in their briefs does not mean that it has not been considered; rather, it has been evaluated and found to either lack merit or significance such that inclusion would only tend to lengthen this Initial Decision without altering its substance or effect.

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[2562] The California Parties argued that the prices of Coral's (and all other Respondents') sales across the market should be reset to the MMCP levels established in Docket No. EL00-95. However, for the reasons discussed *supra* regarding Seattle, the MMCP is not an appropriate benchmark for use in this proceeding. *See supra* Section V.B.4(b).

[2563] *See United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 344 (1956); *FPC v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956).

Accordingly, all arguments made by the Participants which have not been specifically discussed and/or adopted by this decision have been considered and are rejected.

1749. IT IS ORDERED, subject to review by the Commission on exceptions or on its own motion, as provided by the Commission's Rules of Practice and Procedure, that: within thirty days from the issuance of the final order of the Commission addressing this Initial Decision, and in accordance with Phase I of this proceeding, the California Parties and Coral are hereby directed to file pre-hearing briefs addressing the issues remaining to be adjudicated in Phase II of this proceeding in accordance with the findings of fact and conclusions of law set forth in this Initial Decision.

Bobbie J. McCartney
Deputy Chief Administrative Law Judge