



NRRI Colloquium

Orlando, 19 November 2013

Completed and Ongoing Studies

Rishi Garg
General Counsel
NRRI



NRRI Colloquium – Electricity Presentation

Outline

- I. Genesis of research topic
- II. Deciphering a state role in federal enforcement actions
- III. FERC authority to enforce Anti-Manipulation rules
- IV. Summary of recent enforcement actions
- V. Research topics for Phase II report
- VI. Overview of 2013 papers and research going forward



Genesis of Research Topic

Deutsche Bank Fined Over Energy Trading Scheme. Wall Street Journal. January 22, 2013

Barclays, Traders Hit for Manipulating Power Prices. Wall Street Journal. July 17, 2013

U.S. Probes Whether J.P. Morgan Employees Misled Regulators. Wall Street Journal. September 4, 2013

Exelon Settles with U.S. FERC Over Power Market Activity. Thomas Reuters. October 21, 2013



State Role in Federal Actions

Phase I Report:

- FERC authority to pursue anti-manipulation actions after EPACT 2005
- Types of manipulation alleged/actions taken against power marketers

Phase II Report:

Primary Questions

- Opportunities for/barriers to state participation in enforcement actions
- Ratepayers benefits that accrue from state participation
- Worthwhile for state to pursue action given limited resources

Secondary Questions

- Impacts of power market manipulation on ratepayers
- Role of power marketers in functioning of power markets
- Jurisdictional mandates/boundaries of federal and state agencies



Anti-Manipulation History

- Federal Power Commission created in 1920 (Federal Water Power Act)
- FPC becomes independent agency in 1935 (Federal Power Act)
- Renamed FERC in 1977 (Dept. of Energy Reorganization Act)
- Office of Enforcement created in December 1977
- Energy Policy Act of 1992 initiated electric deregulation – enabled commodity prices to be determined by the trading of financial instruments whose value was tied to the underlying commodity
- EPACT 2005 amended
 - Federal Power Act
 - Natural Gas Act
 - Natural Gas Policy Act
 - ✦ Broad authority to prohibit energy market manipulation
 - ✦ Civil penalty authority increased to \$1 million/day for each day violation continues



Anti-Manipulation Authority

FPA §222, 16 U.S.C. §824(v)(a) – it is unlawful for any entity...directly or indirectly... to use or employ, in connection with the purchase or sale of electric energy...any manipulative or deceptive device or contrivance

FERC Rule 1c.2. – unlawful for any entity...to use...any device, scheme or artifice to defraud...to make any untrue statement of material fact...to engage in any act...that operates as a fraud upon any entity

Final Rule on Prohibition of Energy Market Manipulation, FERC Order No. 670, January 2006 – Anti-Manipulation Rules applies where entity

- (1) uses fraudulent device, makes material misrepresentation/omission
- (2) with requisite scienter
- (3) in connection with the purchase...or transmission of electric energy



Types of Manipulation

(A) Deutsche Bank Energy Trading – Docket No. IN12-4-000

- Fraudulent scheme of scheduling physical transactions to benefit its financial Congestion Revenue Right positions in the California ISO
- False designation of imports/exports as “Wheeling-Through” transactions

(B) Constellation Energy Commodities Group – Docket No. IN12-7-000

- Scheme of trading in New York ISO virtual market to move day-ahead prices in one direction that would benefit its financial Contract for Differences positions.
- Widespread economic losses to market participants and distortion of price discovery for all market participants.

(c) JP Morgan Ventures Energy Corporation – Docket No. IN13-5-000

- Series of 12 strategies in the California and MISO markets of submitting bids that falsely appeared economic but were intended to pay JVEC rates far above market prices
- Submitted losing bids in the day-ahead and real time markets to trigger out-of-market “make-whole” payments, intended to ensure fairness to units bid in good faith

(D) Barclays Bank, PLC – Docket No. IN08-8-000

- Scheme to manipulate trading at 4 electricity trading points in the West
- Loss-generating trading of physical electricity to benefit financial swap positions



Common Manipulation Themes

- (1) Physical trades detrimental to organization in order to benefit the organization's financial positions (in other markets)
- (2) Physical trades made without respect to market fundamentals of supply and demand or profitability
- (3) Organization training manuals and other resources prohibit uneconomic behavior that benefits positions in other markets
- (4) Widespread economic loss to market participants or distortion of well-functioning markets



Phase II Report

(A) State participation in federal enforcement actions

Blumenthal v. ISO New England, 129FERC61,057 (“Section 222(b) of the FPA, while barring “private rights of action,” does not operate as a bar to a complainant alleging market manipulation in a complaint filed with the Commission and thereby bringing alleged market manipulation to the Commission’s attention.)

(B) Jurisdiction

Hunter v. FERC, 711 F.3d 155 (2013); FERC and CFTC required to enter an MOU about information sharing; “Absent a clearly expressed congressional intention” to repeal CFTC exclusive jurisdiction, FERC cannot encroach upon it.

(C) Value of Financial Institutions in Electric Power Markets

Cargill, Inc. v. Hardin, 452 F.2d 1154, 8th Cir. 1971) “methods and techniques of manipulation are limited only by the ingenuity of man.” *Amendments to Blanket Sales Certificate*, FERC Order No. 644, “by requiring regulations to be too specific, [courts] would be opening up large loopholes allowing conduct which should be regulated to escape regulation”

(D) Impacts of Manipulation in organized markets/vertically-integrated regions

Utility purchase prices tied to market indices (ICE); Vertically-integrated utilities purchasing power in organized wholesale markets; Artificially-high prices may compel utility to build



Overview of Past and Future Research

February 2013: FERC Order 1000, Public Utility Compliance and Impacts on States, Report 13-03

Recommendation to states: Pay particular attention to requirement to (1) identify and evaluate transmission needs driven by public policy requirements; (2) comply with cost-allocation principle 1 (requiring definition of benefits and beneficiaries); and (3) determine whether ROFR removal will necessitate state action.

April 2013: ROFR, Competitive Solicitation or Incumbent Preference, Report 13-04

Recommendation to states: Consider analysis comparing transmission-selection procedures to determine whether incumbent preference or competitive solicitation confers more benefits to each respective state's ratepayers and factor analysis into decision whether to enact state ROFR.

July 2013: Wind Integration Cost and Regulatory Challenges, Report 13-09

Recommendation to states: consider (1) whether to collectively encourage FERC to adopt further wind integration reforms (contemplated in notice of inquiry) through a formal rulemaking process; (2) undertaking comprehensive analysis that would shed daylight on the wind integration cost models to identify metrics that lend themselves to meaningful comparisons across service territories

November 2013 – February 2014: State Roles in FERC Enforcement Actions (Phase I), Report 13-11
Power Market Manipulation and the Rights of Retail Consumers (Phase II)

July 2014: Distributed Generation and Challenges to the Utility Business Model: What are Options for the Future?