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FERC OPENS INQUIRY TO BROADEN PARTICIPATION IN WHOLESALE ELECTRICITY MARKETS AND IMPOSES CIVIL PENALTY ON AN INDIVIDUAL MARKETER FOR FALSE AND MISLEADING STATEMENTS

At its recent public meeting, FERC approved two orders that affect participants in wholesale electricity markets and their investors.

In one action, FERC began an inquiry into two aspects of its policies toward providers of ancillary services. Ancillary services, traditionally provided by generators, are needed to keep supply and demand on the grid in balance at all times. A FERC restriction on selling ancillary services at market-based rates (instead of cost-justified rates) may be impeding the development of competitive markets for ancillary services. The Commission seeks comments for reforming its policy. FERC also seeks comments on its accounting and reporting requirements for new electricity storage devices such as flywheels and large batteries, which also can be used to provide ancillary services. While the inquiry does not propose new or revised rules or policies, the comments received may lead to such changes.

In the other action, FERC imposed a \$50,000 civil penalty on an individual marketer for violating FERC's market behavior rule against providing false or misleading information in communications with the Commission or an RTO and ruled that intent need not be shown for such a violation. FERC rarely assesses civil penalties outside the context of a settlement with Enforcement Staff or an opinion after an evidentiary hearing.

THE INQUIRY

Ancillary Service Sales Restrictions

FERC generally allows electricity to be sold at market-based rates if the seller can demonstrate that it does not have market power. For sales of ancillary services, it can be difficult for generators to show a lack of market power. Ancillary services require certain equipment characteristics not shared by all generators, and only generators that have these characteristics can be counted as competing suppliers in a market power study. However, detailed information on the pertinent generator characteristics is not always publicly available for use in a study. To address this data limitation, FERC in 1999 began allowing generators to sell ancillary services at market-based prices without a study. However, without a study, FERC prohibited sales at market-based prices to a transmission provider that is purchasing the service to satisfy its transmission tariff obligation to provide ancillary services to its customers at cost-based rates. A study is required for those sales at market-based rates.

Market participants are now looking for more flexibility because the most significant likely market for ancillary services is transmission providers seeking to meet their transmission tariff obligations. There is concern that the current restriction is serving as a barrier to developing competitive ancillary

services markets and to the development of new electricity storage technologies that can provide ancillary services.

Accordingly, FERC issued a Notice of Inquiry (NOI) seeking comments on ways of modifying the current restriction, including reforms to market power study requirements and ideas for other ways to permit rate flexibility. Some of the broad ideas FERC would like to explore are improving the availability of information needed for market power studies, adopting *de minimis* capacity or volume-of-service thresholds below which sellers would not need to perform a market power study, restrictions on the pass-through of ancillary service purchases at prices higher than the transmission provider's tariff rate, and an explicit price cap on sales to transmission providers to satisfy their tariff obligations.

The data problem discussed above generally arises only in the regions of the nation without organized markets such as RTOs and ISOs. The organized markets have developed formal ancillary service markets and performed the needed market power studies.

Accounting and Reporting Requirements for Electricity Storage Devices

The NOI also requests comments regarding accounting and reporting requirements as they pertain to regulatory oversight of electric storage devices. For conventional generation and transmission resources, there are well-established methods of accounting, reporting, and cost-based rate recovery, but this is not necessarily true for the new energy storage resources. Storage resources are capable of providing multiple services to the grid and can operate in ways that resemble production or transmission. For example, storage resources can act as a power marketer by arbitraging peak and off-peak prices and providing ancillary services or they can act like a transmission asset by providing voltage support on the grid. Among other concerns, FERC notes that without clear plant and expense classifications for storage resources, their owners may have difficulty meeting reporting requirements and regulators may have difficulty establishing appropriate rates.

FERC seeks comments on whether, and if so how, to amend the accounting and reporting requirements regarding storage costs and operations.

Comments in response to the NOI are due 60 days after publication in the *Federal Register*. The NOI is available [here](#).

THE ENFORCEMENT ORDER

FERC found that Moussa Kourouma, the owner of a marketing firm seeking to sell electricity at wholesale, violated section 35.41(b) of the Commission's regulations, which prohibits the submission of false or misleading information or the omission of material information in any communication with the Commission, an RTO or ISO, or a FERC-jurisdictional transmission provider. According to the order, issued after giving Mr. Kourouma the opportunity to respond to allegations set forth in a show cause proceeding, Mr. Kourouma made false and misleading statements in filings with FERC regarding an application for market-based rate authority for his company, Qantum, and in related membership filings with the PJM RTO. Mr. Kourouma did so to conceal his ownership of Qantum in order to circumvent a non-compete clause with a former employer. The matter was brought to FERC's attention by Mr. Kourouma's former employer in its protest of the market based rate application.

Mr. Kourouma's filings with FERC stated that his one-year old daughter and an acquaintance of his wife, who was completely unfamiliar with Qantum's business, held various management positions,

and listed the acquaintance's home address as the address of Quntum. The order finds these statements were false. In addition, the order finds the failure of Mr. Kourouma to identify himself as Quntum's owner amounted to a material omission because a seller seeking market-based rate authority must provide fundamental information regarding its corporate structure or upstream ownership. According to the order, Mr. Kourouma made almost identical statements to PJM and PJM staff.

Consistent with its Revised Policy Statement on Enforcement, FERC used five factors to determine a \$50,000 civil penalty: the seriousness of the offense, commitment to compliance, self-reporting, cooperation, and reliance on staff guidance. The only factor FERC found to provide any credit to Mr. Kourouma was his cooperation with enforcement staff during the investigation.

Although Mr. Kourouma did not dispute the material facts in this case, he made two legal arguments that FERC rejected.

- First, FERC found that intent is not a necessary element for finding a violation of section 35.14(b). This section reads as follows:

“A Seller must provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with the Commission, Commission-approved market monitors, Commission-approved regional transmission organizations, Commission-approved independent system operators, or jurisdictional transmission providers, unless Seller exercises due diligence to prevent such occurrences.”

The regulation itself does not make reference to the seller's intent. Moreover, FERC stated that its orders regarding section 35.14(b), which had its genesis in FERC's 2003 Market Behavior rules, are clear that intent is not a required element of a violation. Finally, FERC found that Quntum was a “seller” within the meaning of section 35.14(b) from the day it submitted its application for market based rate authority until the day the Commission rejected the application.

- Second, FERC found that section 35.14(b) is not unconstitutionally vague as applied to the facts of this case. According to FERC, the regulation provides adequate notice of what is prohibited because a “reasonably prudent person would understand that the respondent's conduct was prohibited by the section.” FERC also noted that the respondent admits that his statements were meant to conceal his involvement with Quntum, and that FERC staff gave the respondent an opportunity to correct his filing by directing him to “identify all owners of Quntum.”

FERC's order is available [here](#).

If you have any questions concerning the material discussed in this client alert, please contact the following members of our energy practice group:

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