



## **SUMMARY OF FERC REVISED POLICY STATEMENT ON PENALTY GUIDELINES**

On September 17, 2010, FERC issued a revised policy statement on Penalty Guidelines setting forth the manner in which FERC will calculate civil penalties for violations of FERC statutes, rules or orders.<sup>1</sup> Enforcement staff will hold a technical conference one year from the issuance of these modified Penalty Guidelines to discuss how they have worked and to permit comments and questions from the industry.

### **§1A1.1 APPLICABILITY OF GUIDELINES**

FERC re-affirmed its decision to model the Penalty Guidelines after the U.S. Sentencing Guidelines and its right to depart from the Penalty Guidelines where it deemed appropriate. FERC further clarified that zero dollar penalties are still possible under a guidelines-based approach. FERC clarified that the Penalty Guidelines will not affect Enforcement Staff's discretion to close investigations or self reports without sanctions. Finally, The Penalty Guidelines will apply to any pending FERC investigation where Enforcement Staff and the organization have not yet entered into settlement negotiations as of September 17, 2010.

**§1B1.1 DISGORGEMENT** - The Revised Penalty Guidelines did not change the Commission's practice of requiring disgorgement of unjust profits.

### **§1B2.1 EFFECTIVE COMPLIANCE PROGRAM**

The Revised Penalty Guidelines state explicitly that achieving compliance is the central goal of the Commission's enforcement efforts.

**Compliance Program Credits** - FERC revised the Penalty Guidelines to make explicit that the maximum credit for an effective compliance program is 3 points, and that an organization can earn partial credit. FERC stated that it did not intend to broaden the concept to include an ethics program or areas unrelated to FERC's regulations and requirements. FERC explained that an effective program should account in some fashion for the 7 factors listed in the Penalty Guidelines. FERC then listed 4 hallmarks of compliance as follows:

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<sup>1</sup> On March 18, 2010, FERC enhanced its enforcement program with a new Policy Statement on Penalty Guidelines (PL10-4) modeled on portions of the United States Sentencing Guidelines.

- (1) active engagement of senior leadership;
- (2) effective preventive measures;
- (3) prompt detection and cessation of violations and voluntary reporting; and
- (4) remediation of misconduct.

FERC concluded that it would likely give some degree of compliance credit to an organization that achieves these four factors. FERC agreed to delete the provision in the Penalty Guidelines that would automatically eliminate any compliance credit where an organization's senior-level personnel participated in, condoned, or were willfully ignorant of the violation. Instead, FERC decided that it would consider whether the senior-level employee acted on his or her own or at the direction or supervision or with tacit acquiescence of the organization's governing authority. FERC added that it would likely find that compliance credit is not warranted where senior-level personnel involvement in a violation is so pervasive throughout the organization that it reflects the collective actions of the organization as a whole. FERC also stated that it would not find compliance credit warranted where there is evidence that the organization's governing authority knew of the senior-level involvement in a violation or failed to take timely remedial action.

While FERC did not eliminate the requirement that for compliance credit to be given a detected violation must be reported without unreasonable delay, it did provide a list of factors it would consider, including: (1) the time between when the violation was discovered and the time of the report; (2) the steps the organization took before reporting the violation; and (3) the nature of the violation. FERC recognized that an investigation could take considerable time to determine whether a violation occurred, and encouraged organizations that discover violations to contact Enforcement Staff before submitting a full report.

FERC stated that it would continue to consider the size of an organization for purposes of determining whether an organization has met the requirements for an effective compliance program. FERC explained that size should be determined by looking at multiple factors including: (1) the number of employees; (2) the annual revenue, profits and budget; (3) the number of separate operating divisions or units within the organization; (4) the number of senior level employees and (5) the corporate structure of the organization.

**§1C2.1 DETERMINING PENALTY - Violation Level** - FERC clarified that where there are multiple violations falling under different types of guidelines it will determine the appropriate penalty on a case-by-case basis. Where an organization has engaged in multiple acts of fraud, anti-competitive conduct, or other rule, tariff, or order violations under §2B1.1, or made multiple misrepresentations or false statements under §2C1.1, the Penalty Guidelines would treat each act as a separate violation.

**Culpability Score - Prior History** - FERC declined to create a bright-line rule that the prior history enhancement applies only to serious violations. FERC stated that it would consider the prior history of an organization on a case-by-case basis. FERC also rejected the suggestion that it should not treat prior settlement as "adjudications" that would trigger the prior history enhancement. FERC clarified that an order or injunction that would trigger a 2-point increase in the culpability score applies to violations of enforcement-related or other remedial orders directly related to the violation that is the subject of the instant investigation or enforcement action. An

organization's culpability score increases by 1 point if there was an adjudication of any violation less than 10 years earlier or if there was an adjudication of similar misconduct by any other enforcement agency, and 2 points if the time period is less than 5 years.

**Culpability Score - Mitigation Credits** – FERC agreed to unbundle the mitigation credits for self-reports (-2 pts), cooperation (-1 pt), settling (-1 pt) and accepting responsibility (-1 pt). Cooperation must be both timely and thorough.

#### **§2A1.1 GUIDELINES FOR VIOLATIONS OF COMMISSION APPROVED RELIABILITY STANDARDS**

**Reliability Standards** – FERC affirmed that it would apply the Revised Penalty Guidelines to enforce its reliability regulations and requirements because enforcement of the reliability standards falls under FERC's direct enforcement authority. FERC will apply the Revised Penalty Guidelines to violations of the reliability standards only in formal investigations (conducted under 18 CFR Part 1b (2010)) and enforcement actions, but will not apply them to the review of NERC Notices of Penalty. The Commission and NERC have complementary, but separate, authority to enforce the Reliability Standards. FERC also has authority to review NERC's and the Regional Entities' penalty determinations. FERC added that it will continue to consider the same substantive factors in determining whether to review a Notice of Penalty, including the seriousness of the violation as well as the potential risk to the reliability of the bulk power system and any actual harm that resulted. FERC will also consider the need to ensure consistency of penalties and the need to improve compliance with the Reliability Standards.

FERC reduced the base violation level for reliability violations from 16 to 6 and increased the risk of harm enhancements for reliability violations. FERC also agreed that to set the enhancement for violations involving: (1) a low risk of minor harm to zero, (2) either a moderate risk of minor harm or a low risk of substantial harm from +3 to +5, and (3) either a high risk of minor harm or a moderate risk of substantial harm from +5 to +8.

FERC stated that it will use the quantity of load lost, in MWh, as one measure of the seriousness of the reliability violation. FERC stated that it would consider loss of load only in those situations in which there is a causal connection between a violation of a reliability standard and the loss of load.

#### **§2C1.1 GUIDELINES FOR INTENTIONAL OR RECKLESS MISREPRESENTATIONS AND FALSE STATEMENTS TO THE COMMISSION OR STAFF**

FERC added scienter (a requirement of intent) as a requirement for a misrepresentations or false statement. FERC stated that the section would apply to intentional or reckless misrepresentations and false statements. FERC added that it did not intend this section to apply to inadvertent errors or miscommunications in organizations' filings or communications with FERC and staff.

## HOW TO DETERMINE A PENALTY

FERC's Revised Penalty Guidelines generates a penalty range based on the combination of: (1) a violation level, consisting of a base penalty level that is adjusted for various seriousness factors; and (2) a culpability score, which considers an organization's past and current conduct and efforts to remedy the violation. Generating a Final Penalty Range can be broken down into five discrete steps:

1. §1C2.1 Base Violation Level

- (1) violations of the Reliability Standards for the Bulk Electric System of North America carry a "base violation level" of 6;
- (2) violations involving fraud, manipulation, or anti-competitive conduct and violations of rules, tariffs, and orders carry a "base violation level" of 6;
- (3) violations involving misrepresentations and false statements to the Commission carry a "base violation level" of 18.

2. §2A1.1, §2B1.1 & §2C1.1 Adjustments for circumstance specific to each type of violation.

3. §1C2.2 Base Penalty is the greatest of:

- (1) the dollar amount from the table in the Penalty Guidelines §1C2.2(b) that corresponds to the applicable adjusted violation level;
- (2) the pecuniary gain to the organization from the violation; or
- (3) the pecuniary loss from the violation caused by the organization.

4. §1C2.3 Culpability Score which has six separate considerations (participation of high level personnel & size of the organization; history of prior violations; violations of judicial or FERC orders; obstructing justice; effective compliance program, and self reporting/ cooperation/ settlement/acceptance of responsibility). The Commission will not require organizations to waive attorney-client privilege or work-product protections in order to qualify for a reduction under the Culpability Score. No self reporting is required by subsection (f)(2) if the organization reasonably concluded, based on the information then available, that no violation had been committed.

5. §1C2.4 Multiplication of Base Penalty by Min/Max Multipliers

Applying the adjustments to the "base violation level" from step one generates a "final violation level." Each "violation level" then corresponds to a specific dollar amount listed in a table in Penalty Guidelines §1C2.2(b), which plays a role in determining the "base penalty". The base "culpability score" is adjusted based on the six culpability factors to produce a final "culpability score." The final "culpability score" corresponds to a set of "minimum and maximum multipliers" that are listed in a table in §1C2.4 of the Penalty Guidelines. The fifth and final step involves multiplying the "base penalty" amount by the "minimum and maximum multipliers" to produce the Final Penalty Range. However, if the minimum guideline penalty is greater than the maximum penalty authorized by the \$1 million per day, per violation statutory authority, then the guideline penalty will be reduced to the maximum penalty authorized by statute.