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ENERGY

FERC SLAMS DOOR ON INTERLOCKING OFFICER AND DIRECTOR RULES

The Federal Energy Regulatory Commission ("FERC") slammed a door in the face of those pleading for leniency in complying with its officer and director interlock rules. Adopting final rules, effective October 24, 2005, FERC emphasized again that no prohibited interlock can be assumed unless the individual has received *prior* FERC approval. In one helpful change, applications seeking approval will be deemed approved within 60 days after filing unless FERC takes action otherwise. Under the Energy Policy Act of 2005, FERC has increased ability to impose civil fines, with penalties of up to $1 million, for noncompliance with FERC rules. Public utilities will have to exercise extreme care in selecting officers and directors and in appointing officers within holding company systems to avoid the embarrassment, or worse, of violating these rules.

Section 305(b) of the Federal Power Act requires *prior* FERC approval for any person to hold a position as an officer or director of a public utility and officer or director of certain other entities, including:

- any other "public utility" as defined in the act
- a "bank, trust company, banking association or firm that is authorized by law to underwrite or participate in the marketing of securities of a public utility"
- any supplier of "electrical equipment" to the public utility of which the person is also officer or director.

For these rules, "public utility" means any person who owns facilities used to transmit electricity in interstate commerce or who engages in wholesale sales of electricity in interstate commerce. Traditional investor-owned utilities as well as exempt wholesale generators and energy marketing firms are generally included within this definition.

FERC's rules defining who must seek approval and what must be included in an application for authorization are set out at 18 CFR Part 45. Effective October 24, 2005, these rules are modified in several respects.

First, the final rule makes clear that only a request in advance of the time the person "holds" the interlock will be considered timely. Late filed applications will be denied.

"Holding" an interlocking position means "acting as, serving as, voting as or otherwise performing or assuming the duties and responsibilities of" the position for which authorization is sought. Accordingly, a director cannot be seated on the board with a right to vote or otherwise assume a director's duties, for example, until the application is approved. Similarly, a newly designated officer cannot serve in an "acting" position pending his or her final approval. The person cannot begin his or her duties merely because the application has been filed; no service is permitted until the approval is obtained (or deemed obtained 60 days following the filing, if FERC has not otherwise acted).

Given these requirements, public utilities will have to add additional time to the process of selecting and seating new officers and directors. It may be necessary to elect or appoint officers and directors to their positions expressly conditioned so that they do not begin service until FERC approval is in hand. Public utilities and their general counsel should consider the following:

- Current officers and directors of public utilities will have to be reminded that there are certain other officer and director positions that they cannot accept until they have received advance approval from FERC.
- When a utility is considering adding a new director to its board or filling officer positions, it will be imperative to find out the person's other affiliations well in advance. If the new person is affiliated with another public utility, with a firm authorized to underwrite utility securities, or with an entity that supplies electrical equipment to the utility, FERC approval will have to be sought and obtained before the person can assume the new positions.
- There will be considerable embarrassment if the person involved begins to "hold" the interlocking position without approval and then has to resign. The person may be subject to FERC imposed penalties.

The second change in the rules emphasizes the advance filing requirement necessary to obtain the "automatic" approval allowed in the rules for interlocks between utilities that are part of the same corporate family. Section 45.9 of the rules (18 CFR § 45.9) allows a person serving as officer or director of one public utility to also serve as officer or director of another affiliated public utility (for example, serving as officer of each of the several utility subsidiaries in a holding company system). The required approval for these interlocks is deemed granted automatically upon the filing of a simple informational report with FERC. Under the revised rule, the informational report must be filed *before* the person begins to "hold" the specified interlocking positions. Appointments to this type of internal position will not require a delayed effectiveness as long as the informational report is filed immediately upon the person's selection for the new role.

The third change relates to waivers that FERC typically has granted to public utilities authorized to make wholesale sales of electricity at market-based rates. FERC has often included in its orders authorizing use of market-based rates a partial waiver of the requirement to seek approval for interlocking positions involving that utility. Similar to the automatic approvals for affiliated utilities, these orders authorize a simple notice filing, after the interlock arises, merely stating the facts of the interlock. After October 24, 2005, FERC will not include such a waiver in market-based rate orders. Such interlocks will now require a full advance filing seeking authorization under Part 45 of the commission's rules. The automatic approval under Section 45.9 will apply, however, if its conditions are met.

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