

## FERC Issues Revised Standards of Conduct for Transmission Providers

On October 16, the Federal Energy Regulatory Commission (FERC) issued Order No. 717, a final rule revising the Standards of Conduct for Transmission Providers, applicable to interstate natural gas pipelines regulated under the Natural Gas Act and public utilities regulated under the Federal Power Act. The revised Standards have three core elements: an independent functioning rule, a transparency rule, and a no-conduit rule. Transmission Providers may seek waivers. The new rules become effective 30 days after publication in the *Federal Register*, except that employees must be trained on the rule's requirements within 60 days of the rule's publication.

### BACKGROUND

The Standards of Conduct are intended to prevent interstate natural gas pipelines and public utilities (collectively called "transmission providers") from providing their marketing affiliates preferential access to service or non-public transmission information. FERC's Order No. 2004 had broadened the scope of the Standards of Conduct to apply to relationships between transmission providers and their "energy affiliates," which generally included any affiliate or unit involved in transmission transactions or other transactions involving natural gas or electric energy. In 2006, the U.S. Court of Appeals for the D.C. Circuit vacated Order No. 2004 to the extent that it applied the Standards of Conduct to natural gas pipelines and their non-marketing affiliates. The court found that application of the Standards to gas pipeline affiliates was not supported by substantial evidence. In response to that decision, in 2007, FERC issued an interim rule and a notice of proposed rulemaking (NOPR). Based on its own experience and concerns raised by the commenters, however, earlier this year, FERC proposed a revised and refocused approach in a second NOPR. Generally, the second NOPR proposed to abandon Order No. 2004's corporate affiliate concept, and to reinstate the "employee functional" approach that FERC applied prior to Order No. 2004.

### THE REVISED STANDARDS OF CONDUCT

The new Standards of Conduct follow the employee functional approach proposed by FERC in its 2008 NOPR.

#### *Application of the Standards of Conduct*

Order No. 717's Standards of Conduct apply to transmission providers that conduct transmission transactions with an affiliate that engages in marketing functions. A public utility is subject to the rule if it conducts such affiliate transactions and also owns, operates, or controls facilities for the transmission of electric energy in interstate commerce. A natural gas pipeline is subject to the rule if it conducts such affiliate transactions, but only if it provides open access transportation under subparts B and G of Part 284 of FERC's regulations. Thus, the Standards of Conduct do not apply to pipelines providing service solely under Part 157 of FERC's regulations, intrastate pipelines or Hinshaw pipelines. The final rule also reinstates the previous definition of "affiliate," which means, subject to rebuttal, an entity controlled by, or under common control with a specified entity.

### *Independent Functioning*

The Standards of Conduct require that transmission function employees operate independently from marketing function employees. The rule provides:

- *Transmission Functions.* Transmission functions include the *day-to-day* involvement in “planning, directing, organizing or carrying out” transmission functions. The definition is focused on short-term, real time operations, which FERC believes present the greatest opportunity for affiliate abuse, rather than long-range planning activities.
- *Marketing Functions.* Order No. 717 establishes separate definitions for natural gas and electric marketing functions. Electricity marketing includes only sales, and not purchases or “bids to buy,” and excludes bundled retail sales, and providers of last resort (POLR) when making sales in their POLR capacity. Natural gas marketing is “the sale for resale in interstate commerce, or the submission of offers to sell in interstate commerce, of natural gas.” The final rule retains longstanding exclusions for incidental purchases and sales of gas for operational purposes, sales from a seller’s own production, gathering, or processing facilities, and on-system sales by an intrastate pipeline, Hinshaw pipeline, or local distribution company.
- *Transmission Function and Marketing Function Employees.* Order No. 717 clarifies that being “actively and personally” engaged in transmission functions or marketing functions means to be engaged in either of those functions on a *day-to-day* basis. The final rule provides guidance regarding the activities of officers, directors and supervising employees, stating that merely signing off on activities without having directed or organized them does not constitute being personally engaged in them. Long range planners are excluded if not engaged in *day-to-day* transmission operations, as are field, maintenance, and construction employees, engineers and clerical workers not normally involved in such operations.

### *Transparency and Posting Requirements*

A transmission provider is prohibited from disclosing to marketing function employees non-public information about the transmission system or a transmission customer. Among other things, the final rule:

- Requires that whenever non-public transmission information has been disclosed to affiliated marketing function employees, the transmission provider must immediately post on its website a notice of the disclosure, and the information itself. If the disclosed non-public information involves a customer or critical energy infrastructure information, the transmission provider is required only to post notice of the disclosure.
- Excludes from the posting requirement exchanges of non-public transmission function information and discussions between transmission function employees and marketing function employees concerning specific requests by the latter for transmission service, provided a contemporaneous record is retained.
- Requires that any waiver of tariff provisions granted to affiliates be posted, unless the waiver is specifically approved by FERC and eliminates the requirement that pipelines post exercises of discretion, which are actions within the scope of a tariff provision, but which often require the transmission provider to exercise judgment.
- Permits a transmission provider and marketing function employees to exchange information pertaining to compliance with reliability standards.
- Deletes the requirement to post discounts, because the information is required to be posted under other regulations.



## *No Conduit Rule*

The final rule retains the long-standing no-conduit rule, which prohibits a transmission provider from disclosing non-public information to marketing function employees by using a third party conduit. The final rule eliminates the NOPR's proposal to prohibit marketing function employees from receiving non-public information about an affiliated transmission provider from any source, citing difficulties in determining how the employee received the information. Order No. 717 clarifies that employees, contractors, consultants or agents of a transmission provider or an affiliate engaged in marketing functions are covered by the no-conduit rule.

## *Training*

Order No. 717 requires that a transmission provider provide annual training on Standards of Conduct to all transmission function employees, marketing function employees, officers, directors, supervisory employees, and any other employee likely to become privy to transmission function information. Transmission providers must comply with the training requirement within 60 days after the revised Standards of Conduct are published in the Federal Register.

## **IMPLICATIONS OF THE REVISED STANDARDS**

The revised Standards of Conduct reflect FERC's response to industry concerns that regulatory requirements be clear and less complex, particularly in light of FERC's substantial civil penalty authority. By returning to the employee-function approach to the Standards of Conduct, FERC has attempted to provide more clear-cut rules regarding transmission providers' interactions with their marketing affiliates.

## **FOR ADDITIONAL INFORMATION**

Van Ness Feldman represents natural gas pipelines and electric utilities before FERC on Standards of Conduct policy, and counsels clients on the full range of Standards of Conduct compliance matters. For additional information on the final rule or for assistance on Standards of Conduct issues, please contact Susan Olenchuk, Paul Korman, or Doug Smith in Washington D.C. at (202) 298-1800, or Pam Anderson in Seattle, Washington at (206) 623-9372, or any other member of our Natural Gas or Electricity Practice Groups.

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