

KIRKLAND ALERT

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FERC Issues New Civil Penalty Guidelines

On March 18, 2010, the Federal Energy Regulatory Commission (“Commission”) released a new Policy Statement on Civil Penalty Guidelines in Docket No. PL10-4-000 (“Policy Statement”) for violations of the Commission’s statutes, rules, regulations, restrictions, conditions, or orders. The intended purpose of the Policy Statement and the new guidelines attached thereto (“Penalty Guidelines”) is to add fairness, consistency, and transparency to civil penalty determinations.

Authority for the Penalty Guidelines Under the Energy Policy Act of 2005

The Commission derived the authority to enact the new Penalty Guidelines from the Energy Policy Act of 2005 (“EPAAct 2005”), which expanded the Commission’s civil penalty authority under the Federal Power Act (“FPA”). Prior to the passage of EPAAct 2005, the Commission’s options with regard to civil penalties were limited to (1) \$11,000 per day under Part I of the FPA, (2) \$11,000 per day under Sections 211-214 of Part II of the FPA, and (3) \$5,500 per day under the Natural Gas Policy Act of 1978 (“NGPA”). After EPAAct 2005, the Commission’s civil penalty authority was expanded in three regards. First, the Commission was granted civil penalty authority covering all provisions of FPA Part II. Second, the Commission’s civil penalty authority was extended over the Natural Gas Act (“NGA”). Third, the maximum civil penalty that the Commission could assess was increased to \$1,000,000 per day, per violation for any violation of the NGA, NGPA, and Part II of the FPA.

The Commission modeled the Penalty Guidelines on the United States Sentencing Guidelines, modified to focus on factors that the Commission is required by EPAAct 2005 to consider as part of its enforcement program. Though the Commission has previously released Policy Statements on Enforcement in 2005 and 2008, the Penalty Guidelines are the first civil penalty guidelines adopted by the Commission.

How Penalties are Calculated Using the Penalty Guidelines

Under the Penalty Guidelines, the Commission will base penalty calculations on uniform factors that are given similar, weighted consideration for similar types of violators and similar types of violations. Credit in the form of a penalty reduction will be given to companies that self-report violations and implement extensive compliance programs. The Commission will retain the flexibility and discretion to take specific facts and circumstances of violations into account and, if warranted, impose a penalty outside of the Penalty Guidelines.

To calculate civil penalties using the Penalty Guidelines, the Commission follows a five step process:

1. Step One: Base Violation Level. The Commission determines baseline violation levels and commensurate dollar amounts. There are different baseline violation levels for different types of violations: (i) violations of the Reliability Standards for the Bulk Electric System of North America carry a “base violation level” of sixteen; (ii) violations involving fraud, manipulation, or anti-competitive conduct and violations of rules, tariff, and orders carry a “base violation level” of six; and (iii) violations involving misrepresentations and false statements to the Commission carry a “base violation level” of eighteen.
2. Step Two: Adjustments. The Commission makes adjustments to the base violation level based on various violation characteristics. The Commission considers different factors for each type of violation: (i) for Reli-

ability Standards Violations, the Commission makes adjustments based on the risk of loss caused by the particular violation, with a maximum upward adjustment of sixteen levels for an activity that caused a high risk of extreme harm; (ii) for violations involving fraud, manipulation, or anti-competitive conduct and violations of rules, tariffs, and orders, adjustments are made for monetary gain or loss caused by the violation and the scope of the violation, with a maximum addition of forty-two levels if more than \$400 million in loss results, if 700,000 MMBtus of natural gas or more than 100,000 MWh of electricity is involved, and the violation continued for more than 250 days; (iii) for misrepresentations and false statements of fact, the Commission will make upward adjustments for violations resulting in substantial interference with the administration of justice and violations involving spoliation of records or that are extensive in scope, planning, or preparation, with a maximum upward adjustment of 5 levels. The adjusted level generates a final violation level, corresponding to a specific dollar amount in the Violation Level Penalty Table within the Penalty Guidelines, which ranges from \$5,000 to \$72.5 million.

3. Step Three: Base Penalty. The Commission determines a base penalty amount by calculating the greater of (1) the final violation level, (2) the pecuniary gain to the organization from the violation, or (3) the pecuniary loss caused by the violation.
4. Step Four: Culpability Score. The Commission then determines a culpability score, starting with a base of five and adjusting upward or downward based on six considerations: (i) if high-level management was involved in the offense, the culpability score will be increased between one and five points, depending on the size of the organization; (ii) if the organization has a history of committing violations, the culpability score will be increased up to two points depending on how recently the previous violation occurred; (iii) if the organization violated a judicial or Commission order while committing the offense, the culpability score is increased by two points; (iv) if

the organization obstructed justice or encouraged obstruction of justice, during the investigation, and/or knew of such obstruction of justice and failed to take reasonable steps to prevent it, the culpability score is increased by three points; (v) if the organization had an effective compliance and ethics program when the offense was committed, with active engagement and leadership by senior management, effective preventative measures, prompt detection and cessation of violations and voluntary reporting of violations, and remediation of the misconduct, the culpability score will be reduced by up to three points; and (vi) lastly, if the organization self-reported the violation and cooperated with the Commission, the culpability score will be reduced by up to five points. The final culpability score corresponds to set of minimum and maximum multipliers. A culpability score of zero or less corresponds to multipliers of 0.05 and 0.20. A culpability score of ten or higher corresponds to multipliers of 2.00 and 4.00.

5. Step Five: Multiplication of Base Penalty by Minimum and Maximum Multipliers. The culpability score minimum and maximum multipliers are multiplied by the base penalty to determine the penalty range. The Commission will consider specific facts of each case for determining where in the range the ultimate penalty will fall.

FERC has released a flow chart which summarizes the steps involved in calculating new civil penalties, available at <http://www.ferc.gov/news/news-releases/2010/2010-1/flowchart-M-1.pdf>.

Applicability of the Penalty Guidelines

The civil penalties discussed in the Penalty Guidelines do not include disgorgement of profits, which the Commission can order separately. The Penalty Guidelines will apply to all pending investigations and future violations where the Commission has not commenced settlement negotiations. Commission Chairman Jon Wellinghoff has directed staff in the Commission's Office of Enforcement to conduct workshops to explain the Penalty Guidelines in detail and answer questions from interested parties. The

first workshop is scheduled for April 7, 2010 in Washington, D.C. The Commission will also hold similar workshops in Houston, Texas on April 14, 2010, and in San Francisco, California on April 15, 2010.

The Penalty Guidelines are available to review at <http://www.ferc.gov/whats-new/comm-meet/2010/031810/M-1.pdf>.

Note: After conducting three public workshops on the Penalty Guidelines, on April 15, 2010, the Commission decided to expand the public comment period before issuing a final order and enacting the Penalty Guidelines. The Commission will now accept comments on the Penalty Guidelines until June 14, 2010.

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