

R E P R I N T

*from*

# The Energy ANTITRUST News

Winter 2008

A Publication of the  
Fuel and Energy Industry Committee  
of the Section of Antitrust Law,  
American Bar Association

## FTC Advances Market Manipulation Rulemaking: New regulations expected in early 2009

*By Jeremy Morrison and Bruce McDonald*

In December 2007, President Bush signed into law the Energy Independence and Security Act (EISA)<sup>1</sup> which granted to the Federal Trade Commission authority to enact regulations to prohibit “market manipulation.” In response to this grant of authority, in 2008 the FTC began a rulemaking process to prohibit, “in connection with the purchase or sale of crude oil gasoline or petroleum distillates at wholesale, any manipulative or deceptive device or contrivance.” While the FTC has yet to issue a final rule, the FTC has announced a proposed rule that seems likely to be close to the end product.

In May 2008, the FTC issued an Advance Notice of Proposed Rulemaking (ANPR).<sup>2</sup> In response to the ANPR, 155 comments were filed and reviewed by the FTC.<sup>3</sup> The ANPR specifically sought comment on “the interplay between any proposed FTC rule and other existing federal rules prohibiting market manipulation, the scope of certain definitions, the level of scienter necessary to establish a violation of any proposed rule, the efficacy of the civil penalty authority provided to the [FTC] in EISA, the inclusion or exclusion of certain conduct from the scope of any proposed rule, and the potential costs and benefits of any proposed rule.”<sup>4</sup>

On August 13, 2008, the FTC issued its Notice of Proposed Rulemaking (NPRM). The FTC modeled its proposed rule on securities fraud regulations, finding that the “existing anti-fraud market manipulation regulatory scheme” under SEC Rule 10b-5 is the appropriate model for a market manipulation rule, as it “leverages the significant body of legal precedent interpreting” the anti-manipulation scheme under securities law.<sup>5</sup> The FTC also determined that EISA contemplated conferring the Commission with new authority separate from its current antitrust authority under Section 5 of the FTC Act.<sup>6</sup>

During a November 2008 FTC public workshop on the Commission’s proposed rule, representatives from the petroleum industry expressed concern about the FTC’s decision to extract SEC Rule 10b-5 from the web of financial regulations in the securities industry and apply the rule to the wholesale petroleum markets without alteration. These groups expressed their belief that any FTC rule, or at a minimum the FTC’s application of its rule, should recognize the differences between the financial sector and the fiduciary duties arising in the financial context and the wholesale petroleum markets. Section 10b-5 interacts with numerous securities laws and precedents; the lack of this developed regulatory scheme in the wholesale petroleum markets could be problematic from an enforcement and compliance standpoint, according to some at the workshop. Some commentators from commodity and securities groups expressed a view that the FTC should follow the approach to “market manipulation” under the Commodities and Exchange Act (CEA) and abandon its reliance on SEC Rule 10b-5. This seems very unlikely, as Congress clearly modeled EISA after SEC Rule 10b-5 rather than a CEA standard, and such a departure from the FTC’s proposed rule likely would require an extended rulemaking process.

The FTC’s proposed rule focuses on fraudulent conduct in the wholesale petroleum markets. The rule would make it unlawful (1) “to use or employ any device, scheme or artifice to defraud,”<sup>7</sup> (2) “to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made...not misleading,”<sup>8</sup> or (3) “to engage in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any person.”<sup>9</sup> The Commission noted that, by targeting manipulative or deceptive conduct, it can achieve Section

811's goals while complementing its primary antitrust and consumer protection mandate.<sup>10</sup>

Under the NPRM, the Commission would apply its rule to regulate the wholesale petroleum markets at the "terminal rack level or upstream of the terminal rack level."<sup>11</sup> During the FTC workshop, industry representatives described the near impossibility of manipulating prices at the terminal rack level and the difficulty the FTC would have in applying any rule to those transactions. They encouraged the FTC staff to limit the rule to upstream transaction levels and forego enforcement at the terminal or rack levels.

The FTC tentatively has determined that the rule's scienter requirement should follow securities law precedent and therefore could be satisfied by a showing of recklessness. While many commenting on the proposed rule have argued that the Commission should require a showing of specific intent for there to be a violation, the FTC has said it believes that a showing of recklessness is more appropriate.<sup>12</sup> Under the proposed standard, the FTC would be required to show that the "violator both acted with extreme departure from standards of ordinary care and either knew or must have known that its conduct created a danger of misleading buyers and sellers."

The FTC's final rule is expected to be released early in 2009. ■

*Jeremy Morrison (jmorrison@jonesday.com) is an associate in the Antitrust practice of Jones Day in its Washington office. Bruce McDonald (bmcdonald@jonesday.com) is a partner in the Antitrust practice of Jones Day in its Washington and Houston offices.*

- 1 Pub. L. 110-140, 121 Stat. 1723 (December 19, 2007), Title VII, Subtitle B, codified at 42 U.S.C. 17301-17305.
- 2 73 Fed. Reg. 25614 (May 7, 2008).
- 3 The ABA Antitrust Section filed comments on the ANPR, available at <http://www.abanet.org/antitrust/at-comments/2008/07-08/comments-FTCANPR.pdf>.
- 4 73 Fed. Reg. 48,317, 48,318 (Aug 19, 2008)
- 5 73 Fed. Reg. at 48,322.
- 6 Id.
- 7 Id. at 48,326 (Section 317.3(a) of Proposed Rule).
- 8 Id. (Section 317.3(b) of Proposed Rule) (emphasis added).
- 9 Id. (Section 317.3(c) of Proposed Rule).
- 10 See id. at 48,323.
- 11 Id. at 48,326 (Section 317.2(e) of Proposed Rule, expressly providing that retail gasoline sales are not included or covered by the rule).
- 12 Specifically, the FTC has proposed using the recklessness standard espoused in *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977).

The original article is available on the American Bar Association website at <http://www.abanet.org/abanet/common/login/securedarea.cfm?areaType=premium&role=at&url=/antitrust/mo/premium-at/at-tei/fe-winter2008.pdf>

This information or any portion thereof may not be copied or disseminated in any form or by any means or downloaded or stored in an electronic database or retrieval system without the express written consent of the American Bar Association.

Copyright 2009 American Bar Association. The contents of this publication may not be reproduced, in whole or in part, without written permission of the ABA. All requests for reprint should be sent to: Director, Copyrights and Contracts, American Bar Association, 321 N. Clark, Chicago, IL 60654-7598, FAX: 312-988-6030, e-mail: [copyright@abanet.org](mailto:copyright@abanet.org).