
FEDERAL ENERGY REGULATORY COMMISSION



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NEWS RELEASE

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COMMISSION FINALIZES RULE BARRING MARKET MANIPULATION

The Federal Energy Regulatory Commission today finalized regulations prohibiting energy market manipulation pursuant to its new Energy Policy Act of 2005 authority. The final rule is largely unchanged from the proposed rule the Commission issued in October, while providing clarification of certain matters.

“In my view, this is one of the most important and challenging provisions of the Energy Policy Act. Congress gave us this authority out of recognition that wholesale power and gas markets had changed dramatically since the 1930s. While our legal duty remains the same – protecting wholesale power and gas customers – we needed different regulatory tools to discharge this duty. Today, the Commission uses one of these new tools to issue rules to prevent market manipulation,” Chairman Joseph T. Kelliher said.

“Together with the Commission’s newly enhanced civil penalty authority, this Final Rule opens a new chapter in the Commission’s oversight of the energy marketplace. Along with our recent Policy Statement outlining how we will apply our civil penalty authority, and the industry’s ability to request ‘no action’ letters from staff, we have strived to provide regulatory certainty,” Chairman Kelliher added.

The Commission affirmed that its Final Rule bars energy market manipulation by “any entity,” as Congress directed, providing the entity’s conduct is in connection with a Commission-jurisdictional transaction. This includes governmental utilities and other market participants, and not just jurisdictional market-based rate sellers, natural gas pipelines or holders of blanket certificate authority.

“If any entity engages in manipulation and the conduct is found to be ‘in connection with’ a jurisdictional transaction, the entity is subject to the Commission’s anti-manipulation authority. Absent such nexus to a jurisdictional transaction, however, fraud and manipulation in a non-jurisdictional transaction (such as a first or retail sale) is not subject to the new regulations,” the Commission said in the Final Rule.

“We do not intend to construe the Final Rule so broadly as to convert every common-law fraud that happens to touch a jurisdictional transaction into a violation of the Final Rule. Rather, in committing fraud, including fraud in a non-jurisdictional transaction, the entity must have intended to affect, or have acted recklessly to affect, a jurisdictional transaction,” the Commission clarified.

Noting that the Energy Policy Act did not amend the Commission’s Interstate Commerce Act authority, the Commission further clarified that the anti-manipulation rules do not apply to oil pipeline transportation regulated by the Commission.

The Energy Policy Act bars “any manipulative or deceptive device or contrivance” in wholesale natural gas and electricity commodity and transportation or transmission markets subject to the Commission’s jurisdiction. Under the Final Rule, it is unlawful for any entity, directly or indirectly, in connection with the purchase or sale of electric energy or natural gas or the purchase or sale of transmission or transportation services subject to Commission jurisdiction: (1) to defraud using any device, scheme or artifice; (2) to make any untrue statement of material fact or omit a material fact; or (3) to engage in any act, practice or course of business that operates or would operate as a fraud or deceit.

“The Commission defines fraud generally, that is, to include any action, transaction, or conspiracy for the purpose of impairing, obstructing or defeating the honest functioning of the market. Fraud is a question of fact that is to be determined by all the circumstances of a case,” the Commission stated in today’s Final Rule.

As proposed, and as Congress directed in sections 315 and 1283 of the Energy Policy Act, today’s Final Rule tracks the language of the Securities and Exchange Commission’s Rule 10b-5, which implements section 10(b) of the Securities Exchange Act. The Commission affirmed that it will, on a case-by-case basis, adapt analogous securities precedents as appropriate to specific facts, circumstances, and situations that arise in the energy industry. This will provide “substantial certainty” to the industry because of the large body of securities case law, the Commission said.

The Commission further clarified that the Final Rule does not involve any new affirmative disclosure duty. “Nothing in the Final Rule requires disclosure of sensitive information that would only function to weaken an entity’s bargaining position in arm’s-length, bilateral negotiations,” the Commission said. The Commission also rejected requests to delete from the Final Rule proposed provisions regarding omission of material facts, noting that parties may not misrepresent facts where there is a Commission-imposed requirement to be truthful. The Commission emphasized that “the Final Rule does not create an affirmative duty to disclose beyond any existing requirements.”

Further, the Commission affirmed that there can be no violation of the Final Rule absent a showing of intent to deceive or defraud, legally defined as “scienter,” and declined requests to alter the language in the proposed rule addressing scienter or to provide specific language regarding intent. The Commission noted that the concept of scienter is well-established in securities law and clarified that recklessness satisfies the scienter requirement.

The Commission’s 2003 Market Behavior Rules, which overlap with today’s rulemaking, will remain in effect pending the outcome of a separate proceeding in which the Commission has proposed their revision or repeal (Docket Nos. EL06-16-000 and RM06-5-000).

If the Market Behavior Rules are repealed, “the Commission intends to have a smooth transition from the Market Behavior Rules to the Final Rule on manipulation, and there will be no gap in our prohibition of manipulation as we complete the transition,” the Final Rule stated. The Commission added it will not seek duplicative sanctions for the same behavior under the Market Behavior Rules and today’s Final Rule. Further, the Commission will not seek sanctions for actions taken in compliance with market rules adopted by Independent System Operators or Regional Transmission Organizations.

In addition to providing the Commission with express authority to prohibit market manipulation, the Energy Policy Act enhanced the Commission’s civil penalty authority both by extending it across all of the substantive provisions of Part II of the Federal Power Act, and the Natural Gas Act, and by increasing the maximum civil penalty under these statutes to \$1 million per day per violation. Those violating today’s Final Rule will be subject to those penalties as outlined in the Commission’s October 20, 2005, Policy Statement.

The Final Rule, *Prohibition of Energy Market Manipulation*, takes effect immediately upon publication in the Federal Register (www.gpoaccess.gov).

“The Commission has balanced the necessity for immediate implementation of this Final Rule against the principles of fundamental fairness which require that all affected persons be afforded reasonable time to prepare for the effective date of this ruling,” the Final Rule states. “The Commission is of the view that the persistent high energy prices in the wake of severe damage to the United States’ energy infrastructure from the hurricanes of 2005, together with the potential for severe price events in the event of cold winter weather during the winter months of 2006, may present opportunities for energy price manipulation. It would be contrary to the public interest to delay regulations that implement Congressional intent to prohibit manipulation in energy markets. Immediate adoption of the Final Rule will protect natural gas and electricity markets from manipulative conduct.”

R-06-3

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