

Standards of Conduct and Compliance Audits

The Saga Continues...

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History of Order No. 2004 Standards of Conduct

- NOPR 2001
- Order No. 2004 2003
- 2004-A 2004
- 2004-B 2004
- 2004-C 2004
- 2004-D 2005

D.C. Circuit Appeal of Order No. 2004

- Interstate gas pipelines pursued appeals of the heart of the rulemaking changes.
- The electric industry sat it out...
- In November 2006, the Court vacated Order No. 2004.
- Gas and electric transmission providers read the headlines and rejoiced!

D.C. Circuit Appeal of Order No. 2004

NOT SO FAST!!!

D.C. Circuit Appeal of Order No. 2004

- **Court vacated Order No. 2004 Standards of Conduct with respect to gas transmission providers only.**
 - ✓ Court held there was no evidentiary record to support extension of the rules to the gas transmission providers' non-marketing energy affiliates. Kelliher and Brownell agreed in Order No. 2004-A.
- **Order No. 2004 is in full force and effect for electric transmission providers.**
- On the date the Court order would take effect and eliminate Order No. 2004 regulation of gas transmission providers, FERC issued an **Interim Rule** that put the portions of Order No. 2004 that were not rejected by the court back in place (January 2007).

FERC Issues Standards of Conduct NOPR

Non-Marketing Energy Affiliates

- Consistent with D.C. Circuit decision, FERC proposes to eliminate application of the Standards of Conduct to **gas pipelines' non-marketing Energy Affiliates**.
- FERC requests comment as to whether it should eliminate application of the Standard of Conduct to **electric transmission providers' non-marketing Energy Affiliates**.
- FERC asks - should the rule be uniform for gas and electric?
 - ✓ Lessen industry compliance burden.
 - ✓ Ease FERC Staff's compliance oversight.

Proposal to Eliminate Non-Marketing Energy Affiliates

- **What would it mean?**
- The Standards of Conduct for gas and electric transmission providers would apply to:
 - ✓ **The sales unit in the transmission provider**, unless such unit solely engages in bundled retail sales; and
 - ✓ **Electric and gas marketing affiliates.**
- The NOPR also proposes to extend the Standards of Conduct to **asset managers or agents that control transmission capacity**. (There is record evidence to support this proposal in the AEP, CLECO and SCE&G cases).

Proposal to Eliminate Non-Marketing Energy Affiliates

- Standards of Conduct would not apply to:
 - ✓ Affiliates engaged in electric and gas financial trading;
 - ✓ Producers, gathers and processors;
 - ✓ Local gas distribution companies; and
 - ✓ Interstate and Hinshaw pipelines.

Integrated Resource Planning

- Industry expresses need for guidance and clarity because the rules impede IRP.
 - ✓ April 7, 2006 FERC technical conference
 - ✓ FERC Staff informal outreach to industry in Summer 2006
- In the NOPR, FERC expresses the view that improved coordination in transmission and generation planning is necessary to improve the economics and reliability of the grid.
- FERC seeks to ensure that the evaluation of transmission in planning and procurement is as accurate and efficient as possible.

Integrated Resource Planning

- FERC proposes to create two new categories of employees:
 - ✓ "Planning employees"
 - ✓ "Competitive solicitation employees"

Integrated Resource Planning

- **Order No. 2004:** Planning employees and competitive solicitation employees are either transmission or marketing employees.
- **NOPR proposal:** Planning employees and competitive solicitation employees are neither transmission nor marketing employees.

Integrated Resource Planning

- **Proposed rules for planning employees and competitive solicitation employees:**
 - ✓ They cannot engage in non-planning transmission functions or marketing activities.
 - ✓ They can obtain from transmission employees non-public transmission information necessary to conduct the planning and competitive solicitation activities.
 - ✓ They cannot be an improper conduit for passing non-public transmission information.
 - ✓ Functions are performed for bundled retail load pursuant to state-mandated IRP.

Integrated Resource Planning

- FERC seeks comment on whether and how the Order No. 2004 Standards of Conduct impede IRP.
- FERC seeks comment on its proposal for two categories of employees.
- It requests comment as to whether its proposal should be expanded beyond IRP solely for bundled retail load.
 - ✓ Should it include IRP for POLR load, wholesale requirements contracts, and/or other wholesale contracts?

NOPR Invites Comments in Other Areas

- FERC seeks comment whether additional guidance is needed for **shared employees**, such as:
 - ✓ Shared senior officers and directors;
 - ✓ Risk management employees; and
 - ✓ Attorneys.

NOPR Invites Comments in Other Areas

- In FERC Staff's informal outreach this Summer, the industry commented that there is a **substantial need for guidance concerning shared senior officers and directors**. Issues:
 - ✓ What functions and activities can shared senior officers and directors perform without becoming day-to-day operating employees?
 - ✓ Can they execute, approve or disapprove contracts?
 - ✓ Can they have access to non-public transmission information, including real-time information?
 - ✓ Can they approve or disapprove major capital and operating expenditures?
- There will be an avalanche of comments in this area.

Standards of Conduct NOPR

- FERC just granted the request of EEI and other trade associations to extend the comment due dates.
- Initial comments are now due March 30, 2007.
- Reply comments are due April 30, 2007.

Compliance Audits

- **FERC's compliance audits continue in many areas of regulation, including:**
 - ✓ OATT and OASIS compliance
 - ✓ Standards of Conduct and Code of Conduct
 - ✓ Energy Market Manipulation rules
 - ✓ EQR reporting
 - ✓ Interlocking directorate requirements
 - ✓ Compliance with record retention requirements

Compliance Audits

- When FERC issued its Standard of Conduct NOPR, it also **exercised its new EAct 2005 civil penalty authority** for the first time in settlements and stipulations with five companies.
 - ✓ Civil penalties totaled \$22.5 million
- While Standard of Conduct compliance is still important, **Chairman Kelliher indicated that he is the most concerned about OATT and OASIS compliance.**
- Kelliher noted that the three largest civil penalties were ordered against companies with OATT violations.

Compliance Audits

➤ Order No. 890 Final Rule:

- ✓ FERC adopts a strong FERC Staff audit program for OATT compliance, including operational audits.
- ✓ It encourages companies designate an OATT compliance officer and conduct independent audits.
- ✓ It does not establish a schedule of penalties for various OATT violations.

Compliance Audits

- We strongly encourage our clients to conduct internal audits of their OATT and OASIS compliance.