

FERC Issues Civil Penalty Guidelines

On March 18, 2010, the Federal Energy Regulatory Commission (FERC) issued a Policy Statement on Penalty Guidelines (Penalty Guidelines). Since 2005, FERC has been authorized to assess civil penalties of up to \$1 million per day per violation for many regulatory violations. The Penalty Guidelines establish a significant new approach for FERC to use in determining civil penalties “to be imposed on all organizations for violations of the statutes, rules, regulations, restrictions, conditions or orders overseen by [FERC].” (§1A.1.1). The Penalty Guidelines are modeled after the framework of the United States Sentencing Guidelines that apply to organizations in federal criminal cases and became immediately effective upon issuance. The Penalty Guidelines will be applied to all future violations and to “any pending investigation where Enforcement staff and the organization have not yet entered into settlement negotiations.” (P. 62). The Commission’s use of the Penalty Guidelines is discretionary, not mandatory. On April 7, 2010, FERC Enforcement staff will hold a workshop to discuss how the Penalty Guidelines will be applied and to receive comments and questions.

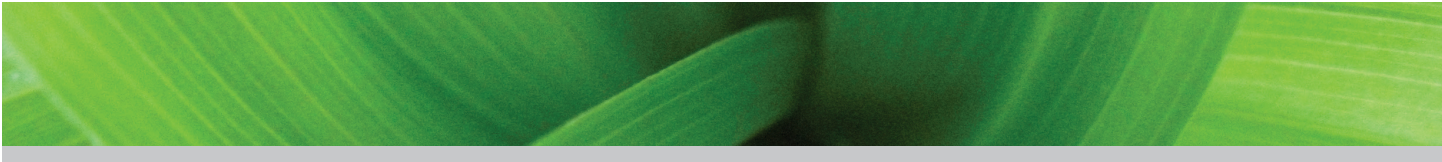
KEY ELEMENTS OF THE PENALTY GUIDELINES

The new Penalty Guidelines establish a multi-step formulaic approach to determine an appropriate range of civil penalties for a particular violation. The calculation of penalties is not simply a mathematical exercise, however, because the application of each factor under the Penalty Guidelines requires a great deal of judgment.

First, a “base penalty” amount is determined, which is the greater of (a) the dollar amount listed in a violation level penalty table contained in the Penalty Guidelines, (b) the gain to the organization from the violation, or (c) the loss caused by the violation. In a major change from FERC’s prior enforcement policy, this approach explicitly considers the pecuniary gain to the organization from the violation and the pecuniary loss caused by the violation when determining the “base penalty” amount. The Policy Statement includes a hypothetical example in which a base penalty of \$15 million is determined based upon the monetary value of the loss of electrical load that was caused by reliability standard violations. Moreover, the Penalty Guidelines explain that the calculation of pecuniary loss will be “enhanced” to reflect any loss that the organization should have incurred to prevent broader consequences, such as the value of firm load that a balancing authority should have, but did not, shed to resolve an emergency condition. This new approach of considering the pecuniary gain or loss resulting from a violation is likely to significantly increase penalties for reliability compliance violations that result in a loss of load. In addition, the Penalty Guidelines set forth a higher “base penalty” for violations that present a serious risk to market transparency, such as violations that circumvent the Commission’s natural gas capacity release rules. The determination of whether an action poses a “serious” risk and the valuation of the pecuniary gain or loss will require subjective analyses by the Commission.

Second, a “culpability score” is calculated based on an organization’s past and current conduct and efforts to remedy the violation. The calculation of the culpability score starts with a base score of “5” that is adjusted up or down depending on several culpability factors. Factors adding to the culpability score are:

- (1) whether high-level personnel in the organization participated in, condoned, or were willfully ignorant of the violation, with additional culpability points added where such actions occurred in larger organizations;

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- (2) whether the organization has a prior history of committing violations;
 - (3) whether the violation involved violation of a judicial or Commission order or injunction directed at the organization by the Commission or other Federal and state enforcement agencies; and
 - (4) whether the organization obstructed justice, or encouraged obstruction of justice, during the investigation or resolution of the violation.

Factors reducing the culpability score are:

- (1) whether the organization had an effective compliance and ethics program at the time of the violation with active engagement and leadership by senior management, effective preventive measures, prompt detection and cessation of violations and voluntary reporting of violations, and remediation of the misconduct; and
- (2) whether the organization self-reported, cooperated, and accepted responsibility for its violation. FERC will also reduce the score where the matter is resolved without the need for a trial-type hearing.

The Penalty Guidelines provide guidance on the elements of an effective compliance and ethics program, which will be used by the Commission in its determination of an organization's culpability score.

Third, the culpability score is used to determine the “minimum and maximum multipliers” which can range between 0.05 and 4.00. The base penalty is multiplied by both the minimum and maximum multiplier to determine the range of the penalty. For example, a base penalty of \$1 million multiplied by the minimum multiplier of 0.05 would produce a minimum penalty of \$50,000. The same base penalty of \$1 million multiplied by the maximum multiplier of 4.0 would produce a maximum penalty of \$4 million. The penalty range determined under the Penalty Guidelines cannot be greater than the maximum civil penalty authorized by statute. The Penalty Guidelines do not change the Commission's policy that permits FERC to independently order disgorgement of any unjust profits, plus interest, gained from a violation.

IMPLICATIONS

The new Penalty Guidelines are likely to result in significantly higher penalties in cases where a violation causes a significant pecuniary gain for the violator or loss caused by the violation, such as the costs of the loss of load resulting from a reliability compliance violation. Moreover, unlike prior Commission policy, the Penalty Guidelines do not expressly provide for a zero civil penalty for minor violations. The Penalty Guidelines leave significant discretion in the hands of the Commission on whether and how to use the new framework.

FOR ADDITIONAL INFORMATION

Van Ness Feldman has extensive experience in representing clients on all aspects of federal energy regulatory compliance. The firm regularly conducts regulatory compliance reviews, helps clients develop compliance plans and training programs, and defends clients in FERC audits, investigations and enforcement actions. For more information, please contact Andrew Art, Doug Smith or Paul Korman in our Washington, DC office at (202) 298-1800, or Malcolm McLellan in our Seattle office at (206) 623-9372, or any member of the firm's FERC practice areas.

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