E-ALERT | Energy

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NEW FERC ISSUANCES ON ENERGY MARKET SURVEILLANCE, DEMAND RESPONSE, AND INTERCONNECTION POLICY AND SIGNIFICANT CFTC SETTLEMENT ON OIL PRICE MANIPULATION

Last week, the Federal Energy Regulatory Commission (FERC) issued a rule requiring RTOs and ISOs to electronically deliver key market data to the agency that it can use to police energy markets, and the Commodity Futures Trading Commission (CFTC) obtained what appears to be its largest settlement in a case involving price manipulation in oil markets.

FERC also issued a Notice of Proposed Rulemaking (NOPR) to incorporate into its regulations business practice standards adopted by the North American Energy Standards Board (NAESB) regarding the measurement and verification of demand response and energy efficiency resources participating in organized electricity markets, and issued a Notice of Inquiry (NOI) on whether it should reconsider its policy regarding priority rights and on alternative approaches to govern third-party requests for service and priority rights on interconnection lines.

FERC RULE ON ELECTRONIC DELIVERY OF KEY MARKETS SURVEILLANCE DATA FROM RTOS AND ISOS

Just a few months after forming a new analytics and surveillance division in its Office of Enforcement, FERC has substantially increased the data it collects from the organized electricity markets (*i.e.*, markets administered by RTOs and ISOs that typically include day-ahead and hourly auction-based energy markets). Until now, data collection by FERC has been limited to quarterly publicly available reports of transactions from market participants and information obtained by FERC via *ad hoc* data requests to the RTOs or ISOs. In Order No. 760, however, FERC adopted new regulations that require each RTO and ISO to electronically deliver to the Commission "on an ongoing basis" non-public data related to the markets that it administers. All of the data is already collected by the RTOs and ISOs.

FERC stated that the new reporting requirements "will enhance Commission efforts to detect anti-competitive or manipulative behavior, or ineffective market rules" and "permit the Commission to improve its screening of participants' market activity for inappropriate conduct, making such conduct more difficult to mask."

The data to be reported include:

- Supply offers and demand bids for energy and ancillary services, and virtual offers and bids;
- Energy/ancillary service awards, including quantity and price;
- Capacity market offers, designations, and prices;
- Resource output data used in market settlements, including RTO and ISO dispatch instructions and measured output levels;

- Marginal cost estimates typically made for the potential replacement of supply offers in market power mitigation procedures;
- Shift factors related to active or binding constraints used to determine the flow contribution to a transmission facility imposed by a change in generator output or load;
- Financial transmission rights data, including how all such rights were acquired (allocation or auction) and details on secondary market transactions;
- Settlement data for internal bilateral energy contracts and for interchange transactions between two or more Balancing Authority Areas; and
- Data on uplift charges and credits.

The required data must be electronically delivered to FERC on an ongoing basis within seven days after each RTO or ISO creates the datasets in a market run or other procedure. FERC indicated it will take steps to ensure that confidential information remains non-public, and expects that FOIA exemption 4 (which protects "trade secrets and commercial or financial information obtained from a person [that is] privileged or confidential") will apply to data so collected.

The new data reporting requirements become effective 60 days after publication in the Federal Register. Order No. 760 is available here.

CFTC SETTLEMENT ON PRICE MANIPULATION IN OIL MARKETS

The CFTC recently obtained what appears to be its largest settlement in a case involving price manipulation in oil markets in *CFTC v. Optiver Holding BV et al.*, No. 08-cv-6560 (S.D.N.Y. 2008).

On April 19, 2012, a federal judge approved a consent order under which Optiver Holding BV, a Dutch-based global proprietary trading company; two of its subsidiaries, including Optiver US, LLC, a Chicago-based corporation; and three individual officers must pay a $13 million civil monetary penalty and Optiver US must disgorge $1 million. Also pursuant to the consent order, for two years Optiver US may not trade futures or options on futures in certain energy commodities within three minutes of the market's closing, and for upwards of eight years the offending officers may not trade in commodities on behalf of themselves or others.

The consent order ends a nearly four-year enforcement proceeding brought against the defendants in a New York federal court. On June 24, 2008, the CFTC filed a complaint alleging the defendants manipulated and attempted to manipulate NYMEX Light Sweet Crude Oil, New York Harbor Heating Oil, and New York Harbor Gasoline futures. In at least 19 instances on 11 days in March 2007, according to the CFTC, the defendants attempted to manipulate prices, and in at least five such instances succeeded in causing artificially high prices. Under the alleged scheme, defendants acquired substantial positions in Trading at Settlement contracts, which are priced with reference to NYMEX's daily closing price, and offset those positions by trading futures contracts shortly before and during the market's closing period in a manipulative manner. This practice is commonly referred to as "banging the close."[1] The defendants allegedly gained approximately $1M from their manipulative conduct.

[1] In 2008, when the CFTC filed its complaint, the Commodity Exchange Act's (CEA) prohibition of market manipulation required showing, among other things, intent to manipulate a price. This CEA prohibition extended to banging the close so long as all the requirements of market manipulation were satisfied. In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act amended the CEA to specifically ban banging the close, even on a showing of mere recklessness.

The complaint also alleged that Optiver US and one of its officers concealed the manipulation by making false statements in response to an inquiry from NYMEX.

The consent order is available here.

DEMAND RESPONSE AND ENERGY EFFICIENCY RESOURCE MEASUREMENT AND VERIFICATION STANDARDS

Demand response and energy efficiency resources are increasingly important in organized electricity markets. Because system operations and compensation depend on the performance of these resources, measurement and verification standards for them are important. FERC recently issued a NOPR to incorporate by reference into its regulations business practice standards adopted by NAESB pertaining to the measurement and verification of demand response and energy efficiency resources participating in organized electricity markets.

The proposed demand response standards add additional specificity to existing measurement and verification standards regarding meter data reporting deadlines, advanced notifications that capacity products will be required, telemetry intervals for submitting data to the system operator, meter accuracy, meter data reporting intervals, and windows for calculating baseline adjustments.

The NOPR also proposes an initial set of standards for energy efficiency products in organized wholesale electricity markets. Their purpose is to create a standard method for quantifying the energy reductions from energy efficiency measures such as lighting, appliances, industrial process improvements, and building management. The standards would provide the basis for compensating energy efficiency resources in accordance with how well they perform, and help to ensure that energy efficiency resources and other electricity resources are treated comparably.

Comments are due June 25, 2012. The NOPR is available here.

GENERATOR DEVELOPER RIGHTS TO INTERCONNECTION LINES

Renewable generating resources, such as wind and solar facilities, are typically located in remote locations and are sometimes developed in stages. Their remote location requires very long, high-voltage transmission lines--sometimes hundreds of miles in length at voltages as high as 345 kV—to interconnect to the grid. These interconnection lines are often financed, and owned, by generation developers. Under FERC's open access transmission rules, if other generators file a request to use any interconnection line capacity not in use, the developer must file an open access transmission tariff (OATT) and provide service, including expanding the line if needed. A developer can retain priority rights to its line for future generation projects or expansions if it can demonstrate specific, pre-existing generator expansion plans, with milestones, for construction of generation facilities and that it has made material progress toward meeting those milestones.

Generator developers claim that this policy is unduly burdensome and ill-suited for generator lead lines, and may have detrimental implications for the future development and financing of generator lead lines and generation projects, especially renewable energy projects. They further assert that:

- Priority rights on an interconnection line are uncertain but are essential for the financing of generation projects because priority rights provide lenders with assurance that developers will still be able to use the line for their planned generation facilities;
- FERC's policy can create a "free rider" problem that creates a disincentive to be the first developer to build a generator lead line, while creating a relative advantage for other generation

developers to be second in line (a relatively low threshold event—a written request unaccompanied by any deposit—can force the owner to incur the costs of filing an OATT and conducting feasibility studies); and

- Generator interconnection lines are simply not appropriate for OATT responsibilities because they are not part of the integrated transmission network, and thus they do not provide capability or reliability benefits and cannot be relied on for coordinated operation of the system.

In response to these concerns, FERC issued an NOI seeking comments on whether it should reconsider its policy regarding priority rights and on alternative approaches to govern third-party requests for service and priority rights.

The first approach on which FERC seeks comments is the continued use of an OATT framework but with modifications, such as:

- Providing more guidance on how to satisfy the "specific plans and milestones" standard for protecting priority rights to a line's capacity;
- Establishing a safe harbor period during which a developer would be assumed to have priority rights;
- Altering the requirements for triggering an OATT filing by the developer; and
- Modifying or eliminating OATT provisions that are not appropriate for interconnection lines and their developers.

The second approach on which FERC seeks comments is a framework that would allow negotiations for the requesting party to use the interconnection facilities and entitle the interconnection line owner to compensation for both capital expenses it incurred to pay for the interconnection facilities and the ongoing costs, including operation and maintenance costs, based on a *pro rata* use among the parties. This framework is used by FERC for third-party use of a transmission provider's interconnection facilities to which an existing generator developer contributed funding.

Comments are due June 11, 2012. The NOI 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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