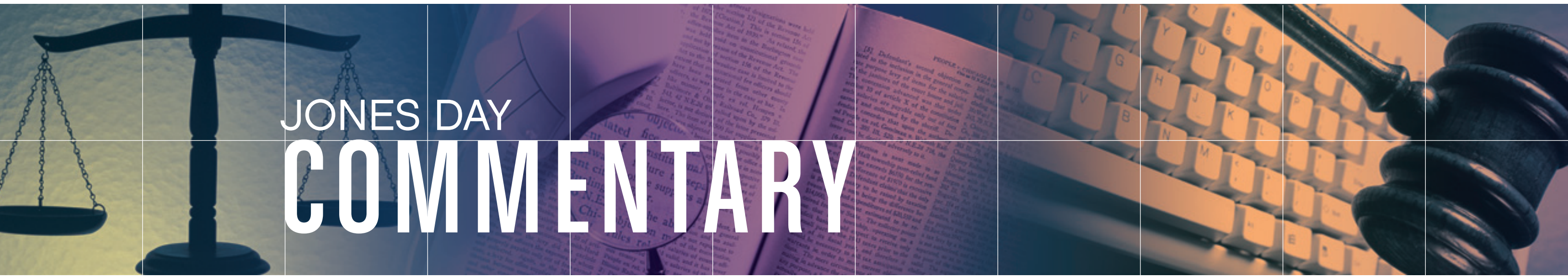
OCTOBER 2010




# FERC'S REVISED PENALTY GUIDELINES: NOT SO DIFFERENT FROM THE ORIGINAL

The Federal Energy Regulatory Commission ("FERC") reissued its Penalty Guidelines on September 17, 2010,[1] after providing industry members the opportunity to comment on the original Penalty Guidelines issued six months earlier, in March 2010. As a result of that comment period, FERC is maintaining the penalty calculation methodology of the original Guidelines but has made some efforts to clarify and adjust the Guidelines to address industry questions and concerns. The most significant of those clarifications and changes are listed below.

When the Guidelines were first issued earlier this year, Jones Day developed an all-inclusive, one-page flowchart to assist companies in applying the Guidelines' penalty calculation methodology to their specific circumstances. We have now revised that flowchart to reflect FERC's changes to the Guidelines. The flowchart reduces the Guidelines' penalty metrics to a single (large, 11"x17") page. To analyze the potential penalty exposure associated with a particular factual situation, begin with the flowchart's Steps 1 & 2 and work through to Step 5.

The reissued Penalty Guidelines are consistent with the penalty calculation methodology that FERC developed in the original March 2010 Guidelines. Of course, when the original Guidelines were issued, they represented a dramatic change in the way FERC planned to calculate penalties for violations of the statutes and regulations it administers. Before the Guidelines, a company had to look to past public settlements and attempt to "read the tea leaves" to determine its possible financial exposure when it uncovered a perceived violation and presented it to FERC Enforcement. Now, with the reissued Guidelines in effect, a FERC-regulated company has a more detailed roadmap that should enable it to conduct an analysis of its particular factual situation and calculate its resulting financial exposure using a prescriptive, formulaic approach.

1 *Enforcement of Statutes, Orders, Rules and Regulations*, 132 FERC ¶ 61,216 (2010) (Revised Policy Statement on Penalty Guidelines).

# NOTABLE CHANGES TO FERC'S PENALTY GUIDELINES

The following is a list of the most significant adjustments and clarifications that FERC has made to the Penalty Guidelines, after taking into account industry comments. Where the change corresponds to a particular step in the penalty calculation methodology (*e.g.*, Step 1, Step 2, etc.), that step is specified.

**Discretion to Close Investigations Without Penalties.** There is now clarification in the Guidelines that FERC reserves the right to depart from the Guidelines where it deems appropriate and that the Guidelines do not affect Enforcement staff's ability to exercise discretion to close investigations and reported incidents without sanctions. Previously, FERC's position on these matters had only been expressed verbally by Office of Enforcement Director Norman C. Bay and Enforcement staff at the Penalty Guidelines workshops held around the country in the weeks following issuance of the original Guidelines.

**Adjustments and Clarifications Related to Reliability Standards Violations.**

- FERC has clarified that it will not apply the Penalty Guidelines to its review of North American Electric Reliability Corporation Notices of Penalty, except in out-of-the-ordinary circumstances. Instead, FERC's use of the Penalty Guidelines with regard to reliability matters will be reserved for its own Part 1b investigations and enforcement actions.

- FERC reduced the base violation level for Reliability Standards violations from 16 to six, but it increased the potential enhancements to a company's base violation level according to the risk of harm posed by the violation. (For example, FERC increased the violation level enhancement for a case involving a low risk of substantial harm from +3 to +5.) (Steps 1 & 2)

- FERC agreed that it would not conduct an individualized assessment of the value of the loss of load as a measure of harm from a Reliability Standards violation. Instead, FERC has developed general enhancements to the base violation level for loss of load on a per-megawatt basis, to be applied consistently across violations. (For example, loss of 10 or more megawatts of load results in a violation level enhancement of +6.) Also, FERC will consider loss of load only in those situations where the load shedding violates the Reliability Standards and where there is a causal connection between a violation of the Reliability Standard and the loss of load. (Steps 1 & 2)

**Misrepresentations and False Statements Have Scienter Requirement.** In assessing penalties for misrepresentations or false statements made to FERC or FERC staff, there is now a scienter requirement. In other words, penalties will not be assessed for inadvertent errors or miscommunications made by companies in their filings or communications with FERC or FERC staff. FERC's application of the Penalty Guidelines will be limited to instances of intentional or reckless misrepresentations and false statements. (Steps 1 & 2)

**Partial Credit for Compliance Programs Is Permitted.** Companies will receive credit for having an effective compliance program that meets some, but not all, of the seven compliance program requirements listed in the Penalty Guidelines. Previously, a company would receive no credit for its compliance program if it did not meet all of the Guidelines' requirements. Now, FERC has departed from this all-or-nothing approach, and a company can reduce its culpability score by up to three points, depending on the level of effectiveness of its compliance program. (Step 4)

**No Automatic Elimination of Compliance Credit Where Senior-Level Personnel Involved in Violation.** FERC has agreed to delete the provision in the original Guidelines that automatically eliminated credit for an effective compliance program when a company's high-level personnel participated in, condoned, or was willfully ignorant of the violation. Instead, FERC will consider whether the senior-level employee acted on his own or at the direction or supervision, or with tacit acquiescence, of the company's governing body. (Step 4)

**Separate Credit Given for Self-Reporting, Cooperation, Avoiding Trial-Type Hearing, and Accepting Responsibility.** FERC will now give credit to companies for the following four factors on an unbundled basis: self-reporting, cooperation, avoidance of trial-type hearings, and acceptance of responsibility. Previously, a company could only reduce its culpability score if its actions met FERC's standards for all of the four factors. Now, because FERC has agreed that each factor carries independent value, companies will be credited separately (*i.e.*, their culpability score will be reduced) for self-reporting, cooperation, avoiding a trial-type hearing, and accepting responsibility. A company can reduce its culpability score by up to five points, depending on its actions with respect to each factor. (Step 4)

Again, these changes do not represent a substantive departure from FERC's previous penalty calculation methodology, but they nevertheless refine the circumstances in which companies will be penalized for their conduct and give companies more opportunity to receive compliance-related credit and reduce their resulting range of penalties. Importantly, FERC's reissuance of the Penalty Guidelines provides companies with a level of transparency in the penalty calculation process that they did not have before.

## LAWYER CONTACTS

For further information, please contact your principal Firm representative or one of the lawyers listed below. General email messages may be sent using our "Contact Us" form, which can be found at www.jonesday.com.


**Kenneth B. Driver**
Washington
+1.202.879.7629
kbdriver@jonesday.com

**Jason F. Leif**
Houston
+1.832.239.3727
jfleif@jonesday.com

**Kevin J. McIntyre**
Washington
+1.202.879.3917
kjmcintyre@jonesday.com

**Jonathan F. Christian**
Washington
+1.202.879.4644
jchristian@jonesday.com

**Emily E. Daniels**
Houston
+1.832.239.3837
edaniels@jonesday.com

**Mosby G. Perrow**
Washington
+1.202.879.3410
mgperrow@jonesday.com