

June 19, 2019

**Re: Energy Associations' White Paper on FERC Enforcement
Docket No. AD07-13-000**

Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

Dear Secretary Bose:

Please find attached a White Paper entitled “Enhancing the Transparency, Efficiency, and Fairness of the Federal Energy Regulatory Commission’s Enforcement Program” prepared for the American Gas Association, Edison Electric Institute, Electric Power Supply Association, Interstate Natural Gas Association of America, and the Natural Gas Supply Association (the “Energy Associations”) by David A. Applebaum, Jones Day, and Todd L. Brecher, Akin Gump Strauss Hauer & Feld LLP. More than thirteen years have passed since Congress enacted the Energy Policy Act of 2005, and more than a decade since the Federal Energy Regulatory Commission (“Commission”) issued key enforcement policy statements. Now, with the benefit of time and experience, the Commission should revisit its enforcement policies and practices to determine whether there are improvements that can help achieve greater transparency, efficiency, and fairness without undercutting the mission of fostering compliance. By submitting the attached White Paper, the Energy Associations seek to begin this dialogue with the Commission and offer some proposals for consideration.¹

The Energy Associations, whose collective views are expressed in this White Paper, agree with the Commission’s long-stated principle that the overarching and fundamentally important goal of the enforcement program is achieving compliance. The White Paper proposes several incremental steps that would enhance the transparency, efficiency, and fairness of the Commission’s enforcement program, making it even stronger and more effective in achieving compliance. These proposals are not intended to diminish in any way the effectiveness of FERC’s enforcement program, which is a critical aspect to the functioning of our nation’s energy markets.

Please contact us if you need any additional information or have any questions regarding this filing.

¹ In fact, the Commission already addressed one suggestion in the White Paper when it recently rescinded the Notice of Alleged Violations (“NAV”) policy. Enforcement of Statutes, Regulations, and Orders, 167 FERC ¶ 61, 153 (2019).

Energy Associations' White Paper on FERC Enforcement
Docket No. AD07-13-000
June 19, 2019

Sincerely,

American Gas Association

/s/ Matthew J. Agen
Matthew J. Agen
Assistant General Counsel
American Gas Association
400 North Capitol Street, NW
Washington, DC 20001
(202) 824-7090
magen@aga.org

Edison Electric Institute

/s/ Lopa Parikh
Lopa Parikh
Senior Director, Federal Regulatory Affairs
Edison Electric Institute
710 Pennsylvania Avenue, N.W.
Washington, D.C. 20004-2696
lparikh@eei.org
(202) 508-5098

Electric Power Supply Association

/s/ Nancy Bagot
Nancy Bagot, Senior Vice President
Sharon Royka Theodore
Senior Director, Regulatory Affairs
Electric Power Supply Association
1401 New York Ave, NW, Suite 950
Washington, DC 20005
stheodore@epsa.org
(202) 628-8200

Interstate Natural Gas Association of America

/s/ Joan Dreskin
Joan Dreskin
General Counsel
Interstate Natural Gas Association of America
20 F Street, NW, Suite 450
Washington, DC 20001
jdreskin@ingaa.org
(202) 216-5928

Natural Gas Supply Association

/s/ Casey Gold
Casey Gold
Director, Regulatory Affairs
Natural Gas Supply Association
900 17th Street, NW, Suite 500
Washington, D.C. 20006
cgold@ngsa.org
(202) 326-9300

Attachment

**ENHANCING THE TRANSPARENCY, EFFICIENCY, AND
FAIRNESS OF THE
FEDERAL ENERGY REGULATORY COMMISSION'S
ENFORCEMENT PROGRAM**

A WHITE PAPER

Submitted on Behalf of:

**American Gas Association
Edison Electric Institute
Electric Power Supply Association
Interstate Natural Gas Association of America
Natural Gas Supply Association**

Prepared by:

**David A. Applebaum
Jones Day**

**Todd L. Brecher
Akin Gump Strauss Hauer & Feld LLP**

May 15, 2019



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Executive Summary

A core mission of the Federal Energy Regulatory Commission (“FERC” or “Commission”) is to enforce the laws, regulations, and orders under its jurisdiction. This mission was greatly expanded through the Energy Policy Act of 2005 (“EPAct 2005”),² which expressly granted the Commission new enforcement authority and, as a practical matter, called upon the agency to create a robust and effective enforcement program. While the Commission has created a successful and effective enforcement program, with some incremental enhancements, FERC could significantly improve regulatory certainty and stakeholder confidence in its program.

The Commission’s enforcement mission is of critical importance, as effective regulation requires compliance with rules, and markets cannot function properly without efforts to deter fraud and manipulation that could thwart market outcomes. The electric and natural gas industries strive to achieve compliance and have invested enormous effort, time, and resources in creating robust compliance programs. The broad range of energy trade associations, whose collective views are expressed in this White Paper, agree with the Commission’s long-stated principle that the overarching goal of the enforcement program is achieving compliance.³

Now more than thirteen years since Congress passed EPAct 2005, and more than a decade since the Commission issued key enforcement policy statements,⁴ with the benefit of time and experience, the Commission should revisit its enforcement policies and practices to determine whether there are improvements that can help achieve greater transparency, efficiency, and fairness without undercutting the mission of fostering compliance. These values promote greater understanding and acceptance of enforcement actions and civil penalties, lead to swifter resolution of matters, thereby providing industry with more timely compliance lessons, and foster greater confidence and regulatory certainty for market participants.

In keeping with the spirit of a previous white paper on enforcement submitted by these same trade associations during the early stages of developing FERC’s enforcement program,⁵ this White Paper suggests that, with the experience gained over time, there are additional steps the

² Pub. L. No. 109-58, § 119 Stat. 594 (2005).

³ *Compliance with Statutes, Regulations, and Orders*, 125 FERC ¶ 61,058, at P 1 (2008) (“2008 Policy Statement on Compliance”).

⁴ *Enforcement of Statutes, Orders, Rules, and Regulations*, 132 FERC ¶ 61,216 (2010) (“2010 Revised Policy Statement on Penalty Guidelines”); *2008 Policy Statement on Compliance; Enforcement of Statutes, Orders, Rules, and Regulations*, 113 FERC ¶ 61,068 (2005) (“2005 Policy Statement on Enforcement”); *Enforcement of Statutes, Regulations, and Orders*, 123 FERC ¶ 61,156 (2008) (“2008 Revised Policy Statement on Enforcement”). The Office of Enforcement has more recently published two informative and helpful white papers (one dealing with market manipulation law, and the other with energy trading compliance). See FED. ENERGY REG. COMM’N, STAFF WHITE PAPER ON ANTI-MARKET MANIPULATION ENFORCEMENT EFFORTS TEN YEARS AFTER EPACT 2005 (2016), <https://www.ferc.gov/legal/staff-reports/2016/marketmanipulationwhitepaper.pdf?csrt=16753783408539705228>; FED. ENERGY REG. COMM’N, STAFF WHITE PAPER ON EFFECTIVE ENERGY TRADING COMPLIANCE PRACTICES (2016), <https://www.ferc.gov/legal/staff-reports/2016/tradecompliancewhitepaper.pdf?csrt=16753783408539705228>. However, the Commission’s most recent formal statements on enforcement policy, process, and penalties are from 2008 and 2010, at the early stages of the Office of Enforcement’s development.

⁵ WHITE PAPER SUBMITTED ON BEHALF OF AM. GAS ASS’N ET AL.: IMPLEMENTATION OF THE FEDERAL ENERGY REGULATORY COMMISSION’S ENFORCEMENT AUTHORITY (2007), <https://www.ingaa.org/File.aspx?id=5739>.

Commission can take to improve the transparency, efficiency, and fairness of the enforcement process—and offers a number of proposals for consideration. These proposals are not intended to diminish in any way the effectiveness of FERC’s enforcement program, which is a critical aspect to the functioning of our nation’s energy markets. Rather, these proposals address specific areas where, based on experience with the current process, improvements are possible, while ensuring that the enforcement program continues to remain strong.

Below is a brief summary of the proposals discussed in this White Paper that could enhance the effectiveness of FERC’s enforcement program and which are based on the experience of a broad range of energy market participants and experts. Importantly, these proposals do not require statutory amendments and, in most cases, do not require changes to the Commission’s existing regulations. Rather, most of these proposals can be implemented through a range of possible actions, including simply improving current Office of Enforcement (“Enforcement”) practices and procedures, changing internal staff policies, or issuing formal policy statements.

1. Increase Transparency with Investigation Subjects. Investigation subjects often find the investigation process to be insufficiently transparent—with only minimal detail provided about the investigation and rarely any meaningful opportunity for a dialogue with staff about the investigation until the very end of the process. Enforcement is also insufficiently transparent when it comes to disclosing relevant data and documents to the subject (including exculpatory information)—which it generally does not do until the investigation is largely complete. Increased transparency would promote fairness, make investigations more efficient, and provide industry with increased confidence in the investigation process. To increase transparency, Enforcement should: (a) have earlier and more frequent meetings with subjects and their counsel to discuss the facts and potential violations at issue in detail; (b) explain the scope of an investigation at the outset, provide the referral and other relevant documents, and explain when the scope of the investigation changes; (c) provide subjects with exculpatory information (“Brady” material) and other information relevant to the conduct under investigation at an earlier stage in the process; and (d) publish an Enforcement Procedures Manual. Further, the Commission should: (e) not allow certain Enforcement staff to advise the Commission on enforcement adjudications by exempting them from the “non-decisional” designation; and (f) provide subjects with a greater opportunity to state their case to Commissioners before the Commission initiates a public enforcement action.

2. Make Investigations More Efficient. Enforcement investigations often last for years, even when they involve discrete conduct or straightforward facts. There are steps the Commission can take to create a more expedited yet thorough investigative process by ensuring that: (a) data requests are limited in scope to the conduct under investigation; (b) Enforcement relies upon the most up-to-date methods for ensuring they have adequate investigative discovery, including search engine technology; (c) interviews are relied upon more frequently as an alternative to depositions; and (d) staff strives to complete its fact-gathering within six months—and if it takes longer, explain why.

3. Ensure Civil Penalties Are Transparent and Not Higher Than Necessary to Achieve Compliance. The Commission has made clear that the focus of its enforcement efforts is not assessing penalties, but rather achieving compliance. While the Commission’s 2010 *Revised Policy Statement on Penalty Guidelines* (“Penalty Guidelines”) has made penalty determinations

more transparent, in many cases, penalties appear to exceed what is necessary to achieve compliance. The Commission should revise certain aspects of the Penalty Guidelines and how they are applied to ensure civil penalties are reasonably calibrated to the violation and not higher than necessary to achieve compliance. The Commission should also authorize downward departures from the Penalty Guidelines more frequently when the facts suggest a lower penalty is justified and reasonable under the circumstances.

4. Formally Repeal the Notice of Alleged Violations Policy. The Commission implemented the Notice of Alleged Violations (“NAV”) policy in 2011 to provide for early public disclosure of investigations (including subjects’ identities). The NAV policy has proved to be both ineffective, not yielding the benefits the Commission intended, and damaging to subjects whose identities are publicly disclosed before the Commission has decided whether there is a basis to bring a case. Therefore, the Commission should formally rescind the NAV policy.

5. Improve Enforcement Policies to Promote Market Participation and Liquidity, Including Through Reforms to FERC’s Price Reporting Policy. The Commission should ensure that Enforcement policies, in general, promote rather than hinder market participation and liquidity, particularly since robust market participation and liquidity make markets more efficient and less susceptible to manipulation. To reduce the risk and regulatory burden faced by companies who price report, the Commission should reform its policy on price reporting, including its “safe-harbor” policy and audit processes.

6. Address FPA Enforcement Action Procedures and Statute of Limitations Policy in Light of Court Rulings. The recent series of Federal Power Act (“FPA”) market manipulation cases to be litigated in federal district courts have led to several decisions addressing the procedures applicable to “*de novo* review” district court actions and how the five-year statute of limitations should be applied in such cases. To provide greater regulatory certainty for market participants, the Commission should formally recognize the courts’ finding that *de novo* review enforcement actions under the FPA will be filed in federal district court as ordinary civil actions, not truncated agency “review” proceedings. Second, while courts have reached different conclusions about how to apply the five-year statute of limitations in *de novo* review cases, the Commission should nevertheless promote fairness and efficiency by deciding as a matter of policy that it will file *de novo* review enforcement actions in federal court within five years of the alleged unlawful conduct, not merely within five years of the Commission’s administrative penalty assessment.

7. Improve the Transparency and Efficiency of Audits. The audit process should also be made more transparent and efficient by adopting the following recommendations: (1) keeping the audit scope clear and defined; (2) using standardized data requests when possible; and (3) providing periodic updates on common errors and findings in audits.

I. Increase Transparency with Investigation Subjects

The Commission has long recognized the importance of transparency in its enforcement program and has taken important steps over the years to increase transparency to the public and regulated community.⁶ However, investigation subjects often find the investigation process itself to be insufficiently transparent *to them*. Subjects often are only provided minimal detail about the scope of an investigation, staff's concerns, and staff's preliminary views of the facts and potential violations at the beginning of the investigation and as the investigation proceeds. This continues until the investigation is nearing completion, when Enforcement staff is at the stage of considering closing or moving forward with the case. While there are exceptions in particular cases, Enforcement staff generally shares very little about its views until the investigation is nearly complete, which frequently takes years. This is often true even when subjects seek to proactively engage Enforcement staff during the investigation through informal outreach and meetings. In response, Enforcement staff often is hesitant to share information about the investigation or its views since it is "still investigating." Similarly, subjects also often are not provided relevant data and documents until the investigation is largely complete—even when the information is exculpatory ("*Brady*" material) or would assist the subject and its employees in recalling, understanding, and explaining the conduct at issue.

Staff has at times sought to justify this approach based on a concern that being more transparent with subjects could allow them to craft false explanations or defenses to alleged misconduct. The possibility that this might occur is a risk in enforcement investigations generally (whether at FERC or other agencies), but it does not mean that increased transparency cannot be achieved. Furthermore, limiting transparency based on this concern is rarely necessary given the skill and sophistication of Enforcement's attorneys and analysts. The notion that providing subjects more transparency into staff's views, or sharing relevant documents and data, would jeopardize staff's ability to uncover misconduct is belied by Enforcement's track record of uncovering various forms of misconduct—which frequently has required Enforcement to disprove explanations offered by subjects (and witnesses) during the investigation. Instead, in the large majority of instances, understanding the nature of an investigation and staff's views and concerns would allow subjects to engage with staff more collaboratively and efficiently, including by providing relevant information and identifying knowledgeable employees. Similarly, having access to relevant data about the conduct at issue, including trade data, would allow subjects to better recall and explain the specific conduct. Without this information, the subject is at a disadvantage and not able to fully defend itself.

Transparency not only makes investigations more efficient and effective, but promotes a sense of fairness and trust, which is beneficial to the Commission, investigation subjects, and the overall process. In many instances, Enforcement staff's unwillingness to share information and provide greater transparency creates circumstances where the individuals staff seeks to interview or depose may not be the most knowledgeable about the core factual concerns at issue because the investigative subject is not aware of those concerns. Likewise, a lack of transparency can create

⁶ For example, in the *2008 Revised Policy Statement on Enforcement*, the Commission directed Enforcement to begin releasing an annual report each year providing transparency into enforcement activities of the preceding year. *2008 Revised Policy Statement on Enforcement* at P 12. The Penalty Guidelines were another effort by the Commission to make the enforcement program more transparent.

difficulties for an investigative subject seeking to provide “responsive” material to a data request because the subject is not as well-positioned to ascertain “responsiveness” or the most knowledgeable custodian of sought-after information. Moreover, it is frustrating and disheartening for corporate and individual investigation subjects to face years of investigation—including numerous requests for data and testimony—without actually knowing staff’s concerns and the facts underlying those concerns, or being able to access information that could assist them in providing accurate information and explanations for business decisions.

Below we provide proposals to improve transparency during investigations. Whether these or other transparency improvements are adopted, one overarching recommendation is that these improvements be a part of a uniform, consistent, standard practice followed by all Enforcement staff, so that investigation subjects feel that their investigation is fair, transparent, and efficient.

A. Enforcement Should Have Earlier and More Frequent Meetings with Subjects and their Counsel to Discuss the Facts and Potential Violations at Issue in Detail

The entire investigative process runs more efficiently and fairly when Enforcement staff engages with the subject early so that the subject understands what is being investigated and why. Providing subjects with an understanding of the investigation is a fundamental tenet that should be adhered to so that investigations can be completed in a manner that promotes fairness, thoroughness, and cooperation. Industry participants believe it would be productive for both staff and the subject of an investigation, or their counsel, to have ongoing meaningful engagement long before the preliminary findings process has even started (if an investigation reaches that point). While Enforcement staff can be receptive to requests from subjects to meet to discuss the investigation before preliminary findings, staff are usually hesitant to share their views. Having an investigation pending for a long time without understanding staff’s views can create enormous and unnecessary uncertainty for subjects, who of course have continuing business interests and obligations to participate in FERC-regulated markets. This, in turn, can cause the process to become more adversarial than need be the case.

This approach is unnecessary and counterproductive. Enforcement staff should be willing to meet with subjects early and regularly to discuss the investigation, including staff’s concerns, initial view of the facts, and potential violations—well before staff starts to form preliminary findings. Earlier meetings and engagement with subjects can also lead to a more efficient investigation. Information that staff has often sought to obtain through more formal and burdensome investigative discovery can be discussed openly at the outset of the investigation, such as how the subject’s business is organized, which employees were likely involved in certain activities or have pertinent information, and which sources of documents are likely to be most relevant and important—allowing staff to better focus its investigative work.

B. Enforcement Should Explain the Scope of an Investigation at the Outset, Provide the Referral and Other Relevant Documents, and Explain When the Scope of the Investigation Changes

The importance of regular and transparent meetings with Enforcement staff is perhaps most important at the outset of the investigation. Enforcement should provide information such that subjects understand the scope of an investigation when it begins. Some information about the

scope of the investigation is provided when staff issues a directive to the subject to preserve data. However, the explanation can be vague, particularly when the scope of the preservation directive is broader than the actual investigation and only generally refers to the type of potential violation being investigated, e.g., market manipulation or a tariff violation, without providing information about the specific conduct and why it is potentially a violation. In investigations arising from market monitor referrals, which constitute a significant percentage of investigations, Enforcement should provide the subject with a copy of the referral, with redactions as needed to protect confidential information. While there may be investigative reasons not to provide the referral itself in certain cases, Enforcement can still provide subjects with as much substantive detail about the market monitor's concerns as possible to better inform subjects why the investigation was commenced. Market monitors often conduct their own inquiries prior to making a referral, so the fact that the impetus of the investigation was a referral is often known to the subject. Disclosing the referral will allow the subject to understand the market monitor's concerns, which can allow the subject to address the matter with Enforcement more efficiently and proactively. To the extent the referral is based on a misunderstanding or miscommunication between the subject and the market monitor, disclosing the referral will allow the subject to address the misunderstanding or miscommunication—again potentially facilitating a more efficient resolution.

Staff should also provide written notice to inform subjects when it expands or changes the scope of the investigation and explain why it is doing so. Staff, of course, can and should modify the scope of an investigation when there is good cause to do so. When that occurs, Enforcement should explain the change or expansion to the subject when it happens—rather than the subject having to infer it from future data requests and deposition questions.

Finally, the Commission should ensure parties are informed in writing when an investigation is closed. In many instances, staff informs the subject's counsel over the phone that the investigation is being closed. Subjects, however, often need assurance in writing that the investigation has been closed without action for purposes of apprising internal stakeholders or meeting external reporting obligations. Furthermore, clarity on the conclusion of an investigation allows the subject to ease administrative burdens, such as the release of legal document hold requirements in connection with the investigation. Although staff provides written notice of closure in some instances, it is not standard practice. The Commission should create a uniform policy of informing the subject in writing that the matter has been closed and the document hold has been lifted.

C. Enforcement Should Provide Subjects with Brady Material and Other Information Relevant to the Conduct Under Investigation (Including Trade Data) Early in the Process

The Commission appropriately adopted a *Brady* policy, which requires disclosure of exculpatory material to the investigation subject.⁷ A *Brady* policy promotes fairness and due process, which are essential to an effective enforcement program. However, staff's *application* of

⁷ *Enforcement of Statutes, Regulations, and Orders*, 129 FERC ¶ 61,248 (2009). “*Brady*” refers to *Brady v. Maryland*, 373 U.S. 83, 88 (1963), where the Supreme Court held that the Due Process Clause of the Fifth Amendment requires disclosure of exculpatory evidence “material to guilt or punishment” known to the government but unknown to the defendant in criminal cases.

the *Brady* policy has been inconsistent with the policy with respect to both the timing and substance of disclosures. Subjects often find that Enforcement does not disclose *Brady* material until at, or near the end of, an investigation, even though the Commission’s policy is for information to be provided “[d]uring the course of [the] investigation.”⁸ Also, as discussed below, there is an overly narrow view of what constitutes *Brady* material. Ensuring a policy of increased—and earlier—disclosure of relevant information in general would not only reduce the number of *Brady* disputes and claims that Enforcement is not properly adhering to the policy but would also lead to a fairer and more efficient investigation process.

One recurring example that highlights subjects’ concerns with the application of the *Brady* policy and Enforcement’s overall approach to disclosure of information in investigations is trade data in market manipulation investigations. Not providing the company with relevant trade data makes it difficult for the company and the trader to fully recall and explain their trading, thereby hindering their ability to defend their actions. While this information may constitute *Brady* material in some investigations but not others, in *all* such investigations it is necessary for the subject to understand and explain the conduct at issue. Therefore, the information should be provided as both a matter of fundamental fairness and due process, and to promote a more efficient and effective investigation process.

This includes not only trade data on executed transactions, which subjects typically already have, but also on unconsummated bids and offers, i.e., the trades they *tried* to make but could not, which provide the full picture of how the trader sought to transact. In many trading investigations—particularly investigations into “open market” trading (e.g., bilateral energy trading on an exchange platform such as the Intercontinental Exchange (“ICE”))—staff obtains the subject’s trading data at or near the outset of the investigation, if not before, but does not provide the data to the subject until much later, if ever. If staff closes the investigation, the subject may never receive the data. If staff issues preliminary findings, staff might provide the data to the subject at that time—years into the process, and after the trader has been required under oath to explain his or her trading. This practice raises both *Brady* concerns and highlights how it is unfair and counterproductive not to provide relevant information to the subject during the investigation.

From a *Brady* standpoint, trade data can often be exculpatory. Many trading investigations concern allegations of intentionally uneconomic trading, i.e., selling at an uneconomically low price or buying at an uneconomically high price to affect a financial index. Unconsummated trade data can show that the trader attempted to transact at more favorable prices but was unable to find willing counterparties. In the context of an investigation into uneconomic selling, for example, evidence that a trader offered to sell at \$4.00 but could not find a willing counterparty would cast doubt on a claim that a subsequent sale at \$3.90 was intentionally uneconomic. Enforcement often takes the position that this data, even in the context outlined above, is not exculpatory—reflecting an overly narrow view of *Brady*.

Yet this is also an example of information that should be provided to investigation subjects as a matter of course—regardless of whether the information is *Brady* material. In a trading investigation, Enforcement, through data requests and depositions, asks the company and the specific trader to explain their reasoning for certain trading practices. There is no good

⁸ *Id.* at P 9.

investigative reason to deny a trader relevant data about their own trading activities when they are being asked to explain those activities to the government. Rather, it is in everyone's interest that the subject in this situation have the basic factual information about the trading under investigation—and even if not *Brady* material, it should be provided as a matter of fairness to the subject and to promote a more efficient and effective fact-finding process.

Trade data is one common example of information that should be provided to investigation subjects. However, there is often other information obtained by Enforcement staff through its investigative powers that subjects could explain and put in context, if given the chance to do so. In sum, the best approach is for the Commission to adopt a policy that ensures subjects are provided *all* data that can assist them in recalling and explaining the facts, early in the investigation and before any depositions are taken. Providing the data would make the investigation process more productive, efficient, fair, and accurate, without compromising any investigative need on FERC's part.

D. Enforcement Should Create a Procedures Manual to Instill Further Confidence in the FERC Investigatory Process

Enforcement should publish an enforcement procedures manual to provide the regulated community, practitioners, and the public guidance and transparency into its investigation practices and procedures. Enforcement divisions of other federal agencies, including the Commodity Futures Trading Commission (“CFTC”), Securities and Exchange Commission (“SEC”), Department of Justice Antitrust Division, and the Consumer Financial Protection Bureau, among others, publish manuals that provide extensive detail on their respective enforcement practices and procedures.⁹ A manual would provide guidance and certainty to market participants and help ensure that Enforcement staff approach issues with a common process. While the Commission's *2008 Revised Policy Statement on Enforcement* provides some overview of the investigative process, this guidance is now dated, having been issued more than ten years ago and while Enforcement was still developing its modern-day enforcement program. FERC's Enforcement website has been updated more recently, but provides only a basic, high-level overview of the process (though such information could provide the starting point for a more detailed manual).¹⁰

A manual would provide subjects and their counsel with a better understanding of how Enforcement conducts investigations and the general expectations of the staff assigned to those investigations—which would increase both the transparency of the process and the efficiency of investigations (an issue discussed in more detail below in Section II). It would also promote greater consistency and standardization within Enforcement. Subjects and their counsel have often

⁹ See COMMODITY FUTURES TRADING COMM'N, DIV. OF ENFORCEMENT, ENFORCEMENT MANUAL (2019), <https://www.cftc.gov/LawRegulation/Enforcement/EnforcementManual.pdf>; SEC. & EXCH. COMM'N, DIV. OF ENFORCEMENT, ENFORCEMENT MANUAL (2017), <https://www.sec.gov/divisions/enforce/enforcementmanual.pdf>; DEP'T OF JUSTICE, ANTITRUST DIV., ANTITRUST DIVISION MANUAL (5th ed. 2012), <https://www.justice.gov/atr/file/761166/download>; CONSUMER FIN. PROT. BUREAU, OFFICE OF ENFORCEMENT, POLICIES AND PROCEDURES MANUAL (3rd ver. 2017), https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201710_cfpb_enforcement-policies-and-procedures-memo_version-3.0.pdf.

¹⁰ See *FERC Enforcement Process*, <https://www.ferc.gov/enforcement/investigations/process.asp?csrc=4426472420851231339> (last updated May 30, 2014).

found it problematic that different Enforcement attorneys and staff have different understandings of basic policies and procedures. The manual could clarify issues where there have been conflicting messages, such as whether company counsel can attend employee depositions, when a transcript must be made available to a witness's counsel, and when and why subjects should refrain from keeping exhibits used at depositions. Also, a manual could provide much-needed consistency in the application of existing FERC policy, for example, when it is appropriate to delay providing subjects transcripts of their depositions and what constitutes a "good cause" standard for withholding a transcript.¹¹

A manual would also be an efficient method for Enforcement to communicate policy and practice changes to industry quickly and uniformly by updating the manual and announcing the update on FERC's website. Many of the suggested improvements above regarding increasing transparency in investigations could be codified in the manual as well.

E. No Enforcement Staff Should Be Exempted from the "Non-Decisional" Designation and Allowed to Advise the Commission on Enforcement Adjudications

Currently, the Commission has a practice of allowing Enforcement staff to advise the Commission on the adjudication of enforcement cases following an Order to Show Cause, provided that such staff did not directly work on the investigation team. When the Commission issues an Order to Show Cause, it designates Enforcement staff as "non-decisional," but specifically provides an exception to a team of Enforcement staffers that are then allowed to communicate with the Commission and other decisional staff off-the-record and advise the Commission on the case, including by drafting the Commission's order resolving the Show Cause proceeding.¹² Allowing Enforcement staff to help adjudicate enforcement cases erodes trust in the fairness of the process, and the Commission should reconsider this practice going forward.

¹¹ Rule 1b.12 of the Commission's regulations only allows a transcript to be withheld for "good cause," though in such instances the witness or his or her counsel "shall have the right to inspect the official transcript of the witness' own testimony." 18 C.F.R. § 1b.12 (2019). Enforcement has stated publicly on multiple occasions that it grants subjects (or their counsel) access to transcripts "immediately" in the "vast majority of cases," and only withholds or delays access when there is "good cause," which it defines as "situations where there is reason to believe that a witness may use the transcript to help develop false testimony; where the witness may use the transcript to coach another witness (in contravention of the Commission's witness sequestration rule); and where a witness may be intimidated or unwilling to testify fully and truthfully due to pressure from his or her employer, who may demand copies of the deposition transcripts from the employee." Responses of Norman C. Bay, FERC Dir. of Enforcement, to Senate Comm. on Energy and Natural Resources Questions for Record (June 4, 2014) (Response to Sen. Mike Lee, Q 4), https://www.energy.senate.gov/public/index.cfm/files/serve?File_id=198f6249-394c-482d-9c7e-0d0ec80692cf; see also Allison Murphy, Todd Hettenbach, & Thomas Olson, *The FERC Enforcement Process*, 35 ENERGY L.J. 283, 309 (2014), <https://www.eba-net.org/assets/1/6/15-283-321-Murphyetal-final-11.1.pdf>. Subjects have found that in practice, however, Enforcement staff withholds or delays access to transcripts more regularly, and for reasons that do not meet the "good cause" standard Enforcement has described. This includes, for instance, denying a witness access to his or her transcript because Enforcement may want to take a second deposition in the future—which, given Enforcement's investigative practices, is a possibility in almost every investigation.

¹² See, e.g., *Maxim Power Corp., et al.*, Notice of Designation of Commission Staff as Non-Decisional, Docket No. IN15-4-000 (Feb. 2, 2015); *BP Am. Inc., et al.*, Notice of Designation of Commission Staff as Non-Decisional, Docket No. IN13-15-000 (Aug. 5, 2013); *Total Gas & Power North Am., et al.*, Update Notice of Designation of Commission Staff as Non-Decisional, Docket No. IN12-17-000 (Feb. 19, 2019).

The better practice, consistent with the Commission’s longstanding practice of separating litigation staff from other advisory staff, would be to designate Enforcement staff as a whole as “non-decisional” once the Commission issues an Order to Show Cause. Doing so would make every staff member of Enforcement, at that time, subject to the Commission’s *ex parte* rules, i.e., Enforcement could then only communicate with the Commission and advisory staff through the pleadings it files in the Show Cause proceeding. This change is appropriate because once the Commission issues an Order to Show Cause, both the Commission’s and Enforcement’s roles change: the Commission goes from supervising an investigation to adjudicating a violation, and Enforcement goes from being the investigator to being a litigant in the Show Cause proceeding. When Enforcement staff is a litigant in a Commission proceeding, it is inappropriate and unfair for any Enforcement staff to also advise the Commission on that proceeding.

The current practice raises concerns for two key reasons. First, while the Enforcement staff exempted from the designation as “non-decisional” are not the staff who conducted the investigation and will not litigate the matter at the Commission or in court (if necessary), that does not mean those staff have not already formed views about the case (from having talked with the investigative team informally and learned about the case during staff meetings before the Order to Show Cause issued). Second, there is also a concern that exempted “non-decisional” Enforcement staff may advise on the adjudication of cases in which some of their colleagues, supervisors, or direct reports are litigants. This creates, at the very least, the perception that they may be less than fully objective, which is alone cause to change the policy given the importance of due process “both in perception and reality.”¹³ Indeed, this practice creates, at the very least, an “appearance of bias” by the exempted Enforcement staff, which alone renders it improper.¹⁴

Furthermore, the practice of providing an exception to some staff instead of designating Enforcement staff as a whole as “non-decisional” employees is unnecessary. While the Commission may find it beneficial to have the expertise of Enforcement staff to advise them, the Commission has experienced, knowledgeable, and skilled staff throughout its other program offices who are fully capable of advising the Commission on enforcement matters. The Commission already has a wealth of knowledge about enforcement issues without having to rely on current Enforcement staff to advise the Commission and draft orders in Show Cause proceedings.

For these reasons, the Commission should discontinue this practice, which, in turn, will bolster confidence in the fairness of FERC’s enforcement process.

F. Subjects Should Have a Greater Opportunity to State Their Case to Commissioners Before the Commission Initiates a Public Enforcement Action

During an investigation, Enforcement staff does not have any *ex parte* restrictions on off-the-record communications with the Chairman and Commissioners until an enforcement action is initiated formally through an Order to Show Cause. Since the Commissioners supervise

¹³ 2008 Revised Policy Statement on Enforcement at P 21.

¹⁴ See *Mitchell v. Sirica*, 502 F.2d 375, 382 (D.C. Cir. 1974) (noting the D.C. Circuit has “adopted the appearance of bias test, with specific reference to the prejudgment of issues in administrative agency disqualification cases”).

Enforcement and its investigations, it is likely not practical to restrict communications between Enforcement staff and Commissioners during an investigation. Investigative subjects' opportunity to communicate with Commissioners and their advisors, however, is much more limited: subjects can communicate in writing with Commissioners at any time, but under the *2008 Revised Policy Statement on Enforcement*, cannot communicate in person or by telephone.¹⁵ As long as the Commission retains a role in adjudicating enforcement cases, the Commission should consider finding ways to allow subjects to have greater access to the Commissioners to state their case directly as to why a public enforcement action should not be initiated on factual, legal, or policy grounds.

An Order to Show Cause—which initiates a public enforcement action—is a key event in an Enforcement proceeding. It can be the first public disclosure of the investigation, and includes the Staff Report—a detailed, inherently one-sided report by Enforcement describing what it believes to be misconduct in violation of FERC regulations. An Order to Show Cause can be highly damaging to the subject reputationally and financially—and is issued without the subject ever having the opportunity to confer directly with the Commissioners. While subjects are allowed to communicate with the Commissioners through written submissions, they, unlike Enforcement staff, do not get to discuss the matter directly with Commissioners, respond to their questions, or clarify misunderstandings or ambiguities. Further, to the extent the Commissioners have questions about the subject's factual, legal, or policy arguments, it is Enforcement staff—who, by recommending an enforcement action, has necessarily discounted the subject's arguments already—who answers them.

Even if the Commission continues its general practice of requiring investigation subjects to communicate with the Commission in writing, allowing meetings with the Commissioners once Enforcement staff has notified the subject that it intends to recommend the Commission issue an Order to Show Cause would promote fairness and due process. It would also impose only a minimal burden on the Commissioners because FERC only issues, at most, a couple of Orders to Show Cause each year. Yet such meetings would go a long way towards the Commission's longstanding goal of providing investigation subjects "due process both in perception and reality."¹⁶ These meetings would provide subjects greater assurance that their arguments against initiating a public enforcement action were considered and understood by the Commissioners, while also promoting increased confidence in the process and a greater sense of fairness.

II. Investigations Should Be More Efficient

While reaching the correct result is paramount given the consequences of an enforcement action, efforts should be made to make the investigation process more efficient. Investigations themselves inflict harm on subjects—they are burdensome and expensive for companies and can have damaging reputational consequences. Despite the need for an efficient process, enforcement investigations frequently take many years to complete, regardless of how they are ultimately resolved. This is often the case even when the facts and violations are relatively straightforward or the investigation concerns limited, discrete conduct. The lengthy nature of investigations is

¹⁵ *2008 Revised Policy Statement on Enforcement* at P 27.

¹⁶ *Id.* at P 21.

demonstrated in a review of just the five enforcement cases publicly resolved during the most recent fiscal year (FY2018):

- *PSEG Energy Resources & Trade, LLC*, 163 FERC ¶ 61,056 (2018) (investigation arose from an April 2014 self-report of inaccuracies in cost-based offers; settlement entered in April 2018, approximately four years after the conduct was self-reported)
- *Duke Energy Corporation*, 163 FERC ¶ 61,189 (2018) (investigation concerned the accuracy of certain information filed with the Commission in a merger proceeding; Enforcement initiated the investigation in December 2014 following the referral from the Commission; settlement entered in May 2018, approximately three-and-a-half years after the investigation began)
- *ETRACOM LLC and Michael Rosenberg*, 153 FERC ¶ 61,314 (2018) (investigation involved a market monitor referral of discrete trading activity at one trading location in the California Independent System Operator region in May 2011; investigation commenced in July 2011 following a market monitor referral;¹⁷ Order to Show Cause alleging market manipulation issued in December 2015, nearly four-and-a-half years after the investigation began)
- *Entergy Nuclear Power Marketing, L.L.C.*, 164 FERC ¶ 61,051 (2018) (investigation concerned bidding behavior in ISO New England Inc. (“ISO-NE”) during two days in December 2013; settlement entered in May 2018, approximately four-and-a-half years later)
- *Wheelabrator Claremont Company, L.P.*, 164 FERC ¶ 61,237 (2018) (investigation concerned a small (4.5 MW) generator’s inadvertent receipt of capacity payments from ISO-NE for a one-year period after the unit was deactivated; investigation opened in March 2015 following a market monitor referral; settlement entered in September 2018, approximately three-and-a-half years after the investigation began)

Based on the Commission orders and settlements, most of these cases involved discrete conduct, fairly straightforward (and in some instances undisputed) facts, and subjects that were cooperative throughout the investigation process. Despite this, each of these investigations took several years.

The extended length of Enforcement investigations is in some cases due to a need for thorough fact-finding by Enforcement on complex matters. However, recognizing the repercussions associated with an open investigation, the Commission must strive to strike a better balance between the length of time required for sufficient fact-finding and efficiency.

When it comes to the time it takes to complete investigations, transparency and efficiency are interrelated concepts. Improving the overall transparency of the investigation process, as

¹⁷ While the Order Approving Stipulation and Consent Agreement does not state when Enforcement opened the investigation, the federal court complaint Enforcement filed to enforce the penalty (prior to reaching a settlement) states the investigation was opened in July 2011. Petition for an Order Affirming the Fed. Energy Reg. Comm’n’s June 17, 2016 Order Assessing Civ. Penalties Against ETRACOM LLC and Michael Rosenberg at 8, *FERC v. ETRACOM LLC and Michael Rosenberg*, No. 2:16-cv-01945-SB (E.D. Cal. 2018).

discussed in Section I above, would help make investigations more efficient. Indeed, a more open, continuous, and productive dialogue between Enforcement and subjects and their counsel, and increased sharing of information relevant to the investigation, would lead to more focused and efficient fact-finding. The proposals below are intended to improve efficiency without compromising the effectiveness of Enforcement investigations.

A. Narrowly Tailor Discovery Requests to the Conduct Under Investigation

Subjects under investigation frequently receive data requests that are very broad and go well beyond the scope of the conduct under investigation. This is a particularly significant problem in market manipulation investigations in which there may be requests for months or years of data in an investigation focused on a narrow timeframe, e.g., a single natural gas bidweek or a few days of bidding in a Regional Transmission Organization (“RTO”) market. In addition to the temporal breadth of requests, there are often requests for extensive data regarding types of transactions or personnel unrelated to the conduct under investigation, including data regarding different employees than those involved in the conduct at issue. The breadth of data requests bogs down the investigation process on both ends: the subjects that must respond to the requests, often at significant expense in both the collection and review of responsive data, and the Enforcement staff who must review and analyze the (vast) information produced. It takes extensive time and resources to comply with broad requests for raw data such as transaction data and trader position information. Subjects often must identify the type of data that are responsive, collect the data from a range of sources (e.g., different trading desks and business divisions), convert it to the requested format (which is often different than how it is maintained by the company), quality check it to verify its accuracy and comprehensiveness, and then host or maintain the data electronically during the pendency of the investigation. Requests for communications and other documents are often even more burdensome, as such information must also be reviewed by counsel for responsiveness and privilege.

While data requests are a necessary component of most investigations, the requests should be reasonably calibrated to obtain the information necessary to determine whether the potential violation that is the subject of the investigation occurred. This does not mean that Enforcement must be overly constricted in determining what information is relevant to the conduct under investigation. In an investigation into one or two days of market activity by one individual, it may well be reasonable to obtain information about the trader’s activities over the prior and subsequent weeks, for example, but it is not necessarily reasonable to ask for data covering the previous six months. Prior to issuing data requests, Enforcement staff should consider the proportionality and likely relevance of all the information being sought and the burden on the subject required to produce it.

B. Embrace Search Engine Technology and Other Tools That Would Make Investigative Discovery More Efficient

Advances in software technology have led to computer-assisted document reviews in litigation and investigations (“technology-assisted review”), reducing the amount of manual attorney review required and, therefore, the time and expense of responding to discovery requests. Technology-assisted review can identify material that is responsive to requests or that warrants further review to determine responsiveness, while also eliminating information that is irrelevant to

the case. While Enforcement has, in some cases, been receptive to “key word” searches and basic forms of technology-assisted review, Enforcement has resisted the use of more advanced technology such as predictive coding and other methods, despite proven advances in the sophistication and reliability of such methods that have been recognized by federal courts and electronic discovery experts.¹⁸ Mandating manual review, or that subjects produce, and therefore review, *all* of an employee’s records for a certain time period without regard to the relevance of such information to the investigation, needlessly increases the time and cost of responding to data requests and the length of the investigation.

In recent years there have been advances in technology that facilitate more efficient, less burdensome investigative discovery methods and Enforcement should expand its use of these technologies in investigations, where appropriate. There is likely no one-size-fits-all approach that makes sense—different approaches will make sense in different cases given the type of investigation and the information sought. For example, technology-assisted review is likely more appropriate in investigations in which Enforcement seeks information that requires subjects to conduct a broad search of company records. But as a general matter, Enforcement should be receptive to good-faith proposals by subjects to reduce the burden of discovery through the use of technology.

C. Use Interviews More Frequently as an Alternative to Depositions

In most investigations in which Enforcement seeks to question witnesses, it does so through depositions rather than informal interviews, even though it recognizes both as options.¹⁹ Enforcement’s default practice—particularly in market manipulation investigations—is to conduct depositions, often of numerous individuals, and sometimes multiple times for the same individual, while informal interviews in such cases are conducted infrequently. Depositions are necessary for certain witnesses in certain cases, especially those involving potential fraud, and where the deponent’s own actions are at issue. However, depositions are generally not efficient. Depositions usually require more time of staff and the witness, who must leave their daily duties and travel to FERC headquarters for a full day (or more) of questioning by Enforcement staff. Moreover, the formality of the deposition process—often in a FERC hearing room, with a court reporter, and numerous Enforcement staff—can create a more adversarial dynamic that is often unwarranted and counterproductive.

In many cases, informal interviews would be more efficient and equally (if not more) effective than depositions. Interviews are typically scheduled and conducted in much less time

¹⁸ See, e.g., *Moore v. Publicis Grp.*, 287 F.R.D. 182, 190 (S.D.N.Y. 2012) (“[W]hile some lawyers still consider manual review to be the ‘gold standard,’ that is a myth, as statistics clearly show that computerized searches are at least as accurate, if not more so, than manual review.”); *Dynamo Holdings Ltd. P’ship v. Comm’r of Internal Revenue*, 143 T.C. 183, 192 (T.C. 2014) (“[W]e understand that the technology industry now considers predictive coding to be widely accepted for limiting e-discovery to relevant documents and effecting discovery of [Electronically Stored Information] without an undue burden.”) (citing, among others, *Progressive Cas. Ins. Co. v. Delaney*, No. 2:11-cv-00678-LRH-PAL, 2014 WL 3563467, at *8 (D. Nev. July 18, 2014)); see also Maura R. Grossman & Gordon V. Cormack, *Technology-Assisted Review in E-Discovery Can Be More Effective and More Efficient Than Exhaustive Manual Review*, 17 RICH. J.L. & TECH 11 (2011).

¹⁹ *FERC Enforcement Process*, <https://www.ferc.gov/enforcement/investigations/process.asp> (last updated May 30, 2014) (fact-gathering can involve “interviews[] and depositions”).

than is required to plan for a deposition; they can be conducted by phone without requiring the individual (and potentially their counsel) to travel and leave their work duties; and they can facilitate a more collaborative environment. Interviews could be used during the early stages of questioning witnesses, i.e., where Enforcement is trying to get a better understanding of the conduct at issue and would find it useful to ask preliminary questions of individuals with relevant knowledge. For example, subject matter experts could be more readily called upon by Enforcement staff to participate in informal interviews and provide background information on the subject entity, its policies and procedures, and reporting structures. Such background information is often discussed at length during depositions, typically in the beginning, and diverts the witness from addressing substantive matters of concern to Enforcement staff. Another example where interviews could be used in lieu of depositions is the questioning of third-parties, whether employees of the subject or not, whose personal conduct is not under investigation but who might have relevant information.

Increasing the use of informal interviews would not only promote efficiency and improve the process but would present little to no risk to Enforcement. Interviews would not preclude Enforcement from determining that a deposition of the individual was warranted at a later time. Moreover, while interviews might facilitate a less formal and adversarial environment, there is no reason to think witnesses will be less truthful in such instances. While depositions are conducted under oath, informal interviews are nevertheless subject to 18 U.S.C. § 1001, which makes it a crime to lie to or mislead a federal officer (including Enforcement staff).

Finally, the efficacy of informal interviews is reflected in Enforcement's Division of Analytics and Surveillance's ("DAS") frequent use of them in surveillance inquiries. DAS regularly conducts surveillance inquiries into instances of potential misconduct, including market manipulation, and often uses informal interviews of relevant company personnel (including traders) to learn about the conduct at issue, understand the company's explanation for it, and determine whether the explanation is credible. DAS's success with interviews in surveillance inquiries into potential market manipulation and other violations only further supports their use as a tool in Enforcement investigations since in both circumstances the core purpose is the same: to speak with a trader or other knowledgeable employee to understand why they engaged in the conduct at issue or what they know about it.

D. Establish a Practice that Fact-Gathering Should Typically be Completed in Six Months—and if it Takes Longer, Explain Why

The duration of time Enforcement can spend investigating is bounded only by the risk that penalties could be barred by the five-year statute of limitations, which is often eliminated if subjects agree to sign a tolling agreement at the request of staff. Additionally, there are no publicly-known targets or metrics for the length of investigations. As explained above, it is all too common for relatively straightforward investigations to take years to conclude. Enforcement should have targets for the length of time the fact-gathering phase of investigations should take. A reasonable target for many investigations is six months as, in most cases, facts can usually be obtained and analyzed in that time period. This target is also consistent with recent policies

adopted by other enforcement agencies.²⁰ In any case, a defined target completion timeframe for the fact-gathering phase of an investigation, as well as other phases to the extent possible, would promote a more efficient investigative process, which ultimately benefits Enforcement, the Commission, subjects, and the regulated community as whole.²¹

The targeted time period for fact-gathering would not be binding and could be extended when required so that there is no incentive for parties to engage in delay tactics to “run out the clock” on the investigation. However, if fact-gathering cannot be completed within the targeted range, Enforcement should explain and discuss the reasons with the subject (and do so periodically thereafter, such as every two months, until fact-gathering is complete). It could be, for example, that the subject took an unexpectedly long time to gather and produce relevant information, or that understanding the conduct under investigation simply proved too complex to complete in the defined time period. At a minimum, open communications between Enforcement and the subject of the investigation about why fact-gathering is taking longer than expected would greatly enhance the Commission’s current enforcement program by increasing efficiency and transparency.

III. Ensure Civil Penalties Are Transparent and Not Higher Than Necessary to Achieve Compliance

The Commission has been consistent from the inception of its modern-day enforcement program that “[a]chieving compliance, not assessing penalties, is the central goal of our enforcement efforts.”²² The Commission reiterated this core tenet at the time it promulgated the Penalty Guidelines, which sets forth a framework for determining civil penalty amounts in enforcement cases.²³ However, penalties in several enforcement cases have gone beyond what is necessary to achieve the Commission’s goal of ensuring compliance. For example, in one recent case, the penalty was nearly one hundred times greater than the subject’s gain.²⁴ While there is unquestionably an important deterrence component to penalties, and it is also true that certain intentional and harmful market conduct merits high civil penalties, the amount of the penalty should be seen as understandable, fair, and reasonable to participants in FERC-regulated markets. When a penalty in one case is especially high compared to other cases involving the same type of violation, and it is not clear why that is the case from reading the settlement document or Order

²⁰ For example, the Department of Justice recently announced that it would work to complete merger investigations in six months. See Makan Delrahim, Assistant Att’y Gen., Antitrust Div., U.S. Dep’t of Justice, *It Takes Two: Modernizing the Merger Review Process*, Remarks at the 2018 Global Antitrust Enforcement Symposium (Sept. 25, 2018), <https://www.justice.gov/opa/speech/file/1096326/download>. While merger investigations are different than FERC Enforcement investigations, they are no less complex. Similarly, the CFTC has announced that as part of its self-reporting and cooperation policy, it would strive to complete investigations arising from self-reports in a matter of “months.” See James McDonald, Dir., Div. of Enf’t, Commodity Futures Trading Comm’n, *Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC*, Speech at the NYU Program on Corporate Compliance & Enforcement/Institute for Corporate Governance & Finance (Sept. 25, 2017), <https://www.cftc.gov/PressRoom/SpeechesTestimony/opamcdonald092517>.

²¹ This proposal of a six-month time period focuses on fact-gathering, not the process following fact-gathering if FERC intends to proceed with the case (such as the time needed to complete settlement discussions).

²² *2008 Policy Statement on Compliance* at P 1.

²³ Penalty Guidelines at P 110.

²⁴ *BP Am. Inc.*, 156 FERC ¶ 61,031 (2016) (assessing a civil penalty of \$20,160,000, more than 97 times the \$207,169 unjust profit).

Assessing Civil Penalties, that can create concerns that the Penalty Guidelines are not necessarily producing the type of transparent, objective, and fair outcomes the Commission intended.

The Commission’s job of determining civil penalty amounts is not an easy task. In EPAct 2005, Congress gave the Commission substantial civil penalty authority—now, with inflation adjustments, nearly \$1.3 million per day, per violation.²⁵ Yet the only statutory directive from Congress about how to *apply* this penalty authority is for the Commission to consider “the seriousness of the violation and the efforts of such person to remedy the violation in a timely manner”—inarguably sound, but vague.²⁶

In promulgating the Penalty Guidelines in 2010, the Commission provided for civil penalties to be determined in a more fair, consistent, and transparent manner.²⁷ The Commission should be commended for taking concrete action to improve the transparency and objectiveness of penalty determinations. The Penalty Guidelines, which are modeled on the United States Sentencing Guidelines, are formulaic and calculate a penalty range based on various factors such as the type of violation, the harm or risk of harm caused by the violation, the duration of the violation, and various “culpability” factors such as senior management involvement, compliance history, cooperation, and self-reporting.²⁸ The Penalty Guidelines assign different weights to these and other factors, and the Commission determines a penalty range by applying the Guidelines to the facts of a particular case.

While the Penalty Guidelines have increased the transparency of penalty calculations for investigation subjects, the Commission should ensure that the way they actually work in practice—i.e., the penalty ranges they produce in different types of cases—aligns with the Commission’s enforcement policies and its longstanding view that compliance, not penalties, is the ultimate goal. With nearly a decade of experience applying the Penalty Guidelines, now is the appropriate time to conduct such a review.

A. Ensure Penalties are Consistent and Proportional, Including by Considering the Financial Benefit Received from the Violation

There is no bright line rule for determining whether a penalty (or penalty range) is “too high” or “too low.” One useful metric, however, is to compare the size of a penalty to the financial benefit received by the subject as a result of the violation, i.e., the “unjust profits,” which the subject is often required to disgorge in addition to paying a penalty. As the Commission has recognized, there is a deterrence component to penalties,²⁹ and in many cases, simply requiring the subject to refund illicit gains, or limiting its penalty to the amount of gains, would be insufficient

²⁵ *Civil Monetary Penalty Inflation Adjustments*, 166 FERC ¶ 61,014 (2019).

²⁶ FPA, § 316A, 16 U.S.C. § 825o-1(b). Section 22 of the (“NGA”), 15 U.S.C. § 717t-1(c), contains substantially similar language (“[T]he Commission shall take into consideration the nature and seriousness of the violation and the efforts to remedy the violation.”).

²⁷ Penalty Guidelines at P 2.

²⁸ *See generally id.*

²⁹ *Id.* at P 194 (“Specifically, the Penalty Guidelines are designed to generate a penalty range that is high enough to serve to provide just punishment, deterrence, and incentives for organizations to develop and maintain sufficient compliance measures.”).

to achieve the Commission’s compliance objectives. There can be sound policy reasons that in certain types of cases (especially market manipulation cases), penalties should be substantially larger than the financial gain the subject received as a result of the violation. At the same time, considering the magnitude of the penalty relative to the unjust gain is a useful metric. Indeed, the penalty authority of other enforcement agencies with similar market oversight and anti-manipulation mandates, including the CFTC and SEC, explicitly focuses on the gain to the violator (with penalties often statutorily limited to three times the gain)—yet there is little suggestion that these agencies have insufficient authority to deter misconduct.³⁰

A review of civil penalties assessed by the Commission under the Penalty Guidelines—particularly in market manipulation cases—shows that penalty amounts often appear to be very high, potentially beyond what may be a reasonable amount necessary to achieve deterrence. Such a review also shows dramatic variances between cases in the penalties relative to the subject’s gain. To provide just a few examples, the Commission’s penalties in market manipulation cases (whether assessed through a settlement or an Order to Show Cause process) have included penalties of approximately: one times the amount of gain (MISO Virtual and FTR Trading, 2014); eight times the amount of gain (ETRACOM, 2016); 45 times the amount of gain (Competitive Energy Services, 2013); and 97 times the amount of gain (BP America, 2016).³¹

Without commenting on the facts or merits of any individual case, it is not clear from the Commission’s settlements or orders why there should be such dramatic variances in the size of the penalty assessed relative to the gain resulting from the violation. Further, in general, absent compelling case-specific factors, penalties that are dozens of times the amount of gain can appear to be beyond what is required to promote deterrence and achieve compliance. At the very least, the Commission should ensure that the penalties it assesses are consistent with its view of what is needed to achieve the intended deterrence effect and provide an explanation so that industry participants can understand how such penalties are gauged. Ensuring that enforcement decisions are informative and transparent—not merely the product of the Penalty Guidelines’ formula—will build increased confidence in the Enforcement program and show that such decisions are not arbitrary.

B. Improve Certain Aspects of the Penalty Guidelines Formula

The Commission should revise the Penalty Guidelines to ensure that penalties are appropriate for the specific violation at hand, and neither higher nor lower than needed to achieve the Commission’s compliance and deterrence objectives. To accomplish this, the Commission can reevaluate the overall formula, including the specific weighting of each element, and make modifications so that the penalty ranges produced by the Penalty Guidelines reflect penalties that

³⁰ See 7 U.S.C. § 9(10)(c)(ii)(I-II) (authorizing the CFTC to assess civil penalties for manipulation of up to the greater of \$1 million or “triple the monetary gain to the person for each such violation”); 15 U.S.C. § 78u-1(2) (authorizing the SEC to seek insider trading penalties of an amount to “not exceed three times the profit gained or loss avoided as a result of” the conduct). Congress obviously could have limited FERC’s penalty authority in this manner, but did not. The suggestion, however, is not that FERC does not have *authority* to issue penalties that substantially exceed the gain to the violator, but rather that such penalties are often unnecessary and, at times, seemingly arbitrary.

³¹ These and every other settlement or Order Assessing Civil Penalties can be found at the FERC Enforcement, Civil Penalties webpage, at <https://www.ferc.gov/enforcement/civil-penalties/civil-penalty-action.asp?csrt=2696216633119269721>.

are appropriate for the case and consistent with the Commission’s overarching objective of promoting compliance. Various modifications can and should be considered, including, but not limited to, the four potential reforms discussed below:

1. Rely on Tangible Unjust Profits Instead of Market Harm. For market manipulation and fraud cases, the Penalty Guidelines currently factor in the larger of either the overall economic harm to the market *or* the violator’s gain, i.e., the unjust profits. The economic harm to the market is often difficult to estimate with any precision. In many cases, Enforcement has put forward market harm calculations that substantially exceed the alleged unjust profits—resulting in penalty ranges that substantially exceed what the range would have been if unjust profits were used in the calculation.³² The Commission should revise the Penalty Guidelines to focus on the subject’s gain from the violation. The use of market harm could be considered when the facts provide a compelling reason to use this measure and when the Commission believes that the use of unjust profits would not promote compliance with the Commission’s enforcement goals.

2. Ensure that the Impact of the Duration or Volume is Not Double Counted. The Penalty Guidelines separately consider the duration of the violation, or the volume of transactions at issue, in addition to the economic harm or unjust profits.³³ As Commissioner LaFleur has observed, this can result in the Penalty Guidelines effectively “double counting” the duration of the violation since in some cases “the total monetary loss caused by the fraud is a direct function of how long the fraud persisted.”³⁴ The same is true for volume, which the Penalty Guidelines can consider in lieu of duration (while still also considering harm). The Commission should revise the Penalty Guidelines to address this risk of “double counting.” One practical solution would be, in every case where “double counting” is at issue, to simply remove the duration or volume adder when calculating a penalty range; the resulting penalty range would be whatever is generated by the economic harm or unjust profits calculation on its own (along with the other applicable Penalty Guidelines factors). The Penalty Guidelines could easily be amended to reflect that approach.

3. Provide Greater Weight for Settlements or, Alternatively, Do Not Apply the Penalty Guidelines to Settlements. The Penalty Guidelines appropriately reduce the penalty range when a subject resolves the case through a settlement rather than litigation.³⁵ However, the one-point reduction in the culpability score can be insufficient to incentivize and reward a subject for settling—particularly when the subject thinks it has meritorious legal or factual defenses to the alleged wrongdoing. Under the Penalty Guidelines, a one-point reduction in the culpability score reduces the range by about twenty percent on average.³⁶ In a clear-cut case where there is no question about liability, perhaps this reduction is sufficient to incentivize and reward settlement.

³² See, e.g., *BP Am. Inc.*, 156 FERC ¶ 61,031 (2016) (finding unjust profits of \$207,169 but calculating \$20,160,000 penalty based on estimated market harm of between \$1,375,482 and \$1,927,728); *Competitive Energy Services, LLC*, 144 FERC ¶ 61,163 (2013) (finding unjust profits of \$166,841 but calculating \$7,500,000 penalty based on estimated market harm of \$3,336,964).

³³ Penalty Guidelines, Guideline for Fraud, Anti-Competitive Conduct and Other Rule, Tariff and Order Violations § 2B1.1.

³⁴ *Lincoln Paper and Tissue, LLC*, 144 FERC ¶ 61,162 (2013) (LaFleur, C., dissenting in part, at 2).

³⁵ Penalty Guidelines, Part C – Civil Penalties § 1C2.3(g)(3).

³⁶ *Id.* § 1C2.4. For example, settlement could reduce a subject’s culpability score from six to five, which would result in applying a multiplier range of 1.00 to 2.00 to the base penalty amount instead of 1.20 to 2.40.

For other cases, however, there is litigation risk on both sides, i.e., the risk that either side could win or lose in court. In such cases, under the Penalty Guidelines, the consequence of “losing” in court is only marginally worse than settling. In those types of cases, the subject has a strong incentive to litigate—on the one hand, it could prevail in court and be absolved of any liability, while on the other hand, it could be found liable and ordered to pay a fine only marginally larger than the fine it could have received in a settlement. By providing only a marginal penalty reduction for settlement, the Penalty Guidelines make it more difficult to settle such cases even though settlement is the Commission’s preferred resolution of enforcement cases.³⁷ The Commission could either revise the Penalty Guidelines to provide a more substantial reduction for settlement, or, alternatively, decide not to apply the Penalty Guidelines to cases that settle prior to litigation.³⁸

4. Provide Greater Transparency About How (and When) the Commission Will Assess Penalties in New Areas of Enforcement. Ensuring transparency and avoiding unnecessarily high penalties are important not just for traditional Commission enforcement priorities, e.g., market manipulation and serious violations of the electric Reliability Standards, but for new areas of enforcement oversight. For example, Enforcement has recently begun to investigate compliance with natural gas pipeline certificates, including compliance with environmental conditions set forth in those certificates.³⁹ Pipeline owners and operators, however, do not have guidance at this point on whether and to what extent civil penalties are appropriate for certificate compliance issues, as factors used in past settlements in different contexts are not applicable. This is just one example where the more transparency and guidance the Commission can provide, the greater the ability of industry participants to understand what conduct might justify civil penalties and why—which, in turn, will promote the goal of achieving compliance with FERC’s rules.

C. Depart from the Penalty Guidelines More Frequently When the Facts Dictate

While transparency and consistency in the penalty assessment process is vital for regulatory certainty, it may be appropriate at times for the Commission to apply the Penalty Guidelines more flexibly. The Penalty Guidelines do not bind the Commission and are clear that

³⁷ 2008 Revised Policy Statement on Enforcement at P 33 (“Settlement is our preferred resolution to investigations that result in a recommendation of remedial action. From the subject’s point of view, settlement can often result in penalty payments significantly lower than those that would result from contesting staff’s conclusions, and avoids litigation risk as well as the time and costs of a hearing. From the Commission’s point of view, the public interest is often better served through settlements because we are able to ensure that compliance problems are remedied faster and that disgorged profits may be returned to customers faster, and we are able to reallocate to other enforcement matters the resources that would have been spent in lengthy litigation.”).

³⁸ If the Commission decided not to apply the Penalty Guidelines to pre-litigation settlements, the Penalty Guidelines would still be relevant since both Enforcement and the subject would recognize that, absent a settlement, the Commission would use the Penalty Guidelines to determine what penalty to seek in litigation. The Penalty Guidelines would essentially serve as a marker for the subject’s potential liability in litigation. However, Enforcement and the subject would have greater flexibility to negotiate a settlement that appropriately discounts from the Penalty Guidelines range based on case-specific factors, including litigation risk. This could facilitate more productive and efficient resolutions of cases.

³⁹ See FERC OFFICE OF ENFORCEMENT, 2018 REPORT ON ENFORCEMENT 34 (2018) (“2018 REPORT ON ENFORCEMENT”) (noting Enforcement’s collaboration with other program offices on potential enforcement matters, including with respect to “regulatory obligations and the terms and conditions of pipeline certificates”), <https://www.ferc.gov/legal/staff-reports/2018/11-15-18-enforcement.pdf>; *Algonquin Gas Transmission, LLC*, 166 FERC ¶ 61,012 (2019) (settlement of alleged violation of natural gas pipeline certificate condition on environmental compliance; ordering \$400,000 civil penalty without significant discussion of how that amount was determined).

the Commission can depart from them in its discretion.⁴⁰ When the Commission first promulgated the Penalty Guidelines in March 2010 (prior to revising them), it recognized that “a guidelines approach always creates the possibility of outcomes not adequately accounting for all of the specifics of a case”—a concern the Commission found was addressed through its ability to depart from the Penalty Guidelines.⁴¹ However, the Commission said it “d[id] not intend to depart from the Penalty Guidelines regularly”—and true to its word, it has done so very infrequently.⁴² Enforcement has recommended departures infrequently, likely because the Commission’s stated policy suggests departures should be rare and based on unique circumstances. When circumstances warrant, the Commission should be willing to depart from the Penalty Guidelines and take a more flexible approach based on the facts of a case. In the same vein, the Commission should encourage Enforcement to recommend departures from the Penalty Guidelines when staff thinks a departure would result in a more reasonable and appropriate outcome. While flexibility is warranted, it is still expected that Enforcement will consider a violation’s impact on individual market participants, the integrity of the overall market, litigation risk associated with Enforcement’s claims, and the subject’s actions prior to seeking a downward departure from the Penalty Guidelines. Moreover, departures from the Penalty Guidelines should be adequately explained in any related Commission order to ensure the transparency of the process.

IV. Formally Repeal the Notice of Alleged Violations Policy

The Commission should formally repeal its Notice of Alleged Violations (“NAV”) policy. The NAV policy, which FERC implemented in 2011, provides for early public disclosure of investigations.⁴³ Under the policy, the Director of Enforcement issues a NAV once the subject “has had the opportunity to respond to staff’s preliminary findings,” but prior to staff finalizing its findings or the Commission itself issuing an order addressing the matter.⁴⁴ The NAV includes a brief description of the conduct and, more consequentially, identifies the investigation subject(s). This policy has proven to be ineffective and even harmful, as described below. Notably, the Commission has not issued NAVs in recent cases. While this is a welcome development, the Commission should provide regulatory certainty by formally rescinding the NAV policy.

The NAV policy was unusual and controversial from the outset, as it upset longstanding Commission policy that investigations, including subjects’ identities, were kept non-public unless and until FERC issued an order approving a settlement or initiating an enforcement action by issuing an Order to Show Cause.⁴⁵ The Commission recognized the potential harm caused by the policy by placing “the entity under investigation . . . in the public eye, with possible adverse consequences to its reputation.”⁴⁶ The Commission, however, found these costs were outweighed

⁴⁰ Penalty Guidelines at P 31.

⁴¹ *Enforcement of Statutes, Orders, Rules, and Regulations*, 130 FERC ¶ 61,220, at P 32 (2010).

⁴² *Id.*

⁴³ *Enforcement of Statutes, Regulations, and Orders*, 129 FERC ¶ 61,247 (2009) (“2009 NAV Order”), order on reh’g, 134 FERC ¶ 61,054 (2011) (“2011 NAV Order”). While these orders characterize the disclosure as a Preliminary Notice of Violations, in practice, the disclosure is called a Notice of Alleged Violations, or “NAV.”

⁴⁴ 2009 NAV Order at P 6.

⁴⁵ *Id.* at P 5.

⁴⁶ *Id.* at P 6.

by specific benefits that increased public transparency into non-public investigations could provide—namely, that disclosure might lead third-party market participants to bring relevant information about the subject or conduct under investigation to Enforcement’s attention in response to the NAV, and that third-party market participants would benefit from the NAV’s educational value.⁴⁷ The Commission also made clear, given the risk of harm, that it would “continue to monitor the [NAV] procedure and [was] open to considering it again after staff ha[d] acquired some experience in its application.”⁴⁸

With eight years of experience applying the NAV policy, it is now possible to reach the conclusion that the policy has simply not worked.⁴⁹ On the one hand, there is no evidence that the intended benefits from the policy have materialized. That is, there is no evidence in the public record that any of the more than 50 NAVs the Commission has issued have prompted third-party market participants to provide relevant information, or that NAVs have otherwise aided any of the Commission’s enforcement efforts.⁵⁰ Likewise, the NAV has provided little to no meaningful transparency or educational value to other market participants—the sparse detail provided in the NAV (generally a few sentences) provides little educational value, particularly since the Commission provides much more detail elsewhere, such as in Commission orders and annual reports.

On the other hand, the harm from the policy, which the Commission previously recognized, persists and has in fact increased in some respects. In one enforcement case, an individual was fired from her employment immediately upon being publicly identified in the NAV, even though Enforcement staff at the time had not yet completed its investigation and the Commission had not decided whether there was a basis to institute an enforcement action.⁵¹ In another case, FERC publicly named an individual in a NAV yet never brought an enforcement action against him, ultimately terminating the matter when it approved a settlement between Enforcement and the company nearly two years later.⁵² For nearly two years, this individual stood publicly accused of committing market manipulation without the Commission ever finding that there was cause to bring a case against him. Given the Commission’s increasing focus on pursuing individuals in

⁴⁷ 2011 NAV Order at PP 15-16.

⁴⁸ *Id.* at P 22.

⁴⁹ See generally David A. Applebaum, Todd L. Brecher et al., *FERC Should Rescind Its Notice of Alleged Violations Policy*, 8.2 GEO. WASH. J. ENERGY & ENVTL L. 87 (2017) (“*FERC Should Rescind Its NAV Policy*”).

⁵⁰ *Id.* at 88-89.

⁵¹ Answer of Karen Levine to Order to Show Cause and Notice of Proposed Penalty, Docket No. IN08-8-000, at 36 (filed Dec. 14, 2012) (“After the NAV was issued, Ms. Levine immediately lost her contract with another company due to the resulting publicity and was unemployed for several months.”). While the Commission ultimately found this individual to have committed a violation, the point is that the NAV itself led to these consequences when the investigation was still ongoing, and the Commission had not yet decided whether there was a basis to bring a case.

⁵² See Maxim Staff Notice of Alleged Violations (Nov. 3, 2014), <https://www.ferc.gov/enforcement/alleged-violation/notices/2014/maxim-nav-11-03-2014.pdf?csrt=8580483965265983313> (alleging Maxim, Kyle Mitton, and one other executive engaged in market manipulation); see also *Maxim Power Corp.*, 156 FERC ¶ 61,223, Stipulation and Consent Agreement, at PP 23, 25 (2016) (reaching a settlement with the Maxim corporate entities and releasing all other Maxim affiliates and employees, including Kyle Mitton and the other executive named in the NAV, from liability).

addition to companies, the potential harm caused by the policy is more significant than it was when FERC first established the policy.⁵³

Notably, the Commission has issued only one NAV since August 2017. While the inference is that the Commission may have rethought the NAV policy internally, there has been no public announcement of a change in policy, which creates some uncertainty about the status of the policy going forward. For this reason, the Commission should remove this uncertainty by formally rescinding the policy.

V. Improve Enforcement Policies to Promote Market Participation and Liquidity, Including Reforms to FERC’s Price Reporting Policy

The Commission should ensure enforcement policies facilitate market participation and liquidity. Enforcement, the Commission, and a wide range of experts have recognized the importance of robust and liquid markets for various reasons, including deterring market manipulation, as liquid markets are self-correcting and less susceptible to manipulation.⁵⁴ Improving the transparency, efficiency, and fairness of the Commission’s enforcement program as suggested above will itself promote more robust market participation.

There is some concern among market participants that the Commission’s current price reporting policy increases regulatory risk and uncertainty for price reporters, which may be responsible for the drop in price reporting—a result that is harmful to markets. While price reporting trends are beyond the scope of this White Paper, the Commission can bolster market participant confidence and facilitate price reporting through adoption of a few key changes. The Commission has recognized the value of voluntary price reporting to market liquidity and confidence.⁵⁵ Given the benefits of a transparent market, the Commission should take steps to

⁵³ At the time the Commission issued the *2009 NAV Order*, the Commission had only pursued individual liability in one enforcement case. The NAV orders, therefore, focused principally on the potential harm to companies. With individual liability now a central component of the Commission’s enforcement program, the risk of reputational harm from the NAV is more significant than it was when the Commission established the NAV policy. *See FERC Should Rescind Its NAV Policy* at 93-94.

⁵⁴ *See, e.g.,* Shaun D. Ledgerwood & Paul R. Carpenter, The Brattle Grp., *A Framework for the Analysis of Market Manipulation*, 8:1 REV. L & ECON. 253, 283 (2012), http://files.brattle.com/files/6998_a_framework_for_the_analysis_of_market_manipulation_ledgerwood_carpenter_rev_law_econ_sep_2012.pdf (“The oft-stated solution to abate efficiency concerns from price-based manipulation is to maximize the liquidity in the price formation process at all times such that manipulative behavior is muted or negated through robust trading.”); FED. ENERGY REG. COMM’N, ENERGY MARKET OVERSIGHT AND ENFORCEMENT: ACCOMPLISHMENTS AND PROPOSAL FOR ENHANCED PENALTY AUTHORITY 1 (2005), <https://www.ferc.gov/legal/maj-ord-reg/land-docs/03-2005-cp-rept.pdf> (noting Enforcement’s recognition of the importance of “encouraging increased participation and liquidity in [FERC-jurisdictional] markets”); *Developments in Natural Gas Index Liquidity and Transparency*, Supplemental Notice of Technical Conference, Docket No. AD17-12-000 (June 21, 2017) (providing notice and agenda for technical conference to address the robustness and liquidity of natural gas markets, including the volume of fixed-price transactions and the reporting of those transactions to index developers); Comments of the Natural Gas Supply Association, Docket. No. AD17-12-000 (July 31, 2017).

⁵⁵ *See generally* *Policy Statement on Natural Gas and Elec. Price Indices*, 104 FERC ¶ 61,121 (2003) (“2003 Price Reporting Policy Statement”).

minimize the costs and perceived regulatory risk so that regulation and enforcement risk do not become a barrier to price reporting.

The following proposals would improve the Commission's price reporting policy:

1. Enhance the Efficiency of the Annual Independent Audit and FERC Price Reporting Audits. One improvement that would reduce the cost and burden of price reporting would be to change the self-audit requirement from an annual requirement to an every-other-year requirement. The price reporting safe harbor requires that data providers conduct an independent audit of their data gathering and submission processes at least once annually. Requiring a price reporting self-audit less frequently would not only reduce the burden of price reporting, but would free up compliance resources that could be more effectively used elsewhere (e.g., to audit other parts of its business).

The Commission could also promote efficiency and reduce costs to market participants by relying on price reporter certifications and applying a materiality threshold to price reporting audits. An internal audit conducted in a manner that follows generally accepted auditing standards is a key principle of the Commission's safe harbor and should adequately assure Division of Audits' ("DA") staff of the company's adherence to the price reporting guidelines. Likewise, the Commission could apply a materiality threshold in price reporting audits so that audit resources are focused on conduct that actually affected index prices rather than insignificant clerical errors.

2. Clarify that the Commission Will Not Consider a Company's Policy to Price Report in Either the Daily or Monthly Market, But Not Both, Selective Reporting and a Violation of the FERC Price Reporting Guidelines. Another improvement to the Commission's price reporting policy that would promote market participation and greater reporting is to allow market participants to price report in either the daily or monthly market without risk that doing so may be considered by the Commission as "selective" reporting. Companies differ in terms of how they use the two different markets, and it is not uncommon for companies to use one market more extensively than the other based on their business needs. For this reason, the burden and relative benefit to a company of price reporting in one market may be different than the other, and the Commission's policy should accommodate that. Thus, the Commission should clarify that it will not consider a company's policy to price report in either the daily or monthly market, but not both, selective reporting and a violation of the FERC price reporting guidelines.

3. Strengthen the Commission's Safe Harbor Policy to Improve Regulatory Certainty for Price Reporters. The "safe harbor" for price reporting established in the *2003 Price Reporting Policy Statement* generally provides "a rebuttable presumption that companies and individuals that report trade data to index developers in accordance with the standards adopted [by the Commission] are doing so in good faith, and will not be investigated or subjected to administrative penalties for inadvertent mistakes made in the course of reporting energy transaction information."⁵⁶ The Commission established the safe harbor to "provide a measure of regulatory certainty to the process of reporting transaction data and encourage more industry participants to contribute to the formation of price indices."⁵⁷ However, the Commission's standards for "good

⁵⁶ *Id.* at P 5.

⁵⁷ *Id.*

faith” and “inadvertent errors” are neither sufficiently transparent nor sufficiently defined to allow reporting entities to believe that they can avoid being penalized for clerical errors. While the safe harbor is important, for many market participants, it still does not provide enough regulatory certainty to justify the business risk and expense of reporting transaction data.⁵⁸

A well-structured safe harbor policy could provide greater regulatory certainty, which would encourage greater price reporting and more confidence and liquidity in fixed-price markets. The Commission should explore ways to increase confidence in the safe harbor protection, since many market participants do not believe that the current safe harbor provides enough protection and, therefore, see the risk of complying with it as too high to justify price reporting.

VI. Address Enforcement Action Procedures and Statute of Limitations Policy Under the Federal Power Act in Light of Court Rulings

The recent FPA market manipulation cases to be litigated in federal district court have led to several decisions addressing both the procedures applicable to “*de novo* review” district court actions and how the five-year statute of limitations should be applied in such cases. In light of these court decisions, clarification of the Commission’s position on these issues would eliminate confusion and provide regulatory certainty for future investigations and enforcement actions.

A. Formally Accept the Unanimous Decisions of Federal Courts that “De Novo Review” Cases are Ordinary Civil Actions

The FPA and the NGA contain different procedures for adjudicating enforcement cases that do not settle. For example, the NGA appears to contemplate a traditional agency adjudication, i.e., a hearing before an Administrative Law Judge, followed by the Commission’s determination of liability, with a right of appeal to a federal circuit court of appeals.⁵⁹ The FPA, on the other hand, allows a subject to elect between a traditional agency adjudication and an alternative procedure in which the Commission assesses a penalty “promptly,” without an administrative hearing, but the penalty must be enforced by the Commission in a federal district court enforcement action where the court has authority to review the matter “*de novo*.”⁶⁰

In every FPA market manipulation enforcement case to reach the Order to Show Cause stage, the subject has elected the alternative *de novo* review procedure. In every subsequent district court enforcement action, the Commission has argued that the court should treat the proceeding as involving a review of an agency record—which Enforcement defined as the Commission’s penalty

⁵⁸ See, e.g., Post-Technical Conference Comments of the American Gas Association, Docket No. AD17-12-000, at 6-7 (July 31, 2017); Comments of the Natural Gas Supply Association, Docket No. AD17-12-000 (July 31, 2017).

⁵⁹ See 15 U.S.C. § 717t-1(b) (“The penalty shall be assessed by the Commission after notice and opportunity for public hearing.”).

⁶⁰ 16 U.S.C. § 823b(d). Note that many market participants and defense counsel think statutory changes could make the Commission’s enforcement procedures clearer, fairer, and more efficient. While there is not consensus on what those changes should be, an alignment of enforcement procedures for all entities regulated by FERC is one possibility. A quicker, more efficient process for bringing enforcement cases in federal court is another. Potential statutory changes, however, are beyond the scope of this White Paper as they require Congress, not the Commission or Enforcement, to act.

assessment order and the information before the Commission when issuing that order rather than as an ordinary civil action, i.e., a complaint initiating a new civil action governed by the Federal Rules of Civil Procedure. While recognizing some statutory ambiguity, all the federal courts to address this issue have decided in favor of the subjects, holding that district court enforcement actions should proceed as ordinary civil actions.⁶¹

The Commission should formally announce that it accepts the courts' decision on this issue and will no longer argue in future cases that district court enforcement actions are something other than ordinary civil actions. At some level, the unanimous view of seven federal courts leads many to view this issue as effectively decided. Indeed, Chairman Chatterjee observed in October 2017 (prior to the most recent two decisions) that "the courts have rejected FERC's interpretation of *de novo* review five times . . . The courts have spoken, and I, for one, am listening."⁶² However, neither the Commission nor Enforcement have announced any change in policy that reflects the courts' decisions. The Commission should now provide regulatory certainty by formally announcing that it will no longer advance its prior position on *de novo* review.

B. Revisit the Commission's Order to Show Cause Process

Exactly how enforcement processes at the Commission should be changed based on these district court rulings is a complex legal and policy discussion beyond the scope of this White Paper. The issue, however, is important and worthy of Commission study, and may provide an opportunity to reform enforcement processes in a way that leads to the more efficient resolution of litigated cases. For instance, one consequence of the courts' decisions on *de novo* review is that they could cause the Commission's Order to Show Cause process in FPA *de novo* review cases to become less resource-intensive. The Order to Show Cause process has generally taken many months to complete, with subjects and Enforcement submitting extensive briefing and the Commission issuing detailed penalty assessment orders (in some cases exceeding 100 pages). Now that courts have made clear that *de novo* review cases are ordinary civil actions, not reviews of agency orders or records, the Commission should reconsider its current Order to Show Cause process to ensure that there is productive and efficient use of the Commission's and subjects' time and resources. As Commissioner LaFleur observed, the district court decisions on *de novo* review "give [the Commission] an opportunity to look hard at our internal enforcement processes to make sure they are as timely and effective as they could be, consistent with our statutory responsibilities and due process."⁶³

⁶¹ Opinion and Order, *FERC v. Coaltrain Energy, L.P.*, No. 2:16-cv-732 (S.D. Ohio Mar. 30, 2018), ECF No. 45; *FERC v. Powhatan Energy Fund, LLC*, 286 F. Supp. 3d 751, 757-58 (E.D. Va. 2017); *FERC v. Silkman*, 233 F. Supp. 3d 201 (D. Me. 2017); *FERC v. Barclays Bank PLC*, 247 F. Supp. 3d 1118 (E.D. Cal. 2017); *FERC v. ETRACOM LLC*, No. 2:16-cv-1945-SB, 2017 U.S. Dist. LEXIS 33430 (E.D. Cal. Mar. 7, 2017); *FERC v. City Power Mktg., LLC*, 199 F. Supp. 3d 218 (D.D.C. 2016); *FERC v. Maxim Power Corp.*, 196 F. Supp. 3d 181 (D. Mass. 2016).

⁶² Neil Chatterjee, Chairman, FERC, Statement at Energy Bar Ass'n 2017 Mid-Year Energy Forum (Oct. 17, 2017), <https://www.ferc.gov/media/statements-speeches/chatterjee/2017/10-17-17-chatterjee.asp#.XBJK1ExFyUl>.

⁶³ Tr. of 1037th Commission Meeting, Remarks of Cheryl A. Fleur, Comm'r, FERC at 25-27 (Nov. 16, 2017) <https://www.ferc.gov/CalendarFiles/20171130074739-transcript.pdf?csrt=11252446675751839139>.

C. Establish a Policy that Enforcement Claims “Accrue” for Purposes of the Statute of Limitations at the Time of the Conduct

The Commission should provide regulatory certainty about how it will interpret the five-year statute of limitations for *de novo* review enforcement actions going forward. The district court in the pending *Powhatan* case, which struggled with how to apply the five-year statute of limitations in the context of a FPA *de novo* review case, expressly invited the Commission (or Congress) “to clarify the expected procedure, including addressing whether an internal statute of limitations would provide guidance to affected parties.”⁶⁴ The Commission should now do so. The best approach would be for the Commission to adopt the policy that, going forward, it will consider the date a claim accrues in a *de novo* review case to be when the conduct occurred rather than the conclusion of the Order to Show Cause administrative proceeding. Even if FERC thinks this may not be required legally, it can (and should) still decide to do so in the interest of certainty, fairness, and efficiency.

How the statute of limitations applies in FPA *de novo* review cases has been contested in several pending and resolved enforcement actions. In brief, the Commission has argued that because it statutorily cannot file a district court enforcement action in a *de novo* review case until 60 days after the subject fails to pay the penalty assessed in the Order to Show Cause proceeding, its claim does not “accrue” until that date (meaning it has five years from then to file its case in court). Because the Commission controls the timing of the Order to Show Cause process that culminates in a penalty assessment order (including when it initiates an Order to Show Cause proceeding and how long it takes to decide the proceeding), this view results in the Commission having an effectively limitless amount of time to file a case in federal court. Subjects, on the other hand, have argued that despite whatever administrative prerequisites to filing a case might apply, the statute of limitations nevertheless runs from the date of the alleged violation (i.e., when the conduct occurred)—and that the Commission’s view runs counter to the core purpose of the statute of limitations, namely, providing a sensible and predictable timeframe by which a legal claim must be pursued. District courts thus far have reached different conclusions, with the court in the *Barclays* case accepting the subjects’ view, and courts in the *Powhatan* and *Silkman* cases accepting FERC’s view.⁶⁵ The *Powhatan* decision is currently on appeal to the U.S. Court of Appeals for the Fourth Circuit.

While pending cases will be decided in court, the Commission should provide regulatory certainty to industry in future cases by establishing a statute of limitations policy that is both legally defensible and consistent with the Commission’s objectives of fairness and efficiency. It is appropriate for claims to begin to “accrue” for purposes of the statute of limitations at the time when the underlying conduct occurred. First, that is the most legally defensible position—and adopting it would avoid the need for the Commission and subjects to litigate statute of limitations issues in future cases, which unnecessarily consumes resources and delays reaching the merits of cases. Second, this position promotes legal and regulatory certainty on all sides—the Commission

⁶⁴ *FERC v. Powhatan Energy Fund, LLC*, 345 F. Supp. 3d 682, 696 n.29 (E.D. Va. 2017) (“*Powhatan*”), appeal docketed, No. 18-2326 (4th Cir. Nov. 5, 2018).

⁶⁵ *Powhatan*, 345 F. Supp. 3d 682; *FERC v. Barclays Bank PLC*, No. 2:13-cv-02093-TLN-DB, 2017 WL 4340258 (E.D. Cal. Sep. 29, 2017); *FERC v. Silkman*, No. 1:16-cv-00205-JAW, 2019 WL 113782 (D. Me. Jan. 4, 2019).

would know that its enforcement actions are timely, and subjects (and the broader industry) would know that the Commission would bring enforcement actions within five years of the conduct occurring. Third, it would promote efficiency and fairness. Even the district court in the *Powhatan* case—which reluctantly accepted FERC’s position in a decision now pending on appeal—found that the subjects’ position that a claim accrues at the time the conduct occurs was “commonsensical” and “seem[ed] more consistent with the overall statutory scheme of [the FPA] and the purposes of statutes of limitations.”⁶⁶ Other similar enforcement agencies (including the SEC and CFTC) routinely file federal court enforcement actions within five years of the conduct, and FERC—particularly if it adopts other reforms proposed in this White Paper to make its enforcement processes more efficient—could do so as well.

VII. Improve the Transparency and Efficiency of Audits

The transparency and efficiency improvements discussed in the preceding sections are focused on improving Enforcement investigations. However, there are also opportunities for the Commission to increase the transparency and efficiency of audits, which are also conducted by Enforcement through its Division of Audits (or “DA”).

Audits serve as an important oversight tool of the Commission and play a key role in FERC’s core regulatory function of ensuring that jurisdictional rates are just and reasonable. Audits serve as a resource for the Commission to examine areas of risk and can result in refunds and recoveries to customers.⁶⁷ Audits also allow companies to receive constructive feedback on their compliance programs. Audits are fundamentally different from investigations, as the purpose of audits is not to “find wrongdoing” but rather to oversee and improve compliance. The Commission and Enforcement have been very effective at preserving this important distinction.

While audits and investigations are different endeavors, they have similarities in that both involve, to a significant degree, fact-gathering, with staff obtaining and analyzing data relating to a particular subject matter. Therefore, some of the transparency and efficiency improvements discussed above with respect to investigations (especially in Sections I and II) could also improve the audit process. We offer below four specific proposals to improve the audit process.

A. Keep the Audit Scope Clear, Defined, and Focused on the Core Compliance Questions at Issue With an Identified Expected Completion Date

While audits almost always require companies to devote substantial time and resources, the cost and burden is even more significant when the initial scope of the audit is overly broad or the scope broadens or changes significantly over the course of the audit. In such cases, it can be difficult to complete the audit in an efficient manner, and the resources needed to fully respond to the audit may be disproportionate to the magnitude of the issue being audited. One improvement to the audit process, therefore, would be to provide greater clarity and transparency into the scope and progress of the audit by not only defining the scope clearly at the outset, but also ensuring that the scope is limited to a defined set of topics or areas and can be completed in a reasonable amount

⁶⁶ *Powhatan*, 345 F. Supp. 3d at 695, 711.

⁶⁷ See, e.g., 2018 REPORT ON ENFORCEMENT at 5 (noting that FY2018 audits “directed \$185.1 million in refunds and recoveries”).

of time. A change or expansion of the audit's scope should be a considered decision based on good cause, and immediately communicated to the subject at the time it occurs.

DA staff should also clearly communicate to the subject the status and timeline of the audit, which is often unclear to subjects. For example, subjects sometimes think DA staff has completed its data requests only to receive additional requests after not hearing from staff for a lengthy period. While it is understandable that there could be delays between sets of data requests as staff works to analyze the information produced, DA staff, throughout the audit process, should keep subjects apprised of the progress of the audit and the expected timeline for completion. Discussions with the subject about an audit timeline should also build in sufficient time for the subject to review and comment on the draft audit report. In fact, in most instances, subjects will require several weeks to respond to the draft report if the subject has concerns or disagreements about the draft.

Finally, frequent discussions around DA staff concerns during the audit, and before the exit conference and draft report are presented, are essential for subjects to fully understand the key issues and to provide the clarification and explanations needed by DA staff. Such open discussions and engagement could lead to agreement about remedial steps that could be taken during the audit process, which could further enhance the role of audits in helping to achieve industry compliance.

B. Use Standardized Data Requests to the Extent Possible

A key distinction between investigations and audits is that each investigation is unique and involves some suspicion of potential wrongdoing, whereas audits do not. As a result, there is a greater degree of standardization in audits with respect to the areas of compliance examined and the information needed to evaluate compliance. Because similar audits will require the Commission to obtain and review similar information, the Commission could improve the efficiency of the audit process by standardizing data requests to the extent possible. For example, audits of electric utilities' compliance with sections of the *pro forma* open access transmission tariff ("OATT") should generally seek the same type of data and documents, particularly for initial data requests seeking background information and information on the control environment. The Commission could also publish these standardized requests so industry can be better prepared for audits, which would also likely improve the efficiency and transparency of the audit process.

C. Provide Periodic Updates on Common Errors and Findings in Audits

While Enforcement's Annual Report has a helpful summary of DA's work over the previous year, regular, ongoing audit compliance tips would be even more helpful in promoting compliance and reducing industry errors. The Commission should consider providing industry with more real-time guidance on common errors and findings in audits. While some of this information can be gleaned from public audit reports, individual audit reports do not show broader trends or reflect whether compliance issues arose from circumstances unique to the company under audit. Moreover, given the length of audits, audit reports are often not issued until long after the Commission identified potential compliance errors.

This type of regular, ongoing guidance could be provided in various ways, including, for example, periodic releases by DA on FERC's website that highlight specific areas of concern staff has identified from ongoing audits—along with guidance on ways to avoid or address those

concerns. For example, on a regular basis (e.g., quarterly), DA could publish a relatively short, focused list summarizing audit take-aways for industry—not necessarily commentary on the specific audits conducted but rather staff’s views about “common errors” as well as “best practices” companies could follow to avoid or minimize audit concerns. DA has done this recently following its completion of a number of audits regarding utility compliance with mandatory Critical Infrastructure Protection (“CIP”) Reliability Standards.⁶⁸ That format and approach has been very useful to reliability compliance personnel as it identifies common areas of concern and allows utilities to assess their own performance in those areas. Similar reports on other audit topics would be equally beneficial to the regulated community.

VIII. Conclusion

This White Paper offers several proposals that would enhance the transparency, efficiency, and fairness of the Commission’s enforcement program, making it even stronger and more effective in accomplishing FERC’s fundamentally important goal of achieving compliance. The trade associations that sponsored this White Paper look forward to receiving feedback from the Commission, hearing the views and ideas of other participants in FERC-regulated markets, and finding the best approaches for advancing these and similar proposals.

⁶⁸ FED. ENERGY REG. COMM’N, 2018 STAFF REPORT: LESSONS LEARNED FROM COMMISSION-LED CIP RELIABILITY AUDITS (2019), <https://ferc.gov/legal/staff-reports/2019/2018-report-audits.pdf>.

The **American Gas Association** (AGA), founded in 1918, represents more than 200 local energy companies that deliver clean natural gas throughout the United States. There are more than 74 million residential, commercial and industrial natural gas customers in the U.S., of which 95 percent — more than 71 million customers — receive their gas from AGA members. AGA is an advocate for natural gas utility companies and their customers and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international natural gas companies and industry associates. Today, natural gas meets more than one-fourth of the United States' energy needs.

The **Edison Electric Institute** (EEI) is the association that represents all U.S. investor-owned electric companies. Our members provide electricity for about 220 million Americans, and operate in all 50 states and the District of Columbia. As a whole, the electric power industry supports more than 7 million jobs in communities across the United States. In addition to our U.S. members, EEI has more than 60 international electric companies, with operations in more than 90 countries, as International Members, and hundreds of industry suppliers and related organizations as Associate Members. Organized in 1933, EEI provides public policy leadership, strategic business intelligence, and essential conferences and forums.

Launched over 20 years ago, the **Electric Power Supply Association** (EPSA) is the national trade association representing leading independent power producers and marketers. EPSA members provide reliable and competitively priced electricity from environmentally responsible facilities using a diverse mix of fuels and technologies. Power supplied on a competitive basis collectively accounts for 40 percent of the U.S. installed generating capacity. EPSA seeks to bring the benefits of competition to all power customers.

The **Interstate Natural Gas Association of America** (INGAA) is a non-profit trade association that advocates regulatory and legislative positions of importance to the natural gas pipeline industry in the United States. INGAA's member companies transport over 95% of the nation's natural gas through a network of nearly 200,000 miles of pipelines. The interstate pipeline network serves as an indispensable link between natural gas producers and the American homes and businesses that use the fuel for heating, cooking, generating electricity and manufacturing a wide variety of U.S. goods, ranging from plastics to paint to medicines and fertilizer.

The **Natural Gas Supply Association** (NGSA) represents integrated and independent companies that supply natural gas. Founded in 1965, NGSA is the only national trade association that solely focuses on producer-marketer issues related to the downstream natural gas industry. NGSA has been involved in a substantive manner in every one of the Federal Energy Regulatory Commission's significant natural gas rulemakings since FERC's creation in 1977.

The views and opinions expressed in this White Paper do not necessarily reflect those of any particular member of the sponsoring associations.