

FERC Investigations: Uncertainty Rules as More Entities Challenge in Federal Court

Q What triggers a Federal Energy Regulatory Commission (FERC) investigation and what does the process entail?

Matt Connolly: Most investigations involve allegations of market manipulation and false statements. FERC also investigates non-compliance with market tariffs or reliability standards and violations of market behavior rules. FERC typically initiates an investigation based on: (i) a company self-reporting a possible violation; (ii) a market monitor reporting anomalous trading activity in an organized electricity market; (iii) a whistleblower claim, including through FERC's Enforcement Hotline; or (iv) FERC's Enforcement staff identifying anomalous trading behavior.

Once an investigation is underway, FERC will request information voluntarily, but it can also issue subpoenas and compel documents. FERC may seek investigative testimony under oath. A market participant may also submit written information to FERC anytime. An investigation can take several years.

Q What are some potential pitfalls companies may encounter in the investigation process?

MC: Discovery productions should be navigated carefully. FERC has alleged obstruction in some cases based on incomplete document productions. Before submitting a referral to FERC, market monitors may ask traders questions, but not inform them that it's for a potential investigation. Traders should therefore preserve records and document the purpose behind any new or unique trading strategies, and ensure that it provides thorough responses to FERC and market monitors.

Consequences can be severe—FERC frequently requires disgorgement and civil penalties in an enforcement action. The largest penalty assessed to date is \$435 million.

Q How can participants challenge a penalty?

MC: There is a lot of uncertainty. A participant facing an enforcement penalty under the Federal Power Act ("FPA") or Natural Gas Act ("NGA") is entitled to an administrative hearing. Instead of an administrative hearing, the FPA (but not the NGA) permits market participants to elect for *de novo* review in federal court. Participants have overwhelmingly chosen review in federal court. Two federal courts recently held, over FERC's objections, that *de novo* review of a FERC enforcement action entitles defendants to the full benefit of the Federal Rules of Civil Procedure. This likely means that a company may seek discovery from FERC and third parties, take depositions, cross-examine witnesses, and have its case determined by a jury. FERC has publicly stated that it disagrees with these decisions, and it continues to seek summary review based solely on the administrative record. No appeals court has ruled on this issue.

Q Can you describe any current trends in Enforcement activities?

MC: Significantly, more participants have chosen to challenge Enforcement actions, either in federal court or before an ALJ. Last year FERC initiated seven litigation proceedings, the most Enforcement has ever had in a year. FERC continues to charge individuals, either in settlements or litigation. In the past, Enforcement has rigidly applied its Penalty Guidelines to market manipulation cases, typically deviating only when a participant shows financial hardship. That may be changing, as FERC recently settled its first manipulation case with a below guidelines penalty and no hardship showing. This may also be a unique event.

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