I. Introduction

The Federal Trade Commission (FTC) staff appreciates this opportunity to submit a comment in reply to certain comments filed last month in this proceeding before the State of New York Public Service Commission (NY PSC). The NY PSC has requested input concerning the NY PSC staff’s Straw Proposal on Track One Issues in the Reforming the Energy Vision (REV) project.2

We commend the NY PSC and its staff for their efforts to rethink the role of the electricity distribution system in the face a number of key developments. Those developments include (1) important technical advances in distributed energy resources (DERs); (2) increasing concerns about the environmental impacts of fossil-fueled generation; and (3) growing evidence that conventional power supplies may lack the resilience to satisfy electricity customers’ differing preferences for increased reliability. Our comment draws on the FTC’s experience both in enforcing competition laws and in advising state and federal regulatory agencies about the competitive effects of an array of regulatory programs focused on the electric power system.

Most fundamentally, the NY PSC staff’s Straw Proposal contemplates a transformation of the function of the electric distribution system. This transformation would involve the adoption of a Distributed System Platform (DSP) framework for the distribution stage of the electric industry. This step, which is akin to creating a separate system operator at the distribution level of the industry, would be a departure from the historic design and operation of the electricity distribution stage.

1 This comment expresses the view of the FTC’s Office of the General Counsel, Office of Policy Planning, and Bureau of Economics. The comment does not necessarily represent the views of the FTC or of any individual Commissioner. The Commission, however, has voted to authorize the filing of this comment.

Largely designed and operated as the lower-voltage extension of the transmission system, the distribution system served historically as the final step in delivery of power to individual electricity customers from large (and often distant) generators, all owned and operated by heavily regulated monopoly utilities. As the Straw Proposal describes, however, recent technical advances in small-scale generators, renewable generation, power system operating technology, demand response (DR), and (most recently) energy storage devices and electric vehicles have opened new opportunities for competition between centralized generators and DERs connected to the distribution system (but often installed on the customer side of the meter).\(^3\) DERs represent an opportunity to better serve the preferences of electricity customers, and DERs can improve the overall efficiency of the electric power system.

The NY PSC (as well as regulators in other states and nations) must determine how to respond to these new opportunities for cost-saving efficiencies and customized service for electricity customers. We agree with the NY PSC staff that the existing regulatory approach is unlikely to bring customers the full potential benefits offered by advances in DERs and related technologies.\(^4\) We also agree that it is crucial to operate the DSP fairly and objectively in order to create a setting in which DER investments can flourish and benefit electricity customers.

As the NY PSC moves forward with the REV process, we encourage it to focus on the lessons learned during the earlier transformation to competition in organized wholesale electricity markets in New York and other states. Like the local distribution system, transmission originally developed as a proprietary system for moving power from each utility’s own generators to customers within its territory (with some relatively weak connections to other utilities). Over the past 25 years, particularly in areas with organized wholesale power markets, the transmission system has gradually become a true network that facilitates technical and organizational innovations, environmental improvements, and greater efficiency through competition. By rewarding the performance of generators and other energy resources, organized competitive markets can produce benefits for customers, including improvements in the overall efficiency, reliability, and resiliency of the power system.

The REV project aims to promote effective competition at the distribution level to benefit electricity customers and shares the organized wholesale electricity market’s goals of increased efficiency, transparency, and customer choice.\(^5\) Ideally, the NY PSC will design the REV project to take into account the experience gained from restructuring wholesale electricity markets.

As we explain in Sections III and IV of this comment, our primary concern about the Straw Proposal is that the NY PSC staff favors an administrative determination that utilities should serve as their own DSP operators. By contrast, we believe that an open competitive procurement process should be the means of selecting the DSP operator. Section III discusses

\(^3\) Straw Proposal, § III.B.

\(^4\) *Id.* § I.D.

\(^5\) *Id.* at 1-2.
the advantages of such a selection process that would entail an objective and transparent evaluation of the costs and benefits associated with different potential DSP operators. Section IV addresses the issue of potential distribution service discrimination against independent DER owners by DSP operators that also own DERs. The potential for such discrimination is the genesis of our recommendation in Section III that the NY PSC institute a competitive selection process to choose DSP operators – a process that would weigh the associated costs and benefits of different applicants for the DSP operator role.

In addition, to a considerable extent, the Straw Proposal would allow each incumbent distribution utility to invest in DERs in its own distribution territory. The Straw Proposal would thus fail to take full advantage of the lessons learned about vertical market power and associated transmission discrimination (in the form of lower quality or more costly transmission service) during the restructuring of wholesale electricity markets. The initial comments of NRG Energy and the National Energy Marketers Association (NEM), among others, also expressed a concern about the Straw Proposal’s treatment of vertical market power issues. As the Federal Energy Regulatory Commission (FERC) concluded in Order No. 2000, it has been difficult to detect, document, and prevent violations of behavioral rules against discrimination in transmission services, and thus behavioral rules have been insufficient to prevent transmission monopolists from using transmission discrimination to raise the costs and risks of rival centralized

6 See Section IV of this comment.

7 NRG Energy, an independent power producer, asserted: “[A]llowing utilities to own and operate DERs in competition with competitive entities will result in anti-competitive pricing, barriers to entry, and bias, and will drive away competitive investment in DERs.” Initial Comments of NRG Energy, Inc. to the DPS Staff Review Proposal on Track One Issues, at 2 (Sept. 22, 2014), available at http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={403F3AE0-09F4-4184-9BB8-755D442CA8F3}. Similarly, NEM contended: “[A]fter nearly two decades of experience with competitive retail markets, it is abundantly clear that the anti-competitive impacts of monopoly utility participation in competitive energy markets, be it for commodity supply or new energy-related value-added services as a DER provider, is poor public policy, is not in the public interest and deters and discourages the private capital investment and technology innovation that is necessary to truly realize the REV vision.” Comment of the National Energy Marketers Ass’n, at 2 (Sept. 22, 2014) available at http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={929C1EFF-B6C6-4779-934A-23EDD5DA11D2}. Further, in a comment submitted in August, the New York Independent System Operator (NYISO) concluded that “vesting the utility with the roles of market manager, distribution utility, DER provider, and DER developer at the same time may stifle the competition and technological advancement the PSC seeks to promote in this proceeding.” Corrected Comment of the New York Independent System Operator, Inc., at 5 (Aug. 18, 2014), available at http://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={B9B3E4DA-4F8E-47FA-8316-DBD4E096A6F5}. 
generators.\(^8\) With regard to the distribution system, we similarly doubt that behavioral rules—intended to curb distribution service discrimination that could reduce the competition faced by utility-owned DERs—will be sufficient by themselves to remedy these concerns over distribution service discrimination. Discrimination in electric system operations at any stage of moving power from generators (or other DERs) can be very subtle, and even the appearance of discrimination in the provision of such services can discourage investment in beneficial DERs in New York by raising the perceived risks and costs facing such investments. To address this concern, we recommend that the NY PSC and its staff revise the Straw Proposal to include: (1) an open competitive process to select each DSP operator with selection criteria that include preventing distribution service discrimination and alleviating perceptions of such discrimination; and (2) one or more independent DSP market monitors (also selected through a competitive process) to augment the enforcement and market monitoring efforts of the NY PSC and its staff.

We also encourage the NY PSC staff to consider two related topics for inclusion in the Straw Proposal, as mentioned in Section V of this comment.

II. Interest and Experience of the FTC

The FTC is an independent agency of the United States Government responsible for maintaining competition and safeguarding the interests of consumers. The FTC does so through law enforcement, policy research, and advocacy. For example, in the field of consumer protection, the FTC enforces Section 5 of the Federal Trade Commission Act, which prohibits unfair or deceptive acts or practices. In its competition mission, the FTC enforces antitrust laws regarding mergers and unfair methods of competition that harm consumers. In addition, the FTC often analyzes regulatory or legislative proposals that may affect competition, allocative efficiency, or consumer protection. It also engages in considerable consumer education through its Division of Consumer and Business Education.\(^9\) In the course of all of this work, the FTC applies established legal and economic principles as well as recent, innovative developments in economic theory and empirical analysis.

The energy sector, including electric power, has been an important focus of the FTC’s merger review and other antitrust enforcement, competition advocacy, and consumer protection efforts.\(^10\) The FTC and its staff have filed numerous comments advocating competition and

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\(^8\) See the italicized material in the body of Section IV of this comment (presented in a less abridged form in the Appendix).


consumer protection principles with state utility commissions, state legislatures, the Department of Energy (DOE), and FERC. In particular, we have filed a number of advocacy comments concerning restructuring of wholesale electricity markets, DR, dynamic pricing, and the interactions of these developments with retail competition. The FTC’s competition advocacy


11 A listing, in reverse chronological order, of FTC and FTC staff competition advocacy comments to federal and state electricity regulatory agencies is available at http://www.ftc.gov/policy/advocacy/advocacy-filings?combine=&field_matter_number_value=&field_advocacy_document_terms_tid=5290&field_date_value%5Bmin%5D%5D=660773160000000000&field_date_value%5Bmax%5D%5D=661451200000000000&=Apply.

program also has issued two staff reports on electric power industry restructuring issues at the wholesale and retail levels. In addition, the FTC staff (along with staff from FERC, the Department of Justice, the Department of Agriculture, and DOE) contributed to the work of the Electric Energy Market Competition Task Force, which issued a Report to Congress in the spring of 2007.

III. Straw Proposal § III.A: “Identity of the DSP Provider”

The Straw Proposal’s blanket administrative determination that each incumbent distribution utility should serve as its own DSP operator does not offer potential rival DSP operators any opportunity to show how they can benefit customers and surpass the distribution utilities in avoiding the potential distribution service discrimination threats outlined in the Straw


13 FTC Staff Report, Competition and Consumer Protection Perspectives on Electric Power Regulatory Reform: Focus on Retail Competition (Sept. 2001), available at
http://www.ftc.gov/reports/competition-consumer-protection-perspectives-electric-power-regulatory-reform (containing edited compendium of excerpts from previous comments that the FTC and its staff provided to various state and federal agencies).

Proposal. Nor does it motivate the distribution utilities seeking to serve as their own DSP operators to think creatively about ways to minimize the actual or perceived risk of distribution service discrimination. If the REV process lacks a focus on open competition in the selection of DSP operators, it may fall short of its potential to benefit New York electricity customers, who generally will be worse off than under a transparent, competitive procurement approach.\textsuperscript{15}

The Straw Proposal’s assignment of each distribution utility to be its own DSP operator could also preclude the realization of any economies of scale and scope that might follow from consolidating the territories of DSP operators. The Straw Proposal highlights the costs that might arise if independent DSP operators were to duplicate the functions already carried out by distribution utilities.\textsuperscript{16} The Straw Proposal, however, does not apply the same logic to the ways in which consolidation of DSP territories can avoid some duplication of operating and set-up costs. Consolidation of DSP territories also might encourage consideration of inter-area distribution investments that would reduce overall system costs by increasing the efficiency of the distribution network.

For example, given what we have learned about opportunities for cost savings involving dispatch across the seams of transmission systems, could the dispatch of DERs across existing distribution area seams help reduce New York’s electricity system costs at the distribution level? Similarly, could much of the concern about coordination between DSP operators and the NYISO be resolved by retaining the NYISO to serve as the DSP operator in the distribution territories or having the NYISO’s subsidiaries fill such positions? The proposed administrative designation of the distribution utilities as their own DSP operators precludes exploration of any benefits that electric power customers might derive from alternative arrangements. By contrast, an open competitive DSP operator selection process would allow consideration of the alternative sets of potential efficiencies and other benefits to customers.

\textsuperscript{15} Competitive selection processes have become part of the mosaic of wholesale electricity market reforms. As an example of this phenomenon, Congress required FERC to use a competitive selection process to designate an organization to handle grid security issues. Ultimately, FERC selected the incumbent organization – the North American Electric Reliability Corporation (NERC) – but the selection process itself caused FERC and NERC to tighten procedures and clarify relationships.

A transparent and objective selection process could still result in awarding a DSP operator contract to the incumbent distribution utility if, for example, the cost of establishing an independent DSP operator proved to be prohibitive. Whatever the outcome, this process should increase current and potential DER investors’ confidence that DSP operators were selected based on the best information about the available alternatives.

\textsuperscript{16} Just as utilities continue to own most of the transmission systems operated by independent system operators (ISOs) and regional transmission organizations (RTOs), utilities could continue to own the distribution systems run by independent DSP operators.
Conclusion on Competitive Designation of DSP Operators

When a decision is as important to the success of the REV process as the selection of DSP operators, we encourage the NY PSC and its staff to rely on an open competitive selection process rather than on an administrative determination. Specifically, we encourage revisions in the Straw Proposal to incorporate a competitive procurement process to determine the DSP operator in each distribution territory, leaving open the possibility that applications for the DSP designations might show that consolidation of two or more DSP territories under a single DSP operator would provide net benefits for customers.

IV. Straw Proposal § VI: “Mitigating Market Power”

Concerned about the prospect of distribution utilities’ vertical and horizontal market power, New York was one of the jurisdictions that encouraged distribution utilities to divest most generation facilities. Now, based on several factors described in Section III.A of the Straw Proposal, there could be a rebundling of distribution and generation by allowing distribution utilities to invest extensively in DERs. At the same time, the Straw Proposal also acknowledges a concern that franchise monopoly distribution utilities would have the ability and incentives to operate the distribution system so as to discriminate against customers and third parties that own (or might own) independent DERs.17

A review of comments on the Straw Proposal makes it clear that there are concerns about the merits of distribution utilities’ serving as their own DSP operators, and that those concerns focus on discriminatory distribution service behavior by utilities serving simultaneously as their own DSP operators and as major investors in DERs in their own distribution territories.

The open competitive procurement process to select among DSP operator applicants that we discussed above is a suitable way to gauge the costs and benefits associated with alternative potential DSP operators and to select an appropriate DSP operator.18 We encourage the NY PSC

17 “These concerns include (1) the potential for a utility-provided platform to maintain barriers, such as burdensome interconnection requirements and outmoded tariffs, to robust entry into the market for DER providers; (2) potential reluctance of a utility-provided platform to provide the system or customer data needed by DER providers to succeed; and (3) the potential for functional competitive advantage on the part of the utility/platform regardless of utility behavior.” Straw Proposal at 67. An additional concern could be discrimination against the dispatch of DERs not owned by the distribution utility. See also James Tong & Jon Wellinghoff, “Rooftop Parity: Solar for Everyone, Including Utilities,” 152:8 Pub. Util. Fortnightly 18 (Aug. 2014), accessible at http://www.fortnightly.com/fortnightly/2014/08/rooftop-parity; Herman K. Trabish, “Jon Wellinghoff: Utilities Should Not Operate the Distribution Grid,” Utility Dive (Aug. 15, 2014), available at http://www.utilitydive.com/news/jon-wellinghoff-utilities-should-not-operate-the-distribution-grid/298286.

18 Transparency in evaluations and decision-making can itself improve market performance by providing information to market participants and by assuaging DER investors’ unwarranted concerns about distribution discrimination.
and its staff to highlight issues involving possible distribution service discrimination by taking account of those issues in the competitive procurement criteria for selecting each DSP operator. We base our recommendation on the lessons learned about transmission service discrimination in the process of restructuring the wholesale electricity market, as explained below. At a minimum, a DSP operator applicant should bear the burden to demonstrate that it will not engage in distribution service discrimination against other DER investors. A DSP operator application should be downgraded or rejected if it does not effectively address concerns over distribution service discrimination. A sufficient case would include ways in which the applicant proposes (1) to eliminate its own incentives to discriminate in providing distribution services and (2) to facilitate the detection, documentation, and prevention of distribution service discrimination.

Although DERs and related advances in technology are major developments in the electric power industry, it remains uncertain how to confer the benefits of these advances on customers. DERs are a major development, but they are not the first such development in the electric power industry. In the late 1970s, initial efforts to remove barriers to less fossil-fuel-dependent types of generation led to regulatory changes (e.g., the Public Utility Regulatory Policies Act of 1978) as well as to the recognition that the transmission system could be adjusted to accommodate independent power producers of many types.19

The period preceding FERC’s promulgation of Order No. 2000 saw policy developments involving experimentation with various ways to unbundle the transmission system from other utility operations, in order to address concerns over discrimination in transmission service while preserving economies of vertical integration, scale, and scope. A key impetus for putting grid operations in the hands of ISOs and RTOs was the realization that simple behavioral rules against transmission service discrimination would not prevent such discrimination (or the perception of such discrimination) and could not deliver to customers all of the available advantages of wholesale competition. At the same time, the decision to create ISOs and RTOs – rather than to require utilities to divest transmission facilities outright – rested in part on an understanding that ISOs’ and RTOs’ operation of the transmission grid would not entail as many lost economies of vertical integration or increased transaction costs as might stem from a change in transmission ownership patterns or a disruption in the existing arrangements used to build or maintain transmission lines or connect generators to transmission facilities.20

With respect to FERC Order No. 888, the FTC and its staff repeatedly raised this concern about relying exclusively on behavioral rules to prevent transmission service discrimination.


20 Some utilities eventually decided that it would be worth more to concentrate their business at the distribution level than to preserve economies of vertical integration between transmission and distribution. Thus, although they were never required to do so, these utilities sold their transmission assets to newly formed transmission-only utilities (“Transcos”). The largest Transco, ITC, owns parts of the transmission grid operated by the Midcontinent (formerly Midwest) Independent System Operator.
FERC subsequently addressed this concern and articulated this key lesson in the following italicized passage (excerpted from FERC Order No. 2000, with footnotes omitted):\

*With respect to continuing opportunities for undue discrimination, the NOPR observed that, when utilities control monopoly transmission facilities and also have power marketing interests, they have poor incentives to provide equal quality transmission service to their power marketing competitors.* . . .

*In the NOPR, the Commission noted that functional unbundling [that relies on behavioral rules] does not change the incentives of vertically integrated utilities to use their transmission assets to favor their own generation, but instead attempt to reduce the ability of utilities to act on those incentives.*

*The NOPR expressed concern about continuing indications that transmission service problems related to discriminatory conduct remain and concluded that these problems are impeding competitive wholesale power markets. The NOPR also noted that instances of actual discrimination may be undetectable in a non-transparent market.* . . . *The Commission expressed concern that the difficulty in determining whether there has been compliance with our regulations raises the question as to whether functional unbundling is an appropriate long-term regulatory solution.*

*The NOPR explained that the Commission considers allegations of discrimination, even if not reduced to formal findings, to be a serious concern for two reasons. First, this can be indicative of additional, unreported, discriminatory actions, because there are significant disincentives to filing and pursuing formal complaints that would result in definitive findings.* . . . *Second, the NOPR explained that allegations of discrimination are serious because, if nothing else, they represent a perception by market participants that the market is not working fairly. If market participants perceive that other participants have an unfair advantage through their ownership or control of transmission facilities, it can inhibit their willingness to participate in the market, thus thwarting the development of robust competition. The NOPR added that such mistrust can also harm reliability.* . . .

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21 The quoted material appears in FERC, Order No. 2000, at 35-38 (Dec. 20, 1999), available at [http://www.ferc.gov/legal/maj-ord-reg/land-docs/RM99-2A.pdf](http://www.ferc.gov/legal/maj-ord-reg/land-docs/RM99-2A.pdf). The Appendix to this comment contains the text of the full passage that includes these quotes. In footnote 68 of Order No. 2000, FERC stated: “As noted in the NOPR [Notice of Proposed Rulemaking], in Order No. 888, the Commission received and considered numerous comments that functional unbundling was unlikely to work, and that more drastic restructuring, such as corporate unbundling, was needed. For example, the Federal Trade Commission advised the Commission that a functional unbundling approach ‘. . . would leave in place the incentive and opportunity for some utilities to exercise market power in the regulated system. Preventing them from doing so by enforcing regulations to control their behavior may prove difficult.’ However, the Commission decided at the time to adopt the less intrusive and less costly remedy of functional unbundling.”
Also, a system that attempts to control behavior that is motivated by economic self-interest through the use of standards of conduct will require constant and extensive policing and requires the Commission to regulate detailed aspects of internal company policy and communication. . . . The NOPR stated that the perception that many entities that operate the transmission system cannot be trusted is not a good foundation on which to build a competitive power market, and it created needless uncertainty and risk for new investments in generation.

We believe that the NY PSC can apply the valuable learning from FERC’s experience and can avoid over-reliance on behavioral rules to prevent distribution service discrimination in the REV project. We do not know of any attribute of the distribution level of the electricity industry in New York State that would protect against vertical market power in the form of distribution system service discrimination (or make it less susceptible to discrimination than the wholesale level). Indeed, the threat of discrimination in the provision of service may be greater at the distribution level than at the transmission level because of greater information asymmetries between the distribution utility/DSP operator and the customer. The distribution utilities know the technology and regulations, while most residential and small commercial (or industrial) customers considering investing in DERs are likely to be unsophisticated regarding distribution service discrimination.

**Recommendation for DSP Market Monitors and Their Selection**

One additional institutional arrangement – the establishment of DSP market monitors – could also prove useful in addressing potential DER investors’ concerns about potential distribution service discrimination. The addition of market monitors to the REV project’s Track One Straw Proposal could also help reduce the perceived risk of distribution service discrimination among customers and third-party owners of existing DER facilities. Again, the experience gained in restructuring wholesale power markets can provide useful guidance. In implementing transmission restructuring, FERC encouraged ISOs and RTOs to contract for expert help to monitor market performance, identify potential rules changes to improve market performance, analyze the likely impacts of stakeholder proposals, and undertake other tasks to protect competition. The resulting independent market monitors provide a valuable added perspective and contribute expertise to the resolution of many issues in organized wholesale markets (including the important topic of interactions between retail and wholesale power markets). NY PSC staff may wish to add to the Straw Proposal a recommendation for independent market monitors for the DSP operators. As with the designation of DSP operators, we recommend using a competitive procurement process to select the market monitors.

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22 If the NY PSC staff knows of any features of the distribution level in New York State that would protect against distribution service discrimination, it would be helpful to revise the Straw Proposal by detailing those features in order to reassure potential DER investors.

23 At least at the transmission level, many independent power producers that could be subject to transmission service discrimination are relatively sophisticated about transmission technology and regulations, and some are even affiliates of transmission-owning utilities. This would better equip them to detect, document, and challenge transmission service discrimination.
Moreover, as we observed above regarding the scope of DSP operations, we recommend further consideration of whether consolidation of DSP areas for market monitoring would be a better way to deliver benefits to electricity customers.  

V. Additional Considerations

We encourage the PSC staff to address the following questions as additions to the Straw Proposal, particularly if distribution utilities serve as DSP operators and invest in DERs within their respective distribution territories:

- If distribution utility/DSP operators start investing in DERs, this will create incentives to discriminate in the provision of electricity distribution services against rival DER investments owned by customers or third parties. With respect to this conflict of interest between a distribution utility’s role as DSP operator and its role as DER owner, what disclosure is appropriate and necessary to avoid deception of electricity customers and third parties contemplating new or expanded DER investments in New York State?

- If distribution utilities are to serve as their own DSP operators, would it be appropriate to prescribe the adoption of performance-based rates that include incentives to connect independent DER facilities to the distribution system? Would this approach add significantly to the portfolio of measures that the Straw Proposal recommends in order to discourage distribution service discrimination by distribution utilities/DSP operators?

VI. Conclusion

The FTC staff appreciates the opportunity to provide this reply comment. If you have any questions or comments, please contact John H. Seesel, Office of the General Counsel, at (202) 326-2702.

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24 As mentioned in Section III of this comment, the independent market monitor for the NYISO – a position tasked with evaluating and encouraging transmission-level market performance in New York State – could be a good candidate for concurrent appointment as monitor over one or more distribution-level markets throughout the state.
Continuing Opportunities for Undue Discrimination

With respect to continuing opportunities for undue discrimination, the NOPR observed that, when utilities control monopoly transmission facilities and also have power marketing interests, they have poor incentives to provide equal quality transmission service to their power marketing competitors. The NOPR explained that the Commission had made this point in Order No. 888:

It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.

In the NOPR, the Commission noted that functional unbundling does not change the incentives of vertically integrated utilities to use their transmission assets to favor their own generation, but instead attempt to reduce the ability of utilities to act on those incentives.

The NOPR expressed concern about continuing indications that transmission service problems related to discriminatory conduct remain and concluded that these problems are impeding competitive wholesale power markets. The NOPR also noted that instances of actual discrimination may be undetectable in a non-transparent market and, in any event, it is often hard to determine, on an after-the-fact basis, whether an action was motivated by an intent to favor affiliates or simply reflected the impartial application of operating or technical requirement. The NOPR added that, while continued discrimination may be deliberate, it could also result from the failure to make sufficient efforts to change the way integrated utilities have done business for many years. The Commission expressed concern that the difficulty in determining whether there has been compliance with our regulations raises the question as to whether functional unbundling is an appropriate long-term regulatory solution.

25 We have omitted some footnotes from this excerpt.

26 At this point, footnote 69 of Order No. 2000 reads in pertinent part: “The NOPR described specific examples of undue discrimination that had been brought to its attention through formal complaints, informal complaints made to the Commission's enforcement hotline, oral and written comments made in conjunction with public conferences held by the Commission, and pleadings filed with the Commission in various dockets. . . .”
The NOPR explained that the Commission considers allegations of discrimination, even if not reduced to formal findings, to be a serious concern for two reasons. First, this can be indicative of additional, unreported, discriminatory actions, because there are significant disincentives to filing and pursuing formal complaints that would result in definitive findings.27 The NOPR expressed a concern that actual problems with functional unbundling may be more pervasive than formally adjudicated complaints would suggest. Second, the NOPR explained that allegations of discrimination are serious because, if nothing else, they represent a perception by market participants that the market is not working fairly. If market participants perceive that other participants have an unfair advantage through their ownership or control of transmission facilities, it can inhibit their willingness to participate in the market, thus thwarting the development of robust competition. The NOPR added that such mistrust can also harm reliability.

The NOPR explained the potential for undue discrimination increases in a competitive environment unless the market can be made structurally efficient and transparent with respect to information, and equitable in its treatment of competing participants. Also, a system that attempts to control behavior that is motivated by economic self-interest through the use of standards of conduct will require constant and extensive policing and requires the Commission to regulate detailed aspects of internal company policy and communication. The NOPR added that functional unbundling does not necessarily promote light-handed regulation and undoubtedly imposes a cost on those entities that have to comply with the standards of conduct and abide by rules that limit the flexibility of their internal management activities. The NOPR stated that the perception that many entities that operate the transmission system cannot be trusted is not a good foundation on which to build a competitive power market, and it created needless uncertainty and risk for new investments in generation.

27 Here, footnote 70 of Order No. 2000 reads: “As noted in the NOPR, transmission customers are reluctant to make even informal complaints because they fear retribution by their transmission supplier; the complaint process is costly and time-consuming; the Commission's remedies for violations do not impose sufficient financial consequences on the transmission provider to act as a significant deterrent; and, in the fast-paced business of power marketing, there may be no adequate remedy for the lost short-term sales opportunities in after-the-fact enforcement.” (Citation omitted.)