

Energy Policy Act of 2005

Market Reforms

The Energy Policy Act of 2005:
A Restructured World for Electric Utilities
EXNET/Bruder, Gentile & Marcoux, L.L.P.
September 28, 2005

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EPA 2005 Market Reforms

- Market Transparency and Market Manipulation
- FERC Refund Authority
- FERC Penalty Authority

Electricity Market Transparency Rules

- Establishes new Section 220 of FPA.
- Directs FERC to facilitate price transparency in markets for wholesale electric energy and transmission.

Electricity Market Transparency Rules

- Authorizes FERC to establish rules for dissemination of information about price and availability of wholesale electric energy and transmission.
 - FERC can obtain information from any market participant.
 - FERC can rely on third parties to receive and disseminate the information (subject to disclosure rules).

Electricity Market Transparency Rules

- Requires FERC to consider and rely on the price transparency provided by existing publishers of price indices and providers of trade processing services to the maximum extent possible.
- Authorizes FERC to establish an “electronic information system” if FERC determines that the existing price publications are not adequately providing price discovery or market transparency.

Electricity Market Transparency Rules

- Exempts disclosure of information that FERC determines would be detrimental to operation of an effective market or jeopardize system security if disclosed.
- Does not affect Electric Quarterly Reporting and other existing reporting requirements.

Implications of Section 220

- In the 2003 FERC Policy Statement on price indices, FERC signaled concern about the level of voluntary reporting to publishers of price indices and about the robustness of price indices.
- At the end of 2004, FERC reported “notable progress” in price indices reporting, but directed FERC Staff to continue careful monitoring. In July 2005, FERC stated that it was continuing to monitor.
- Because of the liability risks under FERC Market Behavior Rules and other laws, some companies have stopped reporting to publishers of price indices.

Implications of Section 220

- We anticipate that, within 18 months, FERC will investigate and issue a report finding that market transparency is inadequate under nation's price indices and price publications.
- We anticipate that, within 3 years, FERC will establish and FERC (or a third party) will administer a nationwide Energy Information System.

Implications of Section 220

- Imagine the possibilities:
 - Every electric LMP price and price index in the country on one website.
 - For other regions, a list of all electric transaction prices based on the point of delivery/locality/state/region.
 - Transmission prices and continuously updated ATC for every transmission system on one website.

Market Manipulation

- Establishes new Section 221 and 222 of the FPA.
- Section 221 Prohibition on Filing False Information.
 - No entity shall willfully and knowingly report any information relating to the price of a wholesale sale of electric energy or the availability of transmission capacity, which information the person knew to be false at the time of reporting, to a Federal agency with intent to fraudulently affect the data being compiled by the Federal agency.

Market Manipulation

- Section 222 Prohibition on Energy Market Manipulation
 - It is unlawful for any entity to use, in connection with a wholesale sale of electric energy “any manipulative or deceptive device or contrivance” (as those terms are defined by the SEC Act of 1934) in violation of FERC rules and regulations.

Market Manipulation

- “Any Manipulative or Deceptive Device or Contrivance”
 - The U.S. Supreme Court has said that manipulation refers generally to practices, such as wash trades or rigged prices, that are intended to mislead investors by artificially raising market activity.
 - Deceptive conduct refers generally to material misrepresentations or material failures to disclose with the intent to defraud.

FERC Refund Authority – 60 More Days

- Amends Section 206 of the FPA to allow the refund effective date to begin 60 days earlier.
 - Third party complaint: The refund effective date can begin the date the complaint was filed or up to 5 months after the complaint was filed.
 - FERC investigation on its own motion: The refund effective date can begin the date FERC publishes notice of its intent to initiate an investigation/proceeding or up to 5 months after this publication is made.

FERC Refund Authority

- If FERC has not issued a final decision in a refund case within 180 days, FERC must report why it has failed to do so and provide an estimate of when it will issue its decision.

FERC Refund Authority

- Addition of FPA Section 206(e), which extends FERC refund authority to traditional, non-jurisdictional market participants under Section 201(f) (i.e. utilities owned by municipalities, states or the federal government) that voluntarily make short-term sales through an organized market at rates established by FERC-approved tariff and the sale violates the terms of the tariff or applicable FERC rule.
- A short-term sale is for a period of 31 days or less.
- Section 206(e) does not apply to electric cooperatives or any entity that sells less than 8 million MWH.

FERC Penalty Authority

- Pre-EPA 2005:
 - FERC had little civil penalty authority for electric.

FERC Penalties

Then



- Under FPA Section 315, FERC may assess a civil penalty of up to \$1,000 for willful failure to comply with FERC orders or reporting requirements or willful failure to produce information in an investigation. (Note: Does not apply to FPA Sections 211-214).
- Under FPA Section 316A, FERC may assess a civil penalty of up to \$10,000 per day for violations of FPA Sections 211-214.

Penalty Authority for Electric Greatly Expands

- Post-EPA 2005:

FERC Penalties
Now



New FERC Penalty Authority

- Post-EPA 2005:
 - Civil Penalty Authority:

For any violation of Part II of the FPA (e.g., Sections 203, 205, and new sections 220, 221, and 222), FERC could assess a penalty of up to \$1 million per day of the violation.

- Three-year statute of limitations for assessing civil penalties for Section 221 market transparency violations (but no limit for Section 222 market manipulation violations).

New FERC Penalty Authority

- Post-EPA 2005:

- Criminal Penalty Authority:

Any person who willfully or knowingly does an act prohibited by the FPA, or omits or fails to do an act required by the FPA could be imprisoned up to 5 years (increased from two years) and face a fine of up to \$1 million (increased from \$5,000). In addition a fine could be assessed of up to \$25,000 per day of the violation (increased from \$500).

New FERC Penalty Authority

- Post-EPA 2005:
 - Violators of Section 221 Prohibition on Filing False Information: Persons who violate Section 221 can be banned by a federal court from acting as an officer or director of an electric utility or engaging in the trading of wholesale electric energy or transmission services.

NOTE: On the day after the EXNET/BG&M conference, Sam E. Fowler, Democratic Chief Counsel, U.S. Senate Committee on Energy and Natural Resources, publicly stated that the above provision was not intended by Congress to apply to FPA Section 221. Instead, he said that the provision was intended to apply to FPA Section 222 on electric market manipulation, which would parallel the EAct05 changes for the Natural Gas Act. He raised the hope, but not the guarantee, that Congress would issue subsequent technical correction legislation to change the EAct05 Section 1288 reference from Section 221 to Section 222.

Implications of New FERC Penalty Authority

Prior Regime: FERC Chairman Wood



Often
Seeking
compliance by
the carrot!

Implications of New FERC Penalty Authority

New Regime: FERC Chairman Kelliher



Enforcing
Compliance by
the Stick!

Implications of New FERC Penalty Authority

Proposed Penalties – Will they be Kelliher's cure-all?

- Order 888 OATT reform NOPR
- Reliability NOPR
- New England LICAP order argument: In response to the argument that generators under LICAP could collect more revenue by exercising market power and increasing prices, Kelliher quickly responded that FERC's new penalty authority would discourage the exercise of market power by generators.

FERC Compliance Audits

- Standards of Conduct
- Code of Conduct
- OASIS posting requirements
- Electric Quarterly Reports
- Market Behavior Rules