
FERC Enforcement Office Remains Focused on Market Manipulation and Compliance Programs

NOVEMBER 29, 2016

This month, the Office of Enforcement (OE) of the Federal Energy Regulatory Commission (FERC) released its tenth Annual Report on Enforcement. The report provides FY2016 statistics on the investigative and enforcement activities conducted by OE's four divisions—Investigations, Audits and Accounting, Energy Market Oversight, and Analytics and Surveillance. [View the full report.](#)

This year, in addition to OE's annual report, FERC staff issued a retrospective “lessons learned” white paper, available [here](#), on the implementation of its anti-market manipulation enforcement program since the passage of the Energy Policy Act of 2005 (EPAAct 2005), as well as a second white paper, available [here](#), on effective energy trading compliance programs.¹

Highlights

OE's annual report confirms that, in FY2017, OE intends to remain focused on (1) fraud and market manipulation, (2) serious violations of reliability standards, (3) anticompetitive conduct, and (4) conduct that threatens the transparency of regulated markets.

Specific statistics in the report include the following:

- FERC opened 17 investigations in FY2016, 12 of which involved market manipulation. These 17 new investigations arose from referrals from FERC program offices, surveillance by FERC and organized market monitoring units, self-reports, and “hotline” tips.
- FERC received 110 new self-reports from a variety of market participants in FY2016. FERC closed 126 self-reports that had been submitted in FY2016 and previous years. As in previous years, one of the many factors OE staff considered in closing self-reports was the absence of significant harm to the market.
- FERC issued four notices of alleged violations in FY2016, three of which involved alleged energy market manipulation.
- FERC approved settlement agreements in FY2016 that resolved allegations of market manipulation by 10 entities, including corporate entities and individual traders. These settlements assessed a total of \$12.2 million in civil penalties and required the

disgorgement of \$5.7 million.

- FERC issued three orders to show cause (OSCs) in FY2016, all of which involved alleged market manipulation. These OSCs proposed a total of \$257.1 million in penalties and the disgorgement of nearly \$13.6 million. FERC is seeking to enforce these OSCs, as well as others from previous years, in federal court. As a result, FERC is seeking to recover a total of \$567.2 million in civil penalties and \$45.7 million in unjust profits through seven litigation proceedings.

The “lessons learned” white paper provides FERC staff’s views on what actions constitute market manipulation, including:

- market behavior with an illicit purpose;
- uneconomic conduct;
- conduct inconsistent with market fundamentals of supply and demand;
- cross-market manipulation schemes;
- gaming of market rules; and
- misrepresentations and omissions.

The “lessons learned” white paper also identifies three mitigating factors that have played a significant role in shaping FERC staff’s penalty determinations: (1) a commitment to compliance, (2) self-reporting and (3) cooperation. Finally, the “lessons learned” white paper provides a few examples from recent OE annual reports in which staff decided to close investigations (which are largely nonpublic). In those examples, FERC staff found insufficient evidence of manipulative intent.

The second white paper, on effective compliance programs, discusses practices that companies may use to prevent and detect market manipulation. Those practices, which draw upon FERC guidance² and the Federal Sentencing Guidelines,³ include:

- appropriate organizational structure and composition;
- diligent recruitment and hiring practices;
- appropriate compensation incentives;
- regular training;
- effective information technology (IT) resources;
- appropriate trading rules and restrictions;
- effective monitoring of trading;
- adequate enforcement of compliance rules and restrictions; and
- regular performance audits and corrective actions.

FERC’s Anti-Market Manipulation Enforcement Program

EPA 2005 amended both the Federal Power Act and the Natural Gas Act to enhance FERC’s authority to prohibit market manipulation and assess significant penalties where manipulation was determined to have occurred. Since then, FERC’s investigative, analytical and surveillance capabilities have continued to expand, and the agency has assessed \$641 million in civil penalties, ordered \$402 million in disgorgement and imposed requirements for energy companies to implement measures to improve compliance.⁴

FERC's enforcement efforts received a boost in April 2015 when Norman Bay, a former federal prosecutor and former head of OE, became FERC chairman. During Chairman Bay's tenure, FERC's enforcement efforts remained aggressive.

The recent election of Donald Trump as president has the potential to change that posture. FERC consists of five commissioners who are appointed by the president, and no more than three commissioners may belong to the same political party.⁵ All three sitting commissioners are Democrats. We expect that President Trump will move quickly to fill the open commissioner seats with Republicans, and will also appoint a Republican as FERC chairman. This latter change may result in a shift in OE's priorities—especially if Chairman Bay decides not to continue serving as a commissioner.

Meanwhile, exactly *what* actions constitute manipulation, and *where* the boundaries of FERC's authority begin and end, continue to evolve as more of the subjects of FERC's enforcement actions forgo settlement and elect to enter into litigation with the agency. For example, in 2016, a federal court allowed FERC to bring an enforcement action based on allegations of manipulative intent (i.e., what would have happened), “not whether the alleged plan ultimately worked.”⁶ Also in 2016, several courts addressed the scope of “*de novo* review” that governs the enforcement process under the Federal Power Act.⁷ While FERC has taken the position that *de novo* review should be based upon the “administrative record” and that full discovery is not required, federal courts have decided that *de novo* review means treating these cases as ordinary civil actions governed by the Federal Rules of Civil Procedure “subject to proper limitations on discovery that take proportionality into account” and culminating, “if necessary, in a jury trial.”⁸

Implications

1. OE's FY2016 annual report confirms that OE intends to continue to investigate and enforce against entities that engage in manipulative conduct in energy markets. The aggressiveness of enforcement efforts, however, may be mitigated as the makeup of the Commission changes.
2. As FERC continues to take action against market manipulation, a body of case law is developing that will provide more clarity on FERC's jurisdiction and what types of activities constitute manipulation in the energy trading context. In its “lessons learned” white paper, FERC staff have set forth examples of the types of activities it may investigate and enforce against. Although those examples do not have the force of regulatory authority, regulated entities should be familiar with those examples, and should continue to monitor ongoing cases and incorporate new precedent into their compliance programs.
3. OE's FY2016 annual report, along with the staff white paper on compliance programs, confirms the important role that effective compliance programs continue to play in FERC enforcement decisions. Companies with effective compliance programs may benefit by preventing energy trading from violating the Anti-Manipulation Rule⁹ in the first place, or, if a violation occurs, by being able to present a stronger case for reduced penalties.

WilmerHale's [Energy, Environment and Natural Resources Practice](#) actively monitors developments at FERC, the Commodity Futures Trading Commission and other entities with jurisdiction over energy markets, advises regulated entities on the development and implementation of compliance programs, and represents entities in investigation and enforcement actions.

¹ Both white papers include a disclaimer that they are the product of FERC staff, and “do not necessarily reflect the views of the Commission, its Chairman, or any individual Commissioner.”

² See *Enforcement of Statutes, Orders, Rules, and Regulations*, 132 FERC ¶ 61,216 (2010) (Revised Policy Statement on Penalty Guidelines); *Enforcement of Statutes, Orders, Rules, and Regulations*, 130 FERC ¶ 61,220 (2010) (Policy Statement on Penalty Guidelines); *Compliance with Statutes, Regulations, and Orders*, 125 FERC ¶ 61,058 (2008) (Policy Statement on Compliance); *Enforcement of Statutes, Regulations, and Orders*, 123 FERC ¶ 61,156 (2008) (Revised Policy Statement on Enforcement); *Enforcement of Statutes, Orders, Rules, and Regulations*, 113 FERC ¶ 61,068 (2005) (Policy Statement on Enforcement).

³ [U.S. Sentencing Commission, Guidelines Manual § 8B2.1\(b\)\(1\)-\(7\)](#).

⁴ FERC, All Civil Penalty Actions, www.ferc.gov/enforcement/civil-penalties/civil-penalty-action.asp.

⁵ 42 U.S.C. § 7171(b)(1).

⁶ *FERC v. Maxim Power Corp.*, 2016 U.S. Dist. LEXIS 107770 (D. Mass. July 21, 2016).

⁷ See, e.g., *id.*; *FERC v. City Power Mktg., LLC*, 2016 U.S. Dist. LEXIS 105421 (D.D.C. Aug. 10, 2016).

⁸ *FERC v. Maxim Power Corp.*, 2016 U.S. Dist. LEXIS 107770 (D. Mass. July 21, 2016).

⁹ 18 C.F.R. Part 1c.

Authors



H. David Gold

SPECIAL COUNSEL

✉ david.gold@wilmerhale.com

☎ +1 617 526 6425