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FEDERAL ENERGY REGULATORY COMMISSION

2012 REPORT ON ENFORCEMENT

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Office of Enforcement
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The matters presented in this staff report do not necessarily represent the views of the Federal Energy Regulatory Commission, its Chairman, or individual Commissioners, and are not binding on the Commission.

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INTRODUCTION

The staff of the Office of Enforcement (Enforcement) of the Federal Energy Regulatory Commission (Commission) is issuing this report as directed by the Commission in its Revised Policy Statement on Enforcement.[1] This report informs the public and the regulated community of Enforcement's activities during Fiscal Year 2012 (FY2012),[2] including an overview of and statistics reflecting the activities of the four divisions within Enforcement: Division of Investigations (DOI), Division of Audits (DA), Division of Energy Market Oversight (Market Oversight), and Division of Analytics and Surveillance (DAS).

Enforcement recognizes the importance of informing the public of the activities of Enforcement staff and prepares this report with that objective in mind. Because much of the investigative work of Enforcement is non-public, most of the information the public receives about investigations comes from public Commission orders approving settlements, orders to show cause, publicly released staff reports, and notices of alleged violations. However, not all of Enforcement's activities result in public actions by the Commission. As in previous years, the FY2012 report provides the public with more information regarding the nature of non-public Enforcement activities, such as self-reported violations and investigations that are closed without any public enforcement action. This report also highlights Enforcement's work in auditing jurisdictional companies, compiling and monitoring data from forms and reports submitted to the Commission by market participants, and the surveillance and analysis of conduct in wholesale electric and natural gas markets.

[1] *Enforcement of Statutes, Regulations and Orders*, 123 FERC ¶ 61,156, at P 12 (2008) (Revised Policy Statement). A current Enforcement organizational chart is attached as Appendix A to this report.

[2] The Commission's fiscal year begins October 1 and ends September 30 of the following year. FY2012, the subject of this report, began on October 1, 2011 and ended on September 30, 2012.

OFFICE OF ENFORCEMENT PRIORITIES

The Commission's Strategic Plan announced its mission of assisting consumers in obtaining reliable, efficient, and sustainable energy services at a reasonable cost through appropriate regulatory and market means.[3] The Strategic Plan identifies two primary goals in order to fulfill this mission: (1) ensuring that rates, terms, and conditions of jurisdictional services are just, reasonable, and not unduly discriminatory or preferential; and (2) promoting the development of a safe, reliable, and efficient energy infrastructure that serves the public interest. To further those goals, Enforcement's four divisions gather information about market behavior, market participants, and market rules to assist the Commission in its obligation to oversee regulated markets. The divisions will continue to work to bring entities into compliance with the applicable statutes, Commission rules, regulations, and tariff provisions.

Enforcement has selected priorities for its four divisions. In FY2012, Enforcement continued its focus on matters involving:

- Fraud and market manipulation;
- Serious violations of the Reliability Standards;
- Anticompetitive conduct; and
- Conduct that threatens the transparency of regulated markets.

Enforcement does not intend to change its priorities in FY2013. Conduct involving fraud and market manipulation poses a significant threat to the markets overseen by the Commission. Such intentional misconduct undermines the Commission's goal of providing efficient energy services at a reasonable cost because the losses imposed by such actions are ultimately passed on to consumers. Similarly, anticompetitive conduct and conduct that threatens market transparency undermine confidence in the energy markets and harm consumers and competitors. Such conduct might also involve the violation of rules designed to limit market power or to ensure the efficient operation of regulated markets. Of particular concern to Enforcement are cases involving the greatest harm to the public, where there is often significant gain to the violator or loss to the victims of the misconduct.

The Reliability Standards established by the Electric Reliability Organization and approved by the Commission protect the public interest by requiring a reliable and secure bulk power system. The office enforces these standards and focuses primarily on violations resulting in actual harm through the loss of load or otherwise. Enforcement also focuses on cases involving repeat violations of the Reliability Standards, violations of Standards that carry a high Violation Risk Factor, or violations that present a substantial actual risk to the bulk power system. In addition, the office enforces safety and environmental standards established by the Commission in order to promote the development of a safe, reliable, and efficient energy infrastructure with a particular emphasis on cases involving actual harm or a high risk of harm.

OE continued its commitment to enforcement of these priorities in FY2012. To better accomplish the OE priority of detecting and preventing manipulation, OE created a new division, DAS, in February 2012. In FY2012 DAS reviewed numerous instances of potential misconduct and referred matters to DOI for investigation. The Commission also issued two final rules in FY2012 that greatly enhance DAS's ability to conduct surveillance of the electric markets and to analyze individual market participant behavior, Order Nos. 760 and 768.

[3] The Federal Energy Regulatory Commission, The Strategic Plan (Oct. 2009 (updated Feb. 2012)), *available at* http://www.ferc.gov/about/strat-docs/FY-09-14-strat-plan-print.pdf.

At the same time, staff from DA continued to review the conduct of regulated entities through forty-four financial, compliance, and performance audits of public utilities, natural gas pipelines, and gas storage companies. DA's audits resulted in almost four hundred recommendations for corrective action and directed over $5.8 million in refunds.

Market Oversight continued its analysis of market structure and operations to identify market anomalies, inadequate or flawed market rules, and potentially improper behavior by market participants. In addition to preparing its annual State of the Markets report assessing significant events of the past year, Market Oversight released its Energy Primer, a comprehensive overview of natural gas and electric markets with detail on specific market product segments.

Finally, DOI continued investigating allegations of misconduct. In FY2012, DOI staff opened twenty-one investigations and closed sixteen. Nine investigations resulted in settlements, including the largest civil penalty the Commission has assessed to date. Staff investigations also led to five Commission Orders to Show Cause and seven Notices of Alleged Violations. In total, staff obtained over $148 million in civil penalties and disgorgement of over $119 million in unjust profits in FY2012. In FY2012, DOI, in conjunction with other Commission offices, processed 33 full Notices of Penalty (NOPs) and 12 Spreadsheet NOPs containing a total of 904 possible or confirmed violations.

DIVISION OF INVESTIGATIONS

A. Overview

DOI conducts public and non-public investigations of possible violations of the statutes, regulations, rules, orders, and tariffs administered by the Commission. Investigations may begin from self-reports, tips, calls to the Enforcement Hotline, referrals from organized markets or their monitoring units, other agencies, other offices within the Commission, or as a result of other investigations. During most investigations, DOI staff coordinates with other divisions in Enforcement and subject matter experts in other Commission offices. Where staff finds violations of sufficient seriousness, staff reports its findings to the Commission and attempts to settle the investigation for appropriate sanctions and future compliance before recommending that the Commission initiate a public show cause proceeding.[4]

The Commission continues to increase the transparency of Enforcement activities and promote consistency in Enforcement actions. In FY2012, the Director of the Office of Enforcement directed the Secretary to issue seven notices of alleged violations. The notices involved alleged violations of the Commission's prohibition of market manipulation, tariffs, reliability standards, and Commission Orders. The notices identify the subject of the investigation and the alleged violations with a concise description of the alleged wrongful conduct.[5]

In FY2012, the Office of Enforcement led two multi-office task forces that inquired into power outages in California and Arizona, and in New England. Building on its experience in FY2011, the task forces identified the causes of the outages and made recommendations for prevention of future widespread electricity failures involving Commission-regulated facilities.

In FY2012, DOI continued to focus on the enforcement of the Reliability Standards. Through Enforcement's investigations, with the assistance of technical expertise from the Office of Electric Reliability (OER) and in conjunction with the investigative efforts of the North American Electric Reliability Corporation (NERC), the Commission addressed and resolved findings of violations of Reliability Standards. Moreover, DOI staff continues its coordination with the compliance programs of NERC and the eight Regional Entities (REs). DOI played a central role in addressing 45 NOPs that NERC filed with the Commission during FY2012, in which REs proposed monetary penalties totaling approximately $6.5 million for alleged violations of the Reliability Standards. FY2012 also saw the implementation of NERC's Find, Fix, and Track Report (FFT) enforcement mechanism. In FY2012, the Commission received 12 FFTs reporting 707 possible violations.

Notably, during this fiscal year the Commission approved a $245 million settlement resolving an investigation into significant violations of the Commission's Anti-Manipulation Rule and its rule barring the provision of inaccurate and misleading information to Regional Transmission Organizations and Independent System Operators (RTOs/ISOs). The settlement included a civil penalty of $135 million, the largest penalty assessed by the Commission to date. The entity also disgorged $110 million in unjust profits, a portion of which will be used by ISOs to enhance market surveillance and analysis, and the remainder will be distributed to the affected states through a proceeding before an Administrative Law Judge.

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[4] For a discussion of the processes by which Enforcement staff conducts and concludes investigations, *see* Revised Policy Statement, *supra* note 1.

[5] *See* Appx. C.

The work of DOI this fiscal year included obtaining nine settlements with market participants (including the settlement noted above) that were approved by the Commission. These settlements resolved investigations concerning market manipulation, submission of misleading information, Reliability Standards violations, Open Access Transmission Tariff (OATT) provisions, and natural gas open access policies. The settlements from these matters resulted in the payment of over $148 million in civil penalties and more than $119 million in disgorgement of unjust profits, as well as compliance monitoring reporting requirements in most cases.

Furthermore, during this fiscal year, DOI staff appeared in federal district court in connection with one of its investigations. Staff filed an action in the United States District Court for the District of Columbia seeking to compel production of over two dozen documents that the subject of the investigation contended were protected from disclosure by the attorney-client privilege. In addition to investigation-related work, DOI continued its rigorous analysis of self-reports, Enforcement Hotline calls, referrals, and other matters brought to staff's attention.

DOI staff continues to provide guidance and assistance as requested by other program offices on advisory matters.

B. Significant Matters

1. Inquiry into Arizona-Southern California Outages on September 8, 2011

On September 9, 2011, one day after a bulk power system disturbance in the Pacific Southwest left 2.7 million customers without power, the Commission announced the formation of a joint inquiry with NERC to determine the causes of the outages and make recommendations to prevent such events in the future. Working with NERC, DOI led an inter-office team that released a report on May 1, 2012.[6] Staff used on-site interviews, sophisticated computer modeling, and event simulations to determine causes of the disturbance and to develop recommendations.

Staff determined that the outages stemmed primarily from weaknesses in two broad areas – operations planning and real-time situational awareness – which, if done properly, would have allowed system operators to take mitigating actions prior to the cascading outages. With regard to operations planning, the affected entities' studies did not accurately predict the impact from the loss of a single transmission line because the studies relied on limited and inaccurate external data points, as the Western Electricity Coordinating Council (WECC) region lacks an organized, formal system of data sharing among entities. Leading into September 8th, entities had limited knowledge of the current status of transmission facilities, expected generation output, and load predictions outside their footprint. As a result, entities' planning studies could not adequately predict the impact of external contingencies on their systems or of internal contingencies on their neighbors' systems. With regard to situational awareness, limited external visibility and entities' failure to monitor key equipment prevented them from accurately analyzing external system conditions and contingencies in real-time that could impact their systems. Without external situational awareness, entities could not understand and react to resulting events occurring on their own systems. Other important factors leading to the outages included the failure to study the impact of sub-100 kV facilities on the bulk power system, the failure to recognize Interconnection Reliability Operating Limits (IROLs) in the Western Interconnection, and the failure to study and coordinate the effect of protection systems.

[6] Report on Arizona-Southern California Outages of September 8, 2011, *available at* http://www.ferc.gov/legal/staff-reports/04-27-2012-ferc-nerc-report.pdf.

The report made 27 recommendations to prevent future events, including that system operators improve their operations studies and situational awareness through improved communication, data sharing, and the use of real-time tools.

2. Northeast Snowstorm Inquiry

In November 2011, the Commission initiated an inquiry into the power outages resulting from the major snowstorm that hit New England and the Mid-Atlantic states on October 29-30, 2011, and caused more than 3 million homes and businesses to lose power. Thousands of customers were without power for more than a week, some for as long as eleven days. The inquiry, led by DOI and OER staff, together with NERC, focused on determining the causes of transmission facility outages and on the steps utilities could take to improve their performance in maintaining grid reliability during future snowstorms or similar weather events.

On May 31, 2012, FERC and NERC staff released an inquiry report.[7] The report explained that only a small portion – approximately 5% – of the customer power outages during the storm were caused by problems with transmission (100 kV and above) facilities; the rest were due to distribution system damage. Most of the transmission facility outages were caused when healthy, leafy trees weighted down with heavy, wet snow and rooted in soft, saturated ground fell into transmission lines. The report included a number of recommendations utilities could take to mitigate the impact of future, similar events, including: (1) where appropriate, taking targeted steps to address off-right-of-way danger trees; (2) employing best practices in managing vegetation on full rights-of-way; (3) laying the foundation for effective vegetation management when establishing new rights-of-way; and (4) enhancing storm preparedness and response plans as needed. The report also recommends increasing the reporting of vegetation-caused outages and improving the content of required disturbance reports.

3. ISO-NE Day-Ahead Load Response Program

In July 2012, the Commission issued separate Orders to Show Cause requiring Rumford Paper Company, Lincoln Paper and Tissue LLC, Competitive Energy Services, LLC (CES), and Richard Silkman (the Managing partner of CES) to explain why each should not be found to have violated the Anti-Manipulation Rule, 18 C.F.R. § 1c.2.[8] Staff alleges that the subjects engaged in fraud in ISO New England, Inc.'s (ISO-NE's) Day-Ahead Load Response Program (DALRP) by falsely inflating load baselines and then repeatedly offering load reductions at the minimum offer price in order to maintain the inflated baseline. Staff alleges that through this scheme the subjects misled ISO-NE and were paid, based on their inflated baseline, for load reductions that never occurred.

All four subjects have denied committing any violation. Consistent with the Federal Power Act (FPA), all subjects have elected not to have a hearing before an Administrative Law Judge, but, instead, if the Commission were to find a violation and assess a penalty, to have that penalty assessment order reviewed *de novo* in federal district court.

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[7] Report on Transmission Facility Outages During the Northeast Snowstorm of October 29-30, 2011, *available at* http://www.ferc.gov/legal/staff-reports/05-31-2012-ne-outage-report.pdf.

[8] *Rumford Paper Co.,* 140 FERC ¶ 61,030 (2012) (order to show cause and notice of proposed penalties); *Lincoln Paper and Tissue LLC,* 140 FERC ¶ 61,031 (2012) (order to show cause and notice of proposed penalties); *Competitive Energy Services, LLC,* 140 FERC ¶ 61,032 (2012) (order to show cause and notice of proposed penalties); *Richard Silkman,* 140 FERC ¶ 61,033 (2012) (order to show cause and notice of proposed penalties).

4. Deutsche Bank Energy Trading, LLC

On September 5, 2012, the Commission issued an Order to Show Cause directed toward Deutsche Bank Energy Trading, LLC (Deutsche Bank) in Docket No. IN12-4-000.[9] In that order, the Commission directed Deutsche Bank to show cause: (1) why it should not be found to have violated the Anti-Manipulation Rule and section 222 of the Federal Power Act;[10] and (2) why it should not be found to have violated the accuracy requirement of the Commission's regulations, section 35.41(b),[11] in connection with its physical energy trades and financial positions in the California Independent System Operator (CAISO) markets. Enforcement staff alleged that Deutsche Bank engaged in manipulation and submitted false information in connection with its trading related to the 17 MW Silver Peak intertie in CAISO from January 2010 through March 2010. Specifically, staff alleged that Deutsche Bank falsely scheduled unprofitable physical exports (purchases) at the Silver Peak intertie with the intent to benefit its financial positions in the CAISO system.

Deutsche Bank has denied committing any violation, and has elected the Federal Power Act option of having any penalty assessment order (if the Commission were to find a violation) reviewed *de novo* in federal district court.

5. JP Morgan Ventures Energy Corporation

In response to staff data requests in connection with a pending investigation into potential market manipulation, JP Morgan Ventures Energy Corporation (JP Morgan) contended that more than 50 emails between non-attorneys, some of which carbon-copied an attorney, were protected by the attorney-client privilege. When asked the basis for these claims, JP Morgan told staff that each of the redacted emails was protected by the privilege. Staff advised JP Morgan of its intent to seek *in camera* judicial review of the redacted documents. Subsequently, JP Morgan produced unredacted versions of 28 of the emails. Because JP Morgan continued to assert privilege on 25 other emails, the Commission petitioned in the U.S. District Court for the District of Columbia[12] to enforce a subpoena seeking *in camera* review of these remaining emails. This matter is pending before the court.

6. Constellation Energy Commodities Group

On March 9, 2012, the Commission approved a settlement between Enforcement and Constellation Energy Commodities Group (CCG)[13] resolving two investigations of CCG. The first investigation, concerning CCG's physical power trading in and around the New York Independent System Operator's (NYISO) control area, was opened after Enforcement staff received two anonymous Hotline calls. The second investigation, concerning whether CCG employed a scheme of trading in the NYISO virtual market to move day-ahead prices in a direction that would benefit CCG's financial contract for differences (CFD) positions, was opened based on Enforcement staff's own surveillance activities and information provided by the NYISO Department of Market Monitoring and Performance (MMP) that it had decided to apply mitigation measures against CCG related to certain virtual trading behavior.

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[9] *Deutsche Bank Energy Trading, LLC*, 140 FERC ¶ 61,178 (2012) (order to show cause and notice of proposed penalties).

[10] 18 C.F.R. § 1c.2 (2012); 16 U.S.C. § 824v(a) (2006).

[11] 18 C.F.R. § 35.41(b) (2012).

[12] *FERC v. J.P. Morgan Ventures Energy Corp.*, Docket No. 1:12-me-00352 (D.D.C. filed Jul. 2, 2012).

[13] *Constellation Energy Commodities Group,* 138 FERC ¶ 61,168 (2012) (order approving stipulation and consent agreement).

Enforcement's combined investigations focused on the period September 2007 through December 2008 and examined virtual trading in the NYISO and ISO-NE, physical day-ahead scheduling between the NYISO and ISO-NE, the PJM Interconnection (PJM), and Ontario Independent Electric System Operator, and CFD positions in the NYISO and ISO-NE. Staff determined that CCG violated 18 C.F.R. § 1c.2 by entering into virtual transactions and day-ahead physical schedules without regard for their profitability, but with the intent of impacting day-ahead prices in the NYISO and ISO-NE to benefit certain significant CFD positions that CCG held. In addition, Enforcement staff determined that CCG violated 18 C.F.R. § 35.41(b) by providing inaccurate and misleading information to the NYISO.

CCG neither admitted nor denied committing the violations, but agreed to pay $135 million in civil penalties – the largest civil penalty the Commission has assessed to date – and $110 million in disgorgement. In addition, CCG agreed to prohibit certain individual employees from engaging in or performing duties relating to managing, directing, or engaging in wholesale physical and financial energy trading. The disgorged unjust profits were divided such that six RTOs/ISOs each received $1 million to enhance their surveillance and analytic capabilities and $104 million was provided to impacted states within the NYISO, ISO-NE, and PJM regions to be used for the benefit of electric energy consumers. The proceeds are being distributed in a proceeding led by a Commission Administrative Law Judge (Docket No. IN12-7-000). CCG also is subject to compliance monitoring and agreed that it, and any successor companies, would develop and enforce policies to preserve communications by its traders for a period of no less than five years and to regularly monitor those communications for irregularities or illegalities.

7. Barclays Bank, PLC, Daniel Brin, Scott Connelly, Karen Levine, and Ryan Smith

On April 5, 2012, a Notice of Alleged Violation was issued disclosing staff's investigation into whether Barclays Bank PLC (Barclays), Daniel Brin, Scott Connelly, Karen Levine, and Ryan Smith (collectively, the individual traders) violated the Commission's Anti-Manipulation Rule and section 222 of the FPA. The investigation focused on whether Barclays and the individual traders engaged in loss-generating trading of next-day fixed-price physical electricity on the IntercontinentalExchange to benefit Barclays' financial swap positions at the primary electricity trading points in the Western United States. Staff concluded that Barclays and the individual traders did engage in the prohibited conduct, and sought disgorgement of $34.9 million plus interest in unjust profits and assessment of a $435 million civil penalty against Barclays, and $18 million total civil penalties against the individual traders. Staff reported these findings to the Commission and recommended that it issue an Order to Show Cause.[14]

8. Brian Hunter

In May 2011, former Amaranth Advisors L.L.C. trader Brian Hunter requested rehearing of the Commission's April 2011 Order affirming the presiding Administrative Law Judge's Initial Decision that he had violated 18 C.F.R. § 1c.1 and assessing a $30 million civil penalty.[15] The Commission had ordered Hunter to pay the full penalty recommended by Enforcement staff. In June, Hunter brought a petition for review before the United States Court of Appeals for the District of Columbia Circuit seeking review of portions of the Order. On October 14, 2011, the court dismissed Hunter's petition for review of the April 2011 Order on the grounds that his

[14] The Commission issued an Order to Show Cause in the proceeding after the conclusion of FY2012. *See Barclays Bank PLC, Daniel Brin, Scott Connelly, Karen Levine, Ryan Smith*, 141 FERC ¶ 61,084 (2012) (order to show cause and notice of proposed penalties).

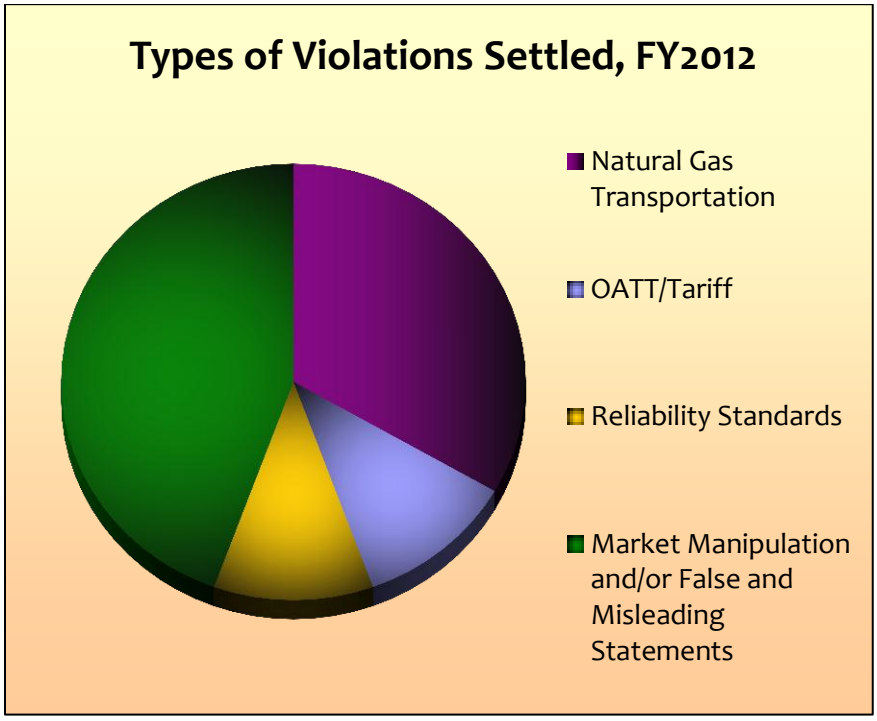
[15] *Brian Hunter,* 130 FERC ¶ 63,004 (2010) (Initial Decision), *reh'g denied,* 137 FERC ¶ 61,146 (2011).

petition was premature because he could not simultaneously seek both agency reconsideration and judicial review of the same agency order. The Commission issued an Order Denying Rehearing in November 2011. Hunter appealed the Commission's November order to the Court of Appeals in December 2011. Briefing for the appeal was completed in June 2012, handled by the Office of the Solicitor. Oral argument will likely be scheduled for early 2013. This is the first fully litigated proceeding under Section 4A of the Natural Gas Act (NGA), and involves one of the largest civil penalties since EPAct 2005.[16]

C. Settlements

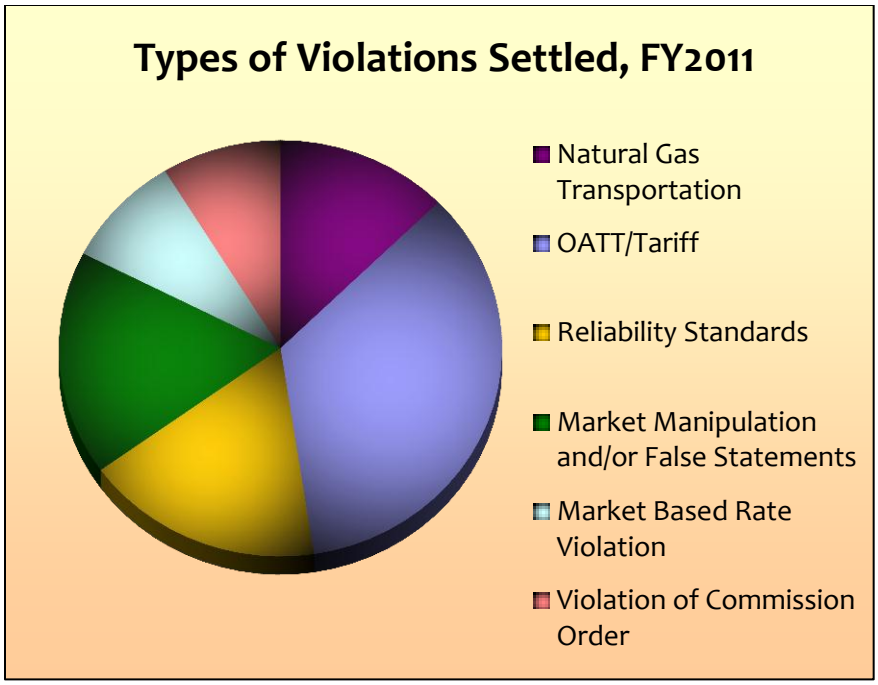
In FY2012, the Commission approved nine settlement agreements entered into by Enforcement for total civil penalty payments of over $148 million and disgorgement of more than $119 million plus interest.[17] These settlements resolved an OATT violation by one entity, a violation of the Reliability Standards by one entity, violations of natural gas open access transportation rules by three entities, a violation of regulations related to Market-Based Rate (MBR) authority by one entity, and violations of the Commission's regulations prohibiting manipulation in natural gas and electric markets by three entities.

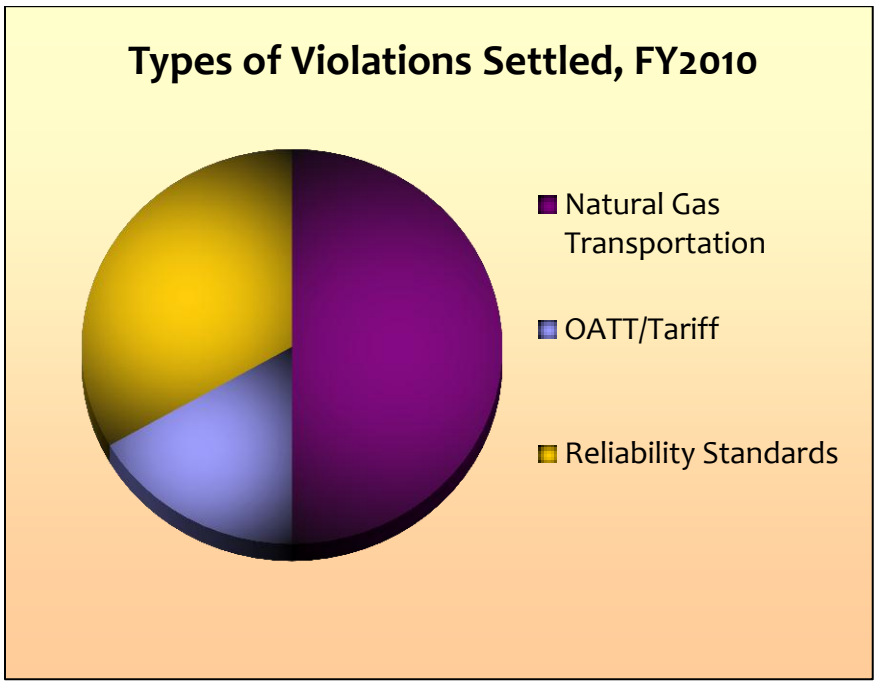
The graphs below compare settlements approved in FY2012, by type of violation, with settlements in prior years.



[16] Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594 (2005).

[17] A table of FY2012 Civil Penalty Enforcement Actions, both those resolved through settlement and those resolved through agency proceedings, is attached to this report as Appendix B.





Eight of the settlement agreements between Enforcement and the investigation subjects are summarized below.[18]

Atmos Energy. On December 9, 2011, the Commission approved a settlement between Enforcement and Atmos Energy, resolving an investigation into whether two of Atmos's

[18] For a description of the Constellation Energy Commodities Group settlement, see section (B)(6) above.

subsidiaries, Atmos Energy Marketing (AEM) and Trans Louisiana Gas Pipeline, Inc. (Trans La), engaged in flipping and shipper-must-have-title (SMHT) violations.[19] Staff's investigation determined that: (1) AEM violated section 284.8(h)(2) of the Commission's regulations when it released capacity through flipping; (2) AEM and Trans La violated section 1c.1 of the Commission's regulations when they acquired 26.1 Bcf of capacity through flipping; (3) some of AEM's and Trans La's flipping transactions involved using defunct companies not affiliated with Atmos, a practice of which high-level personnel at AEM and Trans La were aware; (4) AEM and Trans La high-level personnel knew of and strategized in the use of flipping as a way to continue discounted-rate releases; (5) AEM violated the SMHT requirement and the Commission-approved natural gas tariffs of various interstate pipelines when it shipped 297.8 Bcf of gas titled in its name but using other companies' transportation capacity rights; and (6) AEM high-level personnel had been aware of the SMHT violations since 2004. Atmos, AEM, and Trans La admitted to the violations and agreed to pay a civil penalty of $6,364,029 and to disgorge $5,635,971, plus interest, of unjust profits gained from the SMHT violations. In addition, AEM and Trans La agreed to submit semi-annual compliance monitoring reports.

Missouri Gas Energy. On August 23, 2012, the Commission approved a settlement between Enforcement and Missouri Gas Energy (MGE) resolving an investigation into whether MGE engaged in capacity release violations following MGE's submission of a self-report.[20] Staff's investigation found violations of: (1) section 284.8(h)(2) (rollover transactions); (2) SMHT; (3) prohibited buy/sell arrangements; (4) section 284.8(c) (notice and posting deficiencies); and (5) section 284.8(h)(1) (failure to post biddable transactions). MGE admitted to the violations and agreed to pay a civil penalty of $35,000 and submit a compliance monitoring plan.

Vista Energy Marketing, Inc. On May 24, 2012, the Commission approved a settlement between Enforcement, Vista Energy Marketing (Vista), and an individual member of Vista, Michael P. Whalen, Jr. (Whalen).[21] This settlement resolved staff's investigation into whether Vista violated 18 C.F.R. § 35.41 and a Commission order granting it MBR authority. In its MBR proceeding, Vista made detailed representations and commitments to the Commission that Whalen would play no role in Vista other than that of an investor and would not exert influence or control over Vista. Despite these representations, Whalen was involved in multiple aspects of Vista's management and operations. Vista and Whalen neither admitted nor denied committing the violations, but Vista agreed to pay a civil penalty of $350,000 and Whalen agreed, for a period of two years, to limit his role in, and communications with, other jurisdictional electric entities and their employees and representatives. Whalen also agreed to submit compliance monitoring reports.

Xcel Energy Inc. On January 17, 2012, the Commission approved a settlement between Enforcement and Xcel Energy Inc. (Xcel Energy).[22] This order resolved staff's investigation into whether Xcel Energy committed violations of the Xcel Energy Operating Companies' Open Access Transmission Tariff and the Southwest Power Pool, Inc.'s Open Access Transmission Tariff by the use of firm network integrated transmission service in connection with the purchase and sale of electricity over the Lamar Tie Line. Xcel Energy neither admitted nor denied committing violations of the tariffs or of Commission rules and regulations, but agreed to pay a $2,000,000 civil penalty and to submit compliance monitoring reports.

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[19] *Atmos Energy Corporation*, 137 FERC ¶ 61,190 (2011) (order approving stipulation and consent agreement).

[20] *Missouri Gas Energy*, 140 FERC ¶ 61,135 (2012) (order approving stipulation and consent agreement).

[21] *Vista Energy Marketing, L.P.,* 139 FERC ¶ 61,154 (2012) (order approving stipulation and consent agreement).

[22] *Xcel Energy Inc.,* 138 FERC ¶ 61,026 (2012) (order approving stipulation and consent agreement).

Joseph Polidoro. On January 11, 2012, the Commission approved a settlement between Enforcement and Joseph Polidoro.[23] Polidoro was the Senior Vice President of North America Power Partners (NAPP) from 2006 through the fall of 2008, and was primarily responsible for NAPP's operations and participation as a Curtailment Service Provider in PJM Demand Response programs. Enforcement determined that Polidoro's actions and failure to act on behalf of NAPP in connection with NAPP's participation in PJM's Synchronized Reserve Market and Interruptible Load for Reliability Program violated 18 C.F.R. § 1c.2.[24] Polidoro neither admitted nor denied committing violations, but agreed to pay a civil penalty of $50,000 and agreed to a two-year ban from participation in any PJM Demand Response activities. The size of the penalty took into account Polidoro's limited financial resources; otherwise, the seriousness of the conduct would have resulted in a higher civil penalty.

ConocoPhillips Company. On January 4, 2012, the Commission approved a settlement between Enforcement and ConocoPhillips Company resolving an investigation arising from a self-report of SMHT violations.[25] Enforcement found that: ConocoPhillips used (1) capacity held by a customer to deliver gas to third parties, (2) capacity held by an affiliate to ship its own gas, and (3) capacity acquired from other entities but not yet transferred to ConocoPhillips to ship its own gas. These SMHT violations involved 73.6 Bcf of gas and over $2.5 million in unjust profits. Through further investigation, Enforcement found that ConocoPhillips and its affiliate Brandywine Industrial Gas Inc. obtained releases of discounted rate short-term capacity on an alternating monthly basis, without complying with the Commission's posting and bidding requirements, under prearranged deals with the releasing shippers. The violations occurred on four different pipelines, involved a total of seven releasing shippers, ranged in duration from two months to more than two years, and involved 16.9 Bcf and over $320,000 in unjust profits. Enforcement also found that ConocoPhillips violated the Commission's prohibition on buy-sell transactions with a single, one-month transaction involving 1.3 Bcf of gas. Staff found that ConocoPhillips's conduct circumvented, and therefore frustrated, the Commission's open access transportation policies that promote market transparency. ConocoPhillips neither admitted nor denied that its acts violated a Commission rule, regulation or statute, but agreed to pay a $545,000 civil penalty and to disgorge $3,174,900 plus interest in unjust profits. ConocoPhillips distributed the disgorgement to various state Low Income Heating Assistance Programs and agreed to submit compliance monitoring reports for one year.

PacifiCorp. On December 1, 2011, the Commission approved a settlement between Enforcement, NERC, and PacifiCorp resolving an investigation into a February 14, 2008, bulk electric system disturbance in Utah.[26] Enforcement and NERC determined that PacifiCorp violated 23 requirements of 15 Reliability Standards. Enforcement and NERC determined that PacifiCorp, serving the reliability functions of Balancing Authority and Transmission Operator, failed to respond adequately to the disturbance and thereby violated requirements related to: (1) the restoration of Area Control Error; (2) responding to an emergency; and (3) assuring operator independence, among other requirements. PacifiCorp neither admitted nor denied the violations,

[23] *Joseph Polidoro,* 138 FERC ¶ 61,018 (2012) (order approving stipulation and consent agreement).

[24] On October 28, 2010, the Commission approved a settlement between the Office of Enforcement and NAPP for violations of the PJM Open Access Transmission Tariff and 18 C.F.R. § 1c.2 (2010). *North America Power Partners*, 133 FERC ¶ 61,089 (2010) (order approving stipulation and consent agreement).

[25] *ConocoPhillips Co.,* 138 FERC ¶ 61,004 (2012) (order approving stipulation and consent agreement).

[26] *PacifiCorp,* 137 FERC ¶ 61,176 (2011) (order approving stipulation and consent agreement).

but agreed to pay a $3,925,000 civil penalty, divided equally between the U.S. Treasury and NERC.

Holyoke Gas and Electric Department. On November 29, 2011, the Commission approved a settlement between Enforcement and Holyoke Gas and Electric Department (Holyoke). This order resolved staff's investigation into whether Holyoke violated 18 C.F.R. § 1c.2 (1) by offering two generation units for dispatch when the units were out of service, and (2) for failing to schedule in advance, and report to ISO-NE, three unplanned outages of two of its units that serve as capacity resources, as required by the ISO's Tariff.[27] In the settlement, Holyoke stipulated that it neither notified ISO-NE of the three outages nor scheduled them consistent with ISO-NE tariff requirements, and that it offered its units' energy for dispatch during the three outages when it knew those units could not have provided energy if dispatched by ISO-NE. Holyoke neither admitted nor denied that these actions violated section 1c.2 of the Commission's regulations. Holyoke agreed to disgorge $375,576.31 of unjust profits related to the capacity payments it received and agreed to submit compliance monitoring reports.

D. Self-Reports

From issuance of the first Policy Statement on Enforcement in 2005 through the end of FY2012, staff has received a total of 547 self-reports. Recent years' reports are broken down by fiscal year as follows:

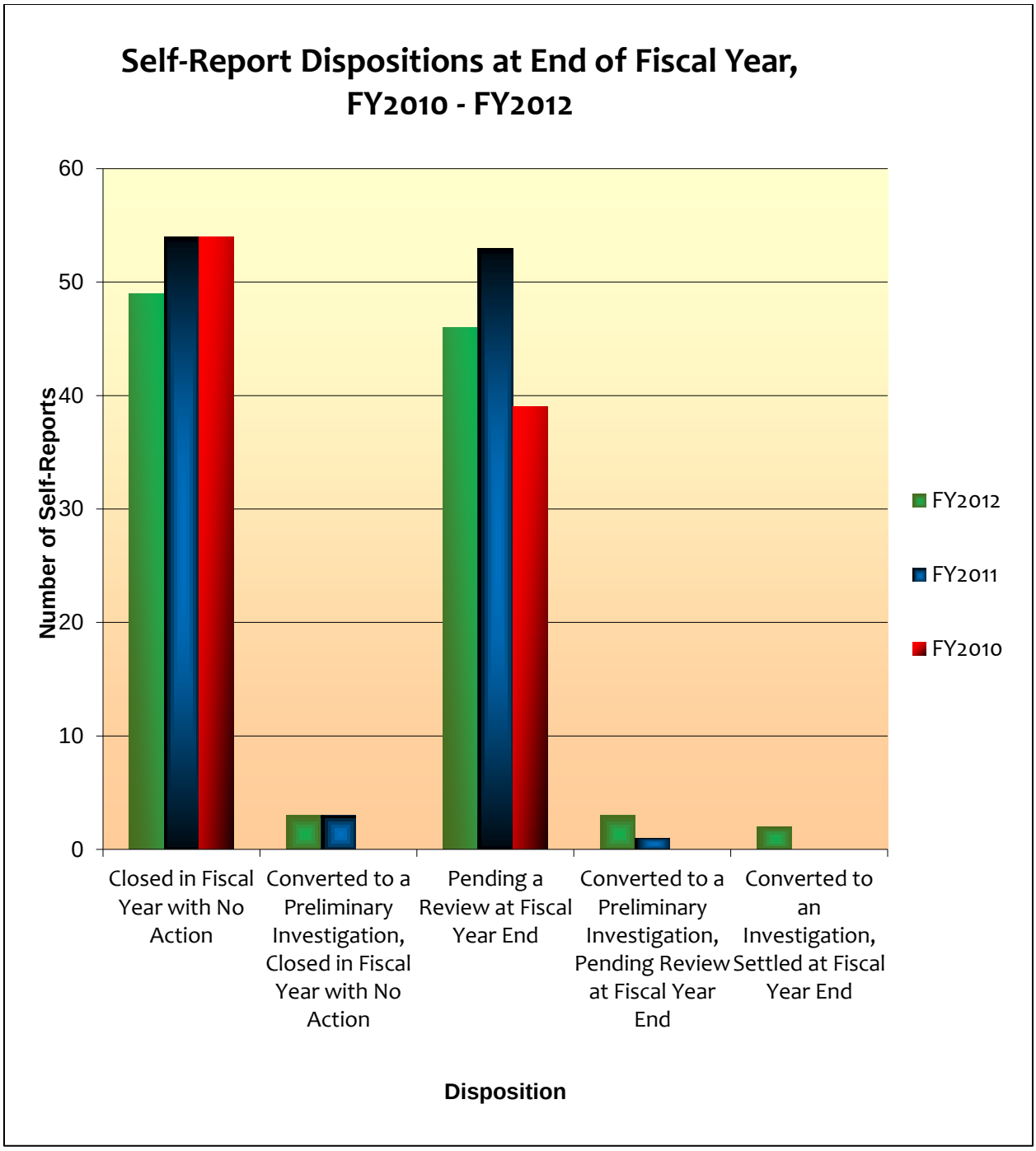
- FY2010 – 93 reports received
- FY2011 – 107 reports received
- FY2012 – 89 reports received

Of the 89 self-reports received in FY2012, staff closed 49 after an initial review and without opening an investigation. At the conclusion of FY2012, staff's review was pending on 46 self-reports (including self-reports received before FY2012). Staff received self-reports from a variety of market participants, including power marketers, electric utilities, natural gas companies, and RTO/ISOs.

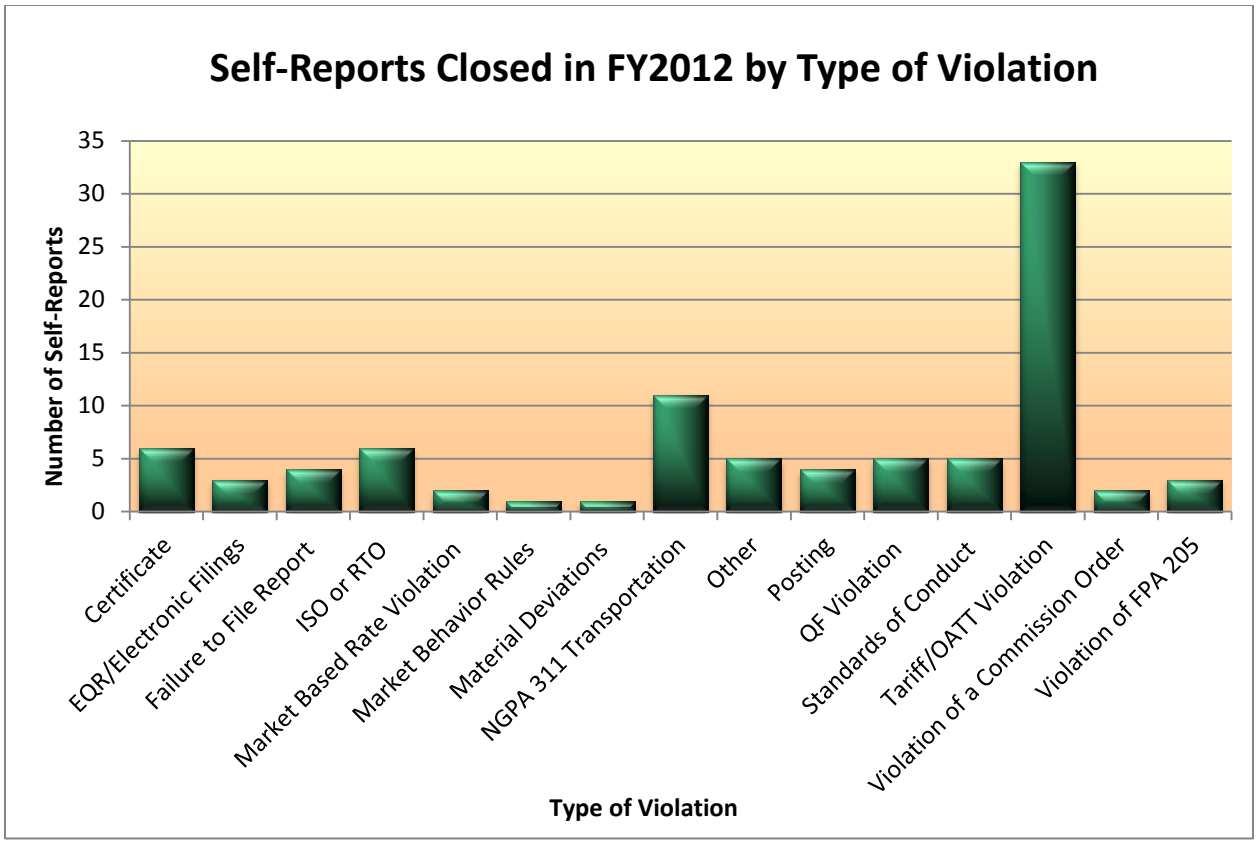
The Penalty Guidelines emphasize the importance of self-reporting, providing credit that significantly mitigates a penalty when a self-report is made.[28] Staff continues to encourage the submission of self-reports and views self-reports as evidence of a company's commitment to compliance.

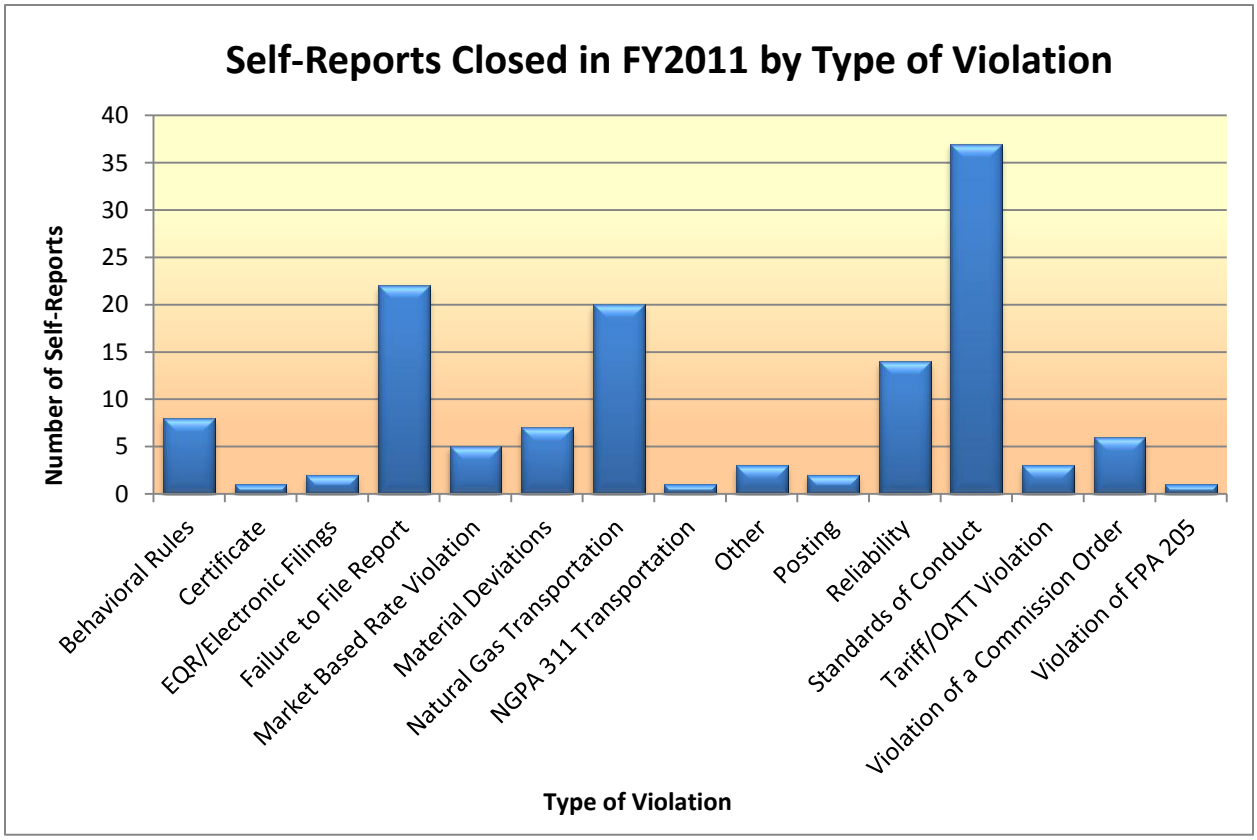
[27] *Holyoke Gas and Electric Department,* 137 FERC ¶ 61,159 (2011) (order approving stipulation and consent agreement).

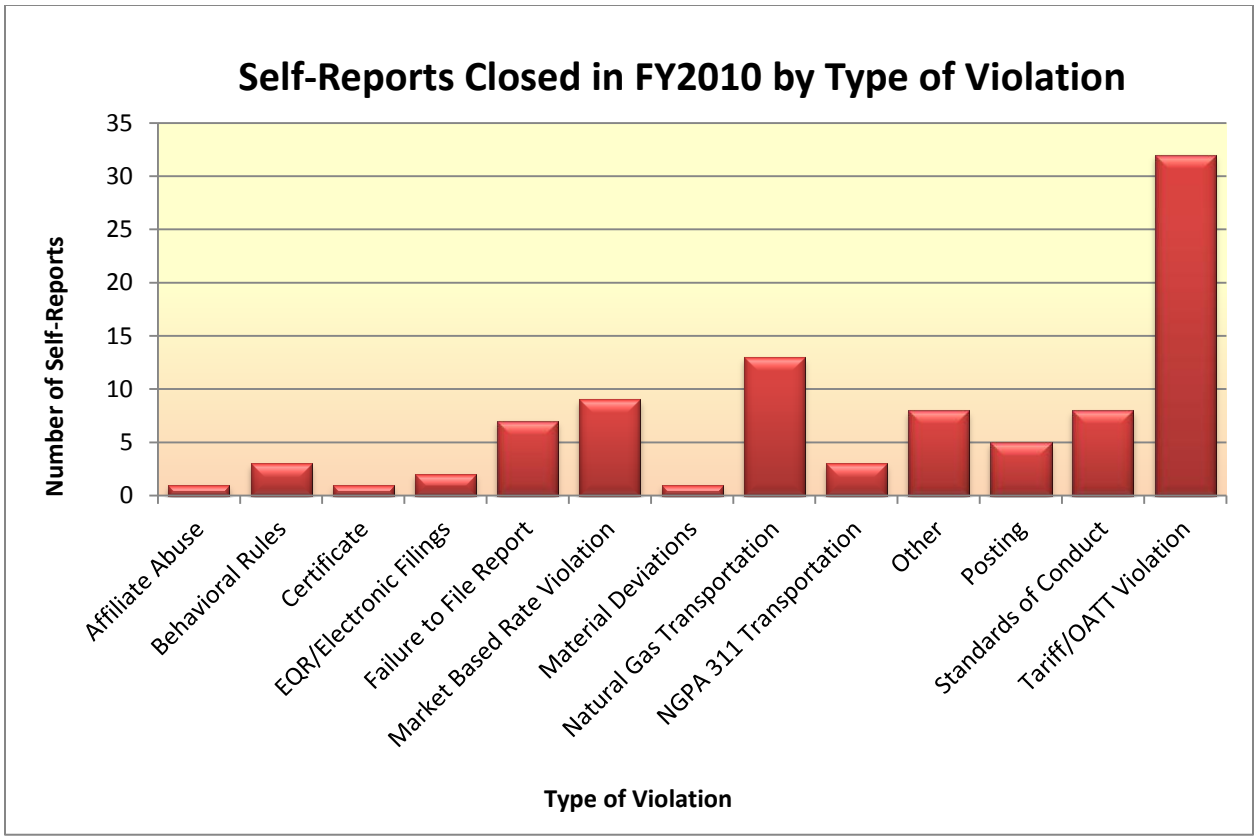
[28] *Revised Policy Statement on Penalty Guidelines*, 132 FERC ¶ 61,216 at P 127 (2010).



The following charts depict the types of violations for which staff received self-reports from FY2010 through FY2012. In FY2012 OATT violations accounted for a significant portion of self-reports received.


Self-Reports Closed in FY2012 by Type of Violation
Number of Self-Reports
35
30
25
20
15
10
5
0
Certificate
EQR/Electronic Filings
Failure to File Report
ISO or RTO
Market Based Rate Violation
Market Behavior Rules
Material Deviations
NGPA 311 Transportation
Other
Posting
QF Violation
Standards of Conduct
Tariff/OATT Violation
Violation of a Commission Order
Violation of FPA 205
Type of Violation


Self-Reports Closed in FY2011 by Type of Violation
Number of Self-Reports
40
35
30
25
20
15
10
5
0
Behavioral Rules
Certificate
EQR/Electronic Filings
Failure to File Report
Market Based Rate Violation
Material Deviations
Natural Gas Transportation
NGPA 311 Transportation
Other
Posting
Reliability
Standards of Conduct
Tariff/OATT Violation
Violation of a Commission Order
Violation of FPA 205
Type of Violation



Illustrative Self-Reports Closed with No Action

In a continuing effort to promote transparency while encouraging the compliance efforts of regulated entities, staff presents the following illustrations summarizing some of the self-reports that staff closed in FY2012. These illustrations are intended to provide guidance to the public and to regulated entities as to why staff chose not to pursue enforcement action, while preserving the non-public nature of the self-reports.

Tariff/OATT Violation. A transmission provider self-reported that it failed to post to OASIS changes to Available Transmission Capacity and Total Transmission Capacity on its network for a period of three years. The entity did not initially log and publicly disclose these changes as required by Commission regulations. On discovery of this violation, the entity posted to OASIS blanket transmission capacity change notices and implemented an alarm system to notify its technicians when they must post capacity changes. It also promptly filed a self-report. Because the conduct did not cause harm to market participants, the entity did not benefit from its oversight, and the entity took appropriate remedial measures, staff closed the self-report with no further action.

Tariff/OATT Violation. An RTO/ISO self-reported a tariff violation concerning the use of its *pro forma* Generator Interconnection Agreement (GIA). The RTO/ISO had revised the *pro forma* GIA in its tariff, but failed to incorporate certain changes into the template it used to prepare and tender initial GIA drafts to interconnection customers and transmission owners for negotiation. After updating its template to include the missing language, the RTO/ISO confirmed the template was consistent with all previous Commission-accepted tariff fillings. Twenty-one GIAs that were negotiated after the effective date of the tariff change contained non-conforming language. Eighteen were reported as conforming GIAs in the RTO/ISO's Electric Quarterly Report (EQR). At staff's request, the RTO/ISO re-executed the eighteen non-

conforming GIAs and re-filed them with the Commission. Furthermore, the RTO/ISO consolidated responsibility for processing future tariff revisions and documented an internal process map for tariff filings to ensure that all relevant RTO/ISO personnel are aware of each tariff filing/Commission order and the resulting impact. Because the RTO/ISO quickly self-reported the violation, took immediate steps to remedy the situation, and no harm resulted from the error, staff closed the self-report with no further action.

Tariff/OATT Violation. An RTO/ISO self-reported that demand forecast and metered data information pertaining to roughly 150 market participants, covering a period of approximately 32 months, had been inadvertently disclosed to five market participants. The information was confidential in nature and each market participant should only have been allowed access to its own information. The RTO/ISO notified the 150 participants of the disclosure and promptly automated its demand forecast review process to ensure that market participants would have access to only their own forecast data. It also obtained affidavits from the five market participants that had received the confidential data and confirmed that each had destroyed the material and would not use the information to gain a competitive advantage in the RTO/ISO's energy markets. Because of the apparent lack of harm from the inadvertent breach, and the institution of new safeguards, staff closed the self-report with no action.

Tariff/OATT Violation. A hydropower project manager failed to explicitly notify an ISO of its derated capacity based on low river flow in violation of the ISO's tariff. The manager did supply the correct amount of capacity the project could provide that day, but failed to send an email making explicit the amount by which that capacity diverged from the project maximum. Because no harm resulted from the errors, the project manager performed a thorough investigation (finding 19 instances over a period of 2,191 days when the derate was not made explicit, an error rate of 0.008%), and the company took measures to ensure the mistake would not be repeated, staff closed the self-report with no further action.

Shipper-Must-Have-Title Violation. A natural gas marketer self-reported potential shipper-must-have-title (SMHT) violations that occurred between 2003 and 2011. The marketer shipped natural gas to various local distribution companies for delivery to retail customers but, for tax-related purposes, transferred title to the customers prior to delivery at the city gates. Because no harm occurred to jurisdictional markets or third parties, the violations were not intentional, and the marketer repaid the avoided tax assessment, restructured its customer contracts, retrained its contract administrator, and obtained regulatory advice on how to ensure ongoing compliance with the Commission's regulations, staff closed the self-report with no further action.

Shipper-Must-Have-Title Violation. While winding down the business of one of its affiliates, a natural gas company discovered that for several years it had transported gas to which it did not hold title and reported the conduct as a violation of the Commission's SMHT requirements. Upon further review of the self-report, staff discovered that the natural gas company had not violated the SMHT rule because the company was transporting gas from a supply area on behalf of a co-interest. Accordingly, staff determined that the natural gas company's activity fell within the Commission's recognized "good right to deliver" exception and closed the self-report with no further action.

Standards of Conduct Violation. Due to an automated feature in its transaction management system, a natural gas pipeline company improperly made available to marketing function employees of its affiliate certain nomination and imbalance information for one month, in violation of the Commission's Standards of Conduct. The company thereafter posted notice of the improper disclosure as required. Because the company altered the configuration of its transaction management system to prevent recurrence, quickly self-reported the problem, and

took steps to remedy the situation, and no harm resulted from the error, staff closed the self-report with no action.

Commission Filing Requirement Violation. A natural gas pipeline company self-reported that it inadvertently failed to include certain offshore facilities abandoned during each of the years 1992, 1994 through 1998, and 2001 through 2008, in its annual blanket certificate reports, as required by 18 C.F.R. §§ 157.207(e) and 157.216(d). During the performance of a comprehensive regulatory compliance review and audit, the company discovered that the facilities the pipeline failed to reference included metering and pressurization equipment and minor small-diameter pipeline segments. Staff closed the self-report with no enforcement action because, after submitting its self-report, the pipeline promptly submitted revised annual blanket certificate reports including the omitted facilities for the years in question to remedy the violations, there was no economic benefit from the pipeline's omissions, no harm was caused to the market from its omission, and the pipeline further implemented compliance procedures to ensure that no similar violations occur in the future.

Market-Based Rate Authority Violation. A seller self-reported that it inadvertently engaged in four hourly wholesale sales of electric power without obtaining MBR authorization from the Commission as required by section 205 of the FPA. The seller explained that an affiliated company had obtained MBR authorization and engaged in four hourly transactions as a test, but inadvertently tagged the sales using the seller's name rather than its own name. The affiliated company identified the error within 48 hours and contacted the ISO, but the ISO's tariff does not permit entities to change the seller's name after the transaction is completed. The seller thereafter submitted a refund report, which the Commission accepted. The seller and its affiliated company have put new compliance measures in place to prevent recurrence of similar violations. Because the seller's violations were inadvertent, the number of sales made was *de minimis* (four total sales), the affiliate discovered the violations promptly and the seller self-reported the violations shortly after discovery, the seller has not engaged in any additional violations, the seller has no prior history of non-compliance, and the seller has taken steps to prevent similar errors in the future, including employee training and computer software and hardware improvements, staff closed the self-report with no action.

OASIS Violation. An RTO/ISO reported a discrepancy between prices posted on OASIS for real-time dispatch and the prices actually used in settlements. The discrepancy, which occurred during a single hour, only affected three market participants. Upon discovery, the RTO/ISO reposted the correct price on OASIS, emailed market participants to inform them of the reposting, and also identified the error in a subsequent quarterly report. Because the prices used in the settlements were correct, the RTO/ISO did not need to adjust any market participant's bill. To prevent such an error from occurring again, the RTO/ISO implemented a manual verification process. Because the error was limited to one hour, affected few market participants who did not object, and caused no harm, and because the RTO/ISO took steps to ensure that a similar error would not occur in the future, staff closed this self-report with no action.

Capacity Release Violation. A corporation, in the midst of restructuring, attempted to transfer all gas supply and capacity contracts out of the name of its gas production subsidiary and into the name of a subsidiary that would be responsible for all shipping and selling of its gas going forward. The gas title transfer was immediately effective, but the corporate subsidiary handling the capacity transfers did not realize that several capacity contracts, which were non-assignable, could not be transferred among affiliated entities without involving the pipeline. Consequently, the affiliate moving the gas committed numerous shipper-must-have-title violations, which the company did not discover for several months. Because the capacity in question was non-assignable, it could not have been posted for bidding. Furthermore, the company continued to

use the capacity, as before, to ship exclusively its own gas. Had the company transferred the capacity and gas using the means of an asset management agreement, it would not have committed a violation. Because of these facts, and because the corporation did not commit the violations intentionally, management investigated promptly and self-reported the violations upon discovery, and because it instituted several measures to prevent recurrence, staff closed the matter without further action.

E. Investigations

During FY2012, DOI staff opened and closed approximately the same number of investigations as it did in FY2011. Staff opened sixteen investigations in FY2012 as compared to twelve investigations in FY2011. In FY2012, twenty-one investigations resulted in settlement, Commission show cause orders, or were closed without enforcement action.

1. Statistics on Investigations

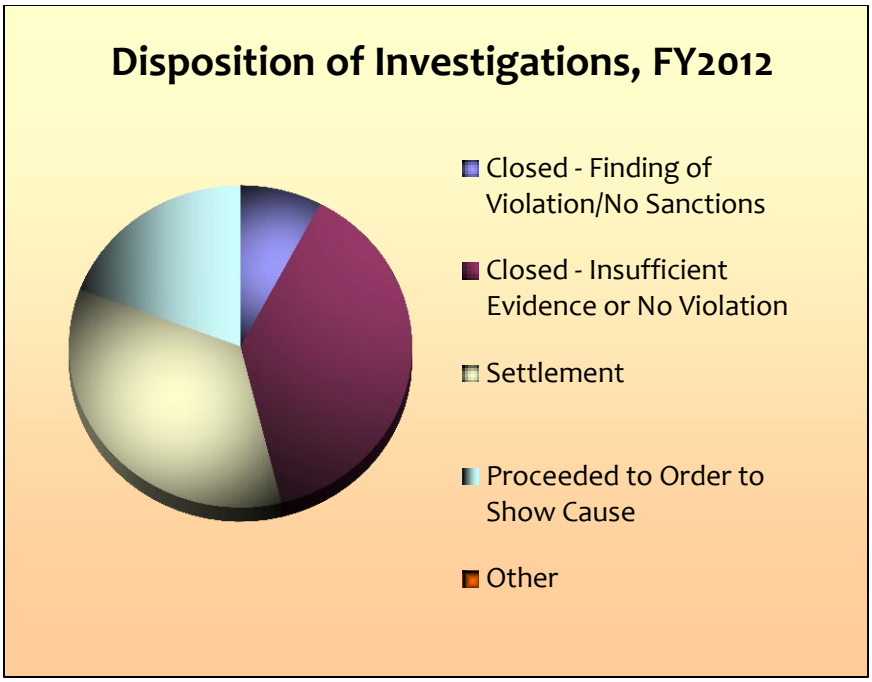
Of the sixteen investigations staff opened this fiscal year, some of which involve more than one type of violation or multiple subjects, eleven involve market manipulation or false statements to the Commission or RTO/ISO, two involve tariff violations and manipulation, two involve MBR authority and one involves section 203 of the FPA.[29]

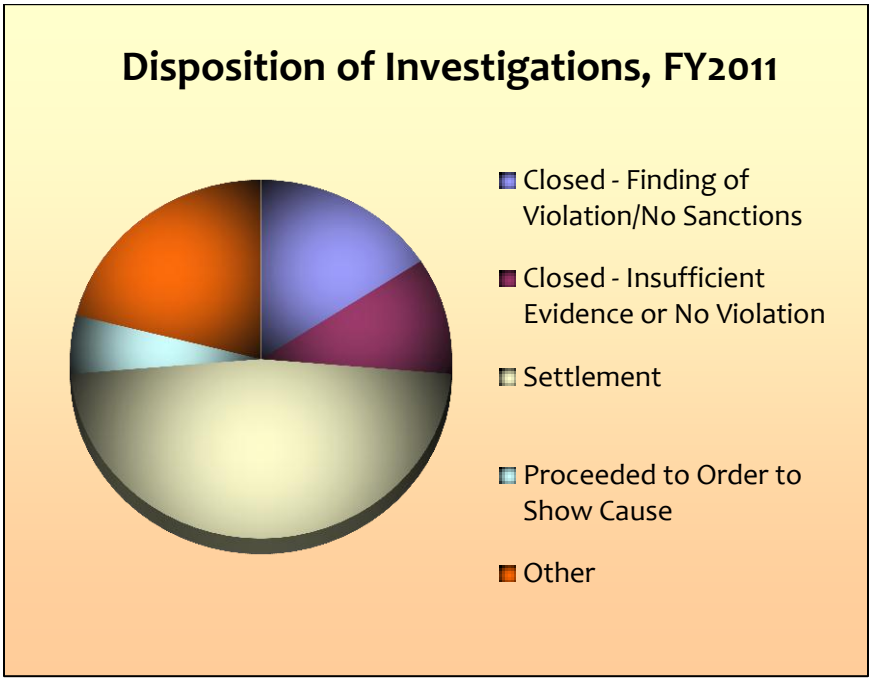
As in previous years, staff opened several investigations in FY2012 based on referrals from RTOs/ISOs, RTO/ISO market monitoring units (MMUs), the Commission, DAS, and other program offices within the Commission. Staff also opened investigations based on tips from outside callers through the Enforcement Hotline, and from self-reports.

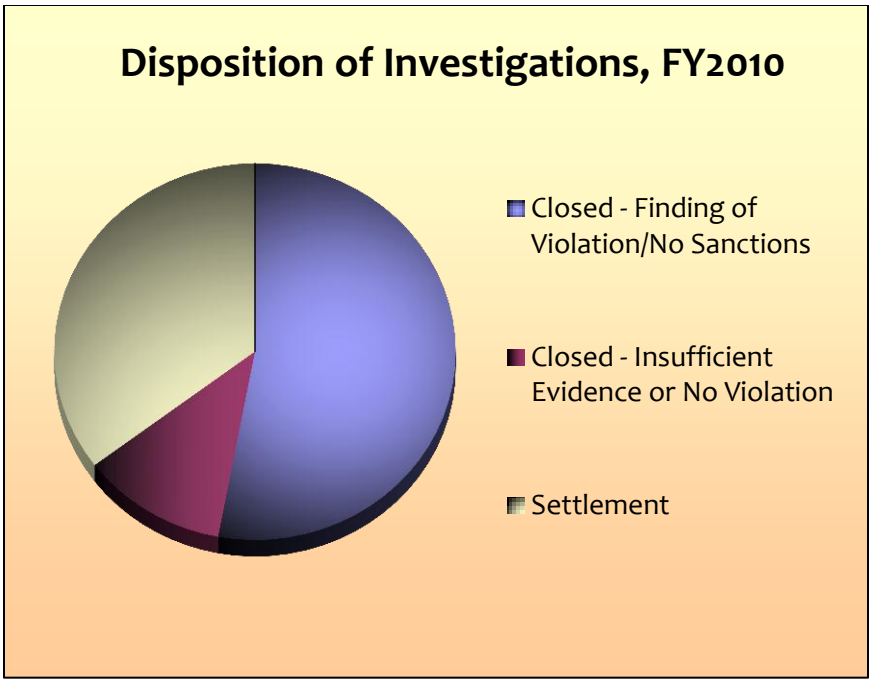
Of the investigations closed this fiscal year, staff closed nine either upon finding no violation or because staff did not have evidence to support finding a violation. In two investigations, staff found a violation, but determined not to pursue an enforcement action. Nine investigations concluded with settlement.

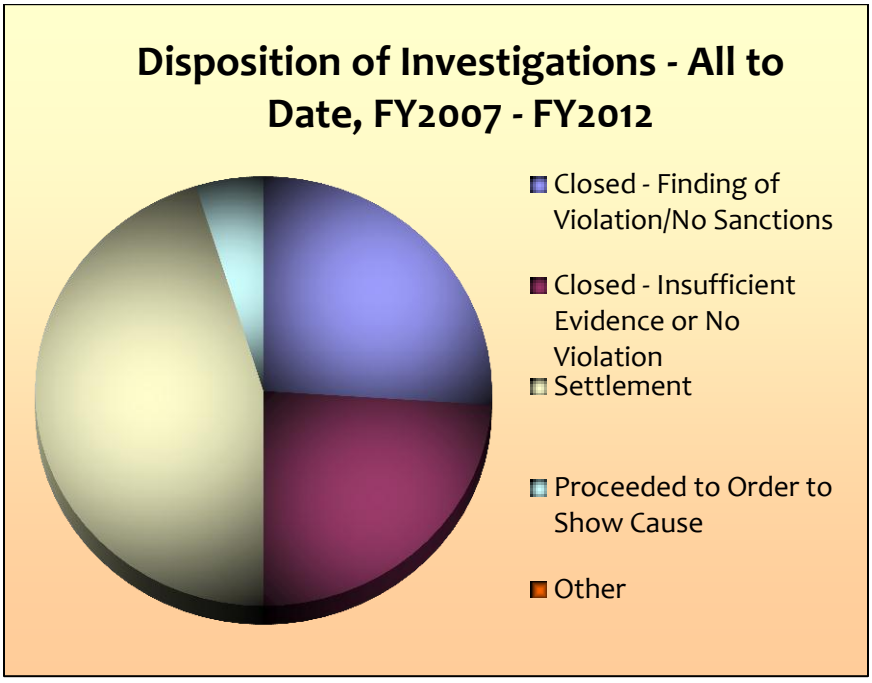
The following charts show the disposition of investigations that closed in fiscal years 2009 through 2012.

[29] Staff also converted one self-reported potential violation to an investigation in FY2012.

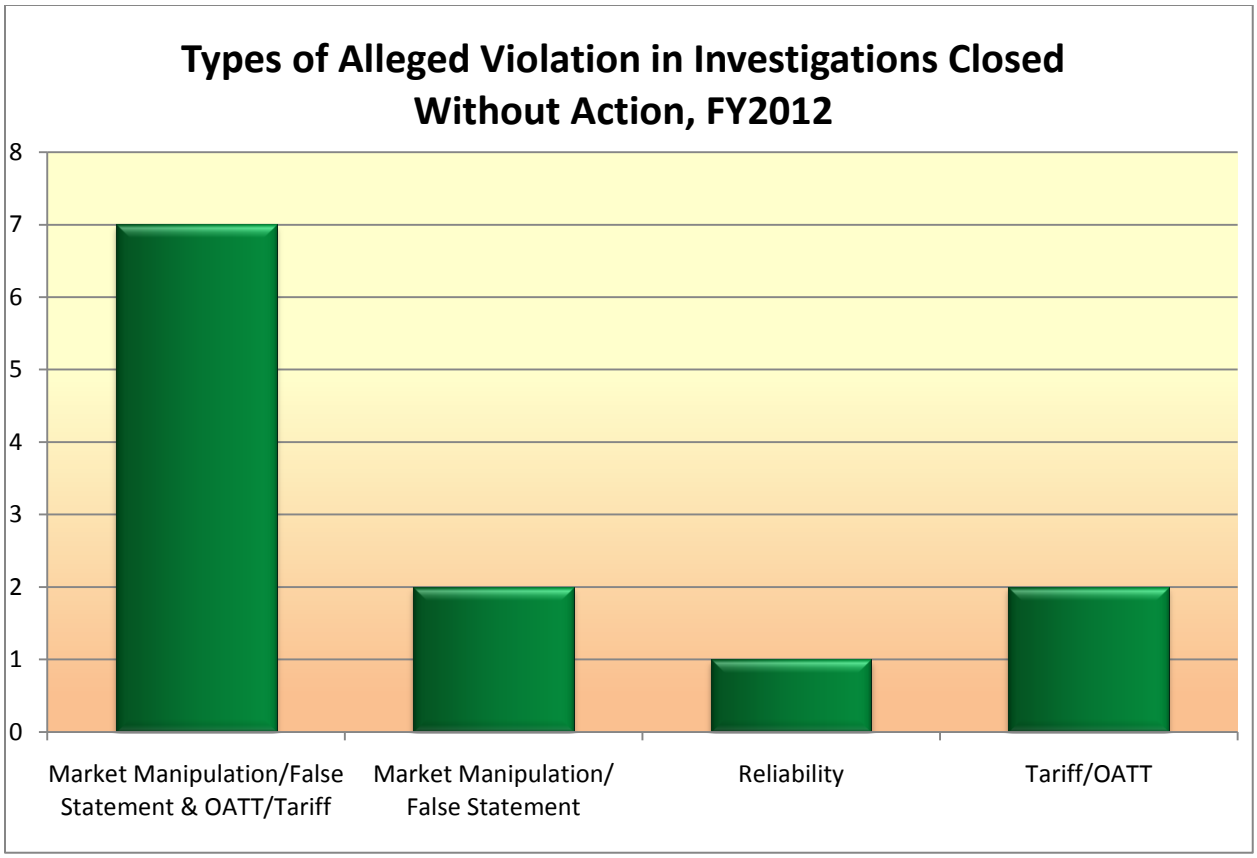

Disposition of Investigations, FY2012
Closed - Finding of Violation/No Sanctions
Closed - Insufficient Evidence or No Violation
Settlement
Proceeded to Order to Show Cause
Other

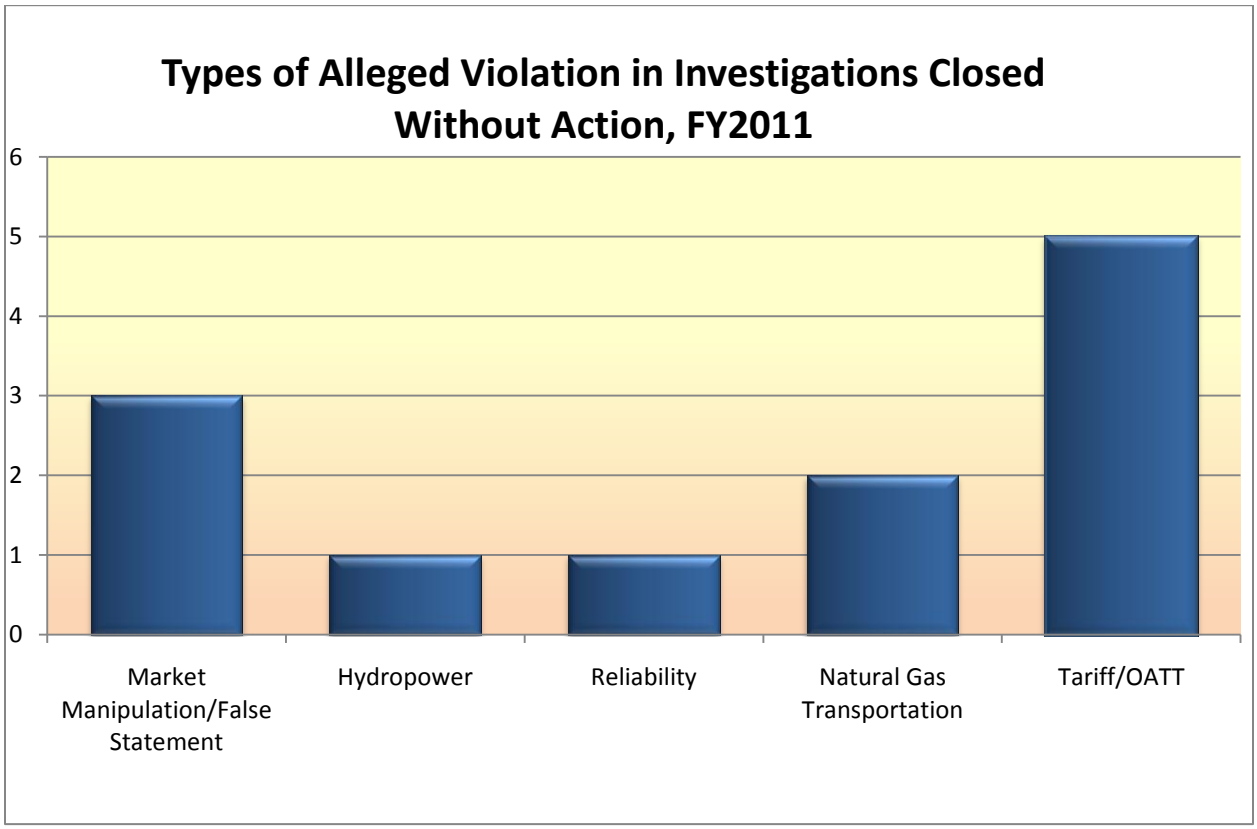

Disposition of Investigations, FY2011
Closed - Finding of Violation/No Sanctions
Closed - Insufficient Evidence or No Violation
Settlement
Proceeded to Order to Show Cause
Other

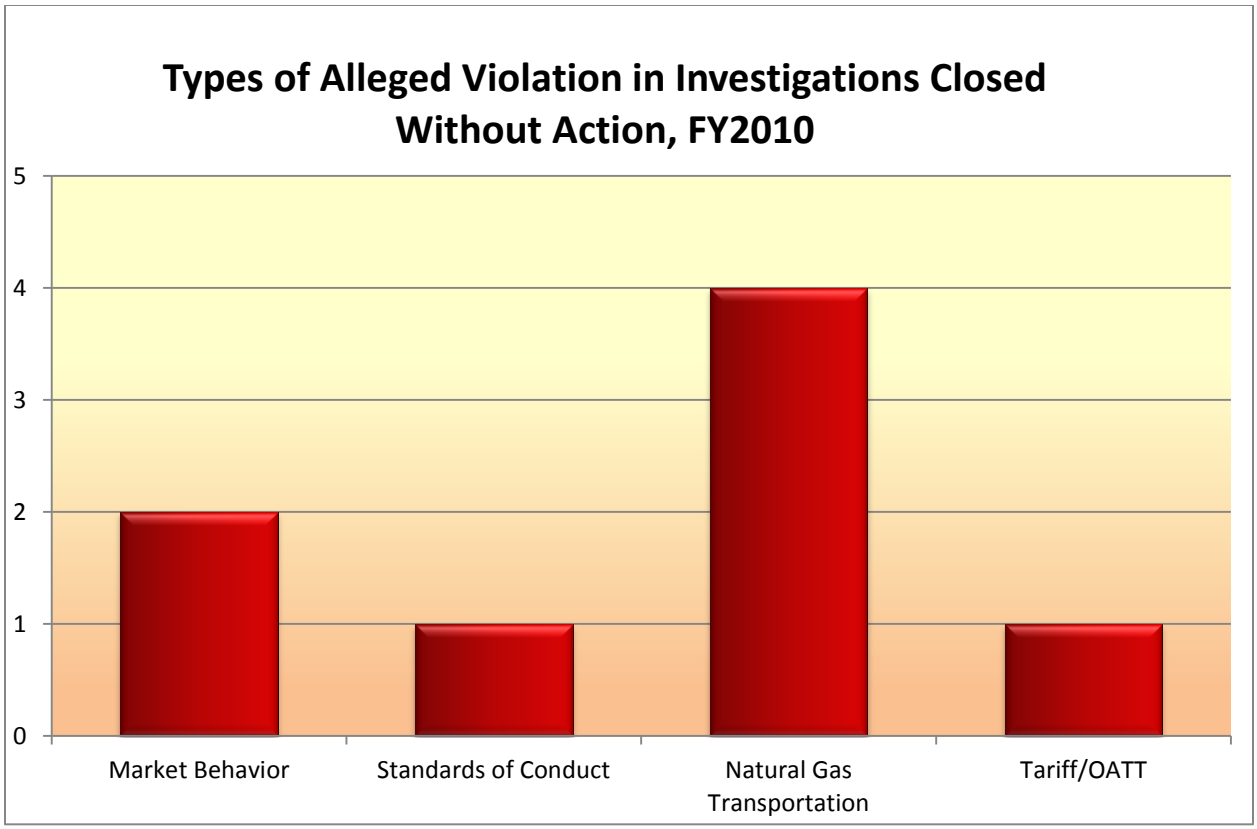




The following charts provide the nature of the conduct at issue for those investigations that were closed without action in fiscal years 2010 through 2012.


Types of Alleged Violation in Investigations Closed Without Action, FY2012
8
7
6
5
4
3
2
1
0
Market Manipulation/False Statement & OATT/Tariff
Market Manipulation/ False Statement
Reliability
Tariff/OATT


Types of Alleged Violation in Investigations Closed Without Action, FY2011
6
5
4
3
2
1
0
Market Manipulation/False Statement
Hydropower
Reliability
Natural Gas Transportation
Tariff/OATT



2. Illustrative Investigations Closed with No Action

The following describes selected instances where staff undertook an investigation, but did not take any enforcement action. Like the self-report illustrations, these are intended to provide guidance to the public while preserving the non-public nature of DOI's investigations.

Market Manipulation. Staff investigated a participant in an organized market that was alleged to have executed strategically-placed virtual transactions at or near nodes where that market participant owned financial transmission rights or congestion revenue rights for the unlawful purpose of artificially inflating the value of those rights. Following a comprehensive investigation, staff closed the investigation without further action because there was insufficient evidence to prove that the virtual transactions were part of a manipulative strategy.

Reliability. Staff investigated whether there were Reliability Standards violations committed by two entities related to a loss of transmission lines. Several 345 kV transmission lines tripped over three days in 2009, while the company attempted to energize capacitor banks at a substation. On the first and third day, one line tripped; on the second day, five lines tripped and one of the two main buses at the substation also tripped. Staff's investigation determined that two practices caused or contributed to the trips: (1) failure to adequately maintain battery chargers used for substation equipment, and (2) use of unshielded cables. Although these two practices caused or contributed to the trips, they did not violate the Reliability Standards. Staff found potential violations of the COM-002-2 R2 Reliability Standard, but determined that those violations did not cause or contribute to the trips. Because the relevant RE had already identified these violations with regard to one of the entities, staff decided to refer its findings for both entities to the RE for resolution.

Tariff Violations. Staff investigated potential tariff violations related to the performance of certain generators in an RTO/ISO's market for ancillary services. The tariff provided that entities offering non-spinning reserves must respond to deployment commands within a defined time limit. At the initiation of the investigation, approximately seven months after the market was established, the RTO/ISO reported that not all generators responded within the time limit. Although the investigation determined that the resources failed to provide the requested amount of reserves within the required time, contrary to the explicit requirements of the tariff, staff determined that it was appropriate to close the investigation without further action because the RTO/ISO had already assessed the applicable failure charges, the failures were inadvertent, and the response rate had improved to nearly one hundred percent by the close of the investigation.

F. Reliability

Pursuant to its Compliance Monitoring and Enforcement Program, NERC files NOPs with the Commission that reflect violations of the Reliability Standards discovered by NERC or one of the eight REs after investigation. Each NOP indicates resolution of a violation or potential violation through a penalty and mitigation plan, which may result from an assessment by the relevant RE or NERC, or from settlement negotiations with the registered entity. Pursuant to the Commission's regulations, an NOP becomes effective by operation of law thirty-one days after filing with the Commission if the Commission takes no action within that time either to extend the time for consideration, to request more information, or to open the matter for further review, or if the entity does not file an application for review.

In FY2012, the Commission received 33 full NOPs, encompassing 285 potential or confirmed violations.[30] One hundred fifty two potential or confirmed violations were of the Critical Infrastructure Protection (CIP) Reliability Standards (CIP-002 through CIP-009). The Commission also received 12 Spreadsheet NOPs, consisting of minimal or moderate risk violations, encompassing 619 potential or confirmed violations. Two hundred seventy nine of these potential or confirmed violations were of the CIP Reliability Standards.[31] The NOPs filed in FY2012 proposed $6,490,499 in penalties. The largest single penalty assessed by an NOP submitted to the Commission in FY2012 was $400,000. DOI staff, together with staff from OER and the Office of the General Counsel (OGC), reviewed the NOPs as they were filed and recommended whether the Commission should take action or decline further review. The Commission declined to review all NOPs submitted in FY2012.

On March 15, 2012, the Commission accepted, with conditions, NERC's proposed FFT enforcement mechanism.[32] The FFT Report disposes of certain possible violations that pose lesser risks to the bulk power system and that the entity has mitigated prior to NERC's filing to the Commission, through a monthly informational filing to the Commission. This filing is in lieu of processing these same issues as NOPs. In FY2012, the Commission received 12 FFT Reports detailing 707 possible violations. Four hundred and four possible violations were of the CIP Reliability Standards. The Commission declined to review 631 possible violations submitted in

[30] Two additional NOPs were filed by NERC, but were subsequently withdrawn prior to consideration by the Commission.

[31] All NOPs are available on the NERC website at http://www.nerc.com/filez/enforcement/index.html.

[32] *North American Electric Reliability Corp.,* 138 FERC ¶ 61,193 (2012) (order accepting with conditions the ERO's petition requesting approval of new enforcement mechanisms and requiring compliance filing).

FY2012. Seventy-five FFTs filed in RC12-16-000 are still under consideration by the Commission at the time of this report.

On June 21, 2012, the Commission issued an order denying rehearing and providing clarification on the Turlock Irrigation District NOP filed in Docket No. NP10-18-000.[33] The NOP, affirmed by the Commission on March 17, 2011,[34] proposed an $80,000 penalty for multiple violations, of which the most severe is a violation of FAC-003-1 R2, related to a vegetation-caused outage and loss of load of 270 MW for more than an hour on August 29, 2007. This NOP was the first in which a vegetation contact that led to the outage of a transmission line resulted in a loss of load.

On July 19, 2012, in response to a request for review of an NOP assessing a $19,500 penalty against the Southwestern Power Administration, the Commission found that section 215 of the FPA authorizes the imposition of a monetary penalty against a federal agency for violation of a mandatory Reliability Standard.[35] Requests for Rehearing are currently pending before the Commission.

G. Enforcement Hotline

DOI staff fields calls and other inquiries made to the Enforcement Hotline (Hotline).[36] The Hotline is a means for people to inform Enforcement staff, anonymously if preferred, of potential violations of Commission statutes, rules, regulations, and orders. The Hotline also allows the public to obtain informal guidance and non-binding opinions on matters within the Commission's jurisdiction, including applicability of Commission orders and policies in particular circumstances. When staff receives calls concerning possible violations, such as allegations of market manipulation, abuse of an affiliate relationship, or violation of a tariff or order, staff researches the issue presented and consults other members of the Commission's staff with expertise in the subject matter of the inquiry. In some cases, the Hotline calls lead to investigations by DOI.

In FY2012, Enforcement received 185 Hotline calls and inquiries, and resolved 165 matters (including matters that remained open at the end of FY2011). The majority of these calls were closed without action, and a significant number were successfully resolved through advice provided by DOI staff. In some instances staff informally assisted callers in resolving disputes with the assistance of subject matter experts from other Commission program offices. In FY2012, staff converted three Hotline calls to preliminary investigations. Every year, a significant percentage of the calls received relate to subjects outside of the Commission's jurisdiction or contested matters pending before the Commission. DOI staff advises those callers on where they may find the information they need, or directs them to the appropriate Commission docket.

[33] *North American Electric Reliability Corp.,* 139 FERC ¶ 61,248 (2012) (order denying rehearing and providing clarification).

[34] *North American Electric Reliability Corp.*, 134 FERC ¶ 61,209 (2011) (order on review of NOP).

[35] *North American Electric Reliability Corp.,* 140 FERC ¶ 61,048 (2012) (order on review of NOP).

[36] *See* 18 C.F.R. § 1b.21 (2012).

DIVISION OF AUDITS

A. Overview

The Division of Audits within Enforcement continues to administer the Commission's audit and accounting programs. These programs help the Commission achieve effective and appropriate oversight of jurisdictional entities while maintaining accountability and transparency. To accomplish its mission, DA conducts operational and financial performance and compliance audits of jurisdictional entities, and conducts other activities that aid the Commission. These audits and other activities assess how jurisdictional entities implement statutes, orders, rules, tariffs, and regulations the Commission administers.

Audits are typically initiated without any allegation of wrongdoing. DA provides continuous feedback to the audited entities, primarily focusing on operational improvements, transparency, accountability, efficiency, effectiveness, and compliance. Through publicly issued audit commencement letters and audit reports, DA provides audited entities and the industry with insights into areas of emphasis and concern. DA coordinates its audit activities with other Enforcement divisions and other Commission offices, and applies its experience from conducting audits to ensure effective Commission oversight, modify or create regulations, assist in policy formulation, and encourage transparency to the public.

DA's Chief Accountant ensures compliance with the Commission's accounting regulations by participating with other Commission offices in the processing of various filings. The Chief Accountant and DA staff provide expert accounting advice and analysis to support Commission actions. The Chief Accountant also reviews audit reports involving accounting matters to ensure compliance with Commission accounting regulations, and reviews and acts on accounting filings from jurisdictional entities involving a variety of accounting matters.

In addition, DA continues to work with other Commission offices to address various policy matters and advises the Commission on accounting matters affecting regulated industries. DA reviews and comments on exposure drafts and other publications of the Securities and Exchange Commission (SEC), Financial Accounting Standards Board (FASB), and International Accounting Standards Board (IASB) to address accounting matters that may affect Commission oversight and regulation of jurisdictional entities.

DA continues to make its staff available to discuss accounting matters with jurisdictional entities informally before they make a filing with the Commission and provides guidance during formal pre-filing conferences with jurisdictional companies. DA promotes transparency by posting accounting orders on the Commission's website and by addressing accounting inquiries through a dedicated phone line and email address.[37]

Communicating and emphasizing what constitutes effective oversight, accountability, transparency, performance, and compliance continue to be central goals of DA's audit and accounting programs. DA conducts industry outreach at formal speaking engagements, industry liaison meetings, and through discussions with audited entities and their outside counsel. DA also provides information about the audit process on the Commission's website.[38]

[37] FERC accounting guidance, including a topic index and accounting point-of-contact information is available at www.ferc.gov/legal/acct-matts.asp.

[38] The OE audit process is described at www.ferc.gov/enforcement/audits/audit-process.pdf.

B. Compliance Program Reviews

Robust internal compliance programs are the first line of defense in ensuring compliance with Commission statutes, orders, rules, tariffs, and regulations. Among other characteristics, a well-designed compliance program should be formally structured and organized, and independent. Such a program should also regularly assess risk, include a reporting process with direct linkages to senior management, and provide adequate training for employees and contractors at all levels. A well-designed compliance program with strong support by executive-level corporate officials should foster a strong and sustainable culture of compliance over the entire company.[39]

Consistent with the Commission's strategic goal of promoting internal compliance, DA has continued to review company compliance programs and provided informal feedback and recommendations on most DA-directed audits. Rather than wait for DA to conduct an audit and provide feedback on their compliance programs, some companies have taken a more proactive approach and conducted their own internal audits to assess their compliance programs. Several of these companies have spoken publicly about the positive impact these audits have had on their own operations and internal compliance programs.

DA takes a broad view with respect to compliance and considers not only compliance with Commission rules and regulations, but also evaluates a company's compliance with its own internal processes and procedures and makes recommendations when appropriate. DA has observed that companies with a strong compliance culture typically abide by all requirements, whether internal or external. These same companies are also more likely to follow the spirit of the Commission's rules and regulations, not just the literal interpretation. A robust compliance program accompanied by appropriate training will normally lead to effective internal oversight, accountability, transparency, and increased performance and compliance throughout the company.

Beyond reviewing internal compliance programs, DA has had a long-standing history of promoting compliance through transparency in its audit process and industry outreach. DA's publicly posted audit commencement letters and audit reports provide the public and jurisdictional entities with information about the focus of the Commission's attention to particular topics. In addition, DA has expanded its audit reports to provide greater detail to enable entities to be better informed and prepared to avoid noncompliance and improve performance in their operations. In particular, DA has enhanced the detail in the Scope and Methodology section of its audit reports to enable company compliance staff to replicate procedures DA has employed in its audits. This enhanced detail also provides internal compliance programs with a roadmap to follow for companies' own self-evaluation.

DA's outreach efforts also include responding to questions received directly from jurisdictional entities, industry stakeholders, and consultants, as well as questions arising through the Commission's Compliance Help Desk, Office of External Affairs, Enforcement Hotline, and other offices within the Commission. During FY2012, DA responded to more than 119 such questions, providing informal advice on various aspects of Commission accounting, financial reporting, and record retention regulations.

DA also oversees accounting liaison activities with industry groups, such as the Edison Electric Institute, American Gas Association, Interstate Natural Gas Association of America, the Association of Oil Pipelines, and various accounting firms. In meetings with industry groups

[39] *Revised Policy Statement on Penalty Guidelines*, 132 FERC ¶ 61,216 at § 1b2.1 (2010).

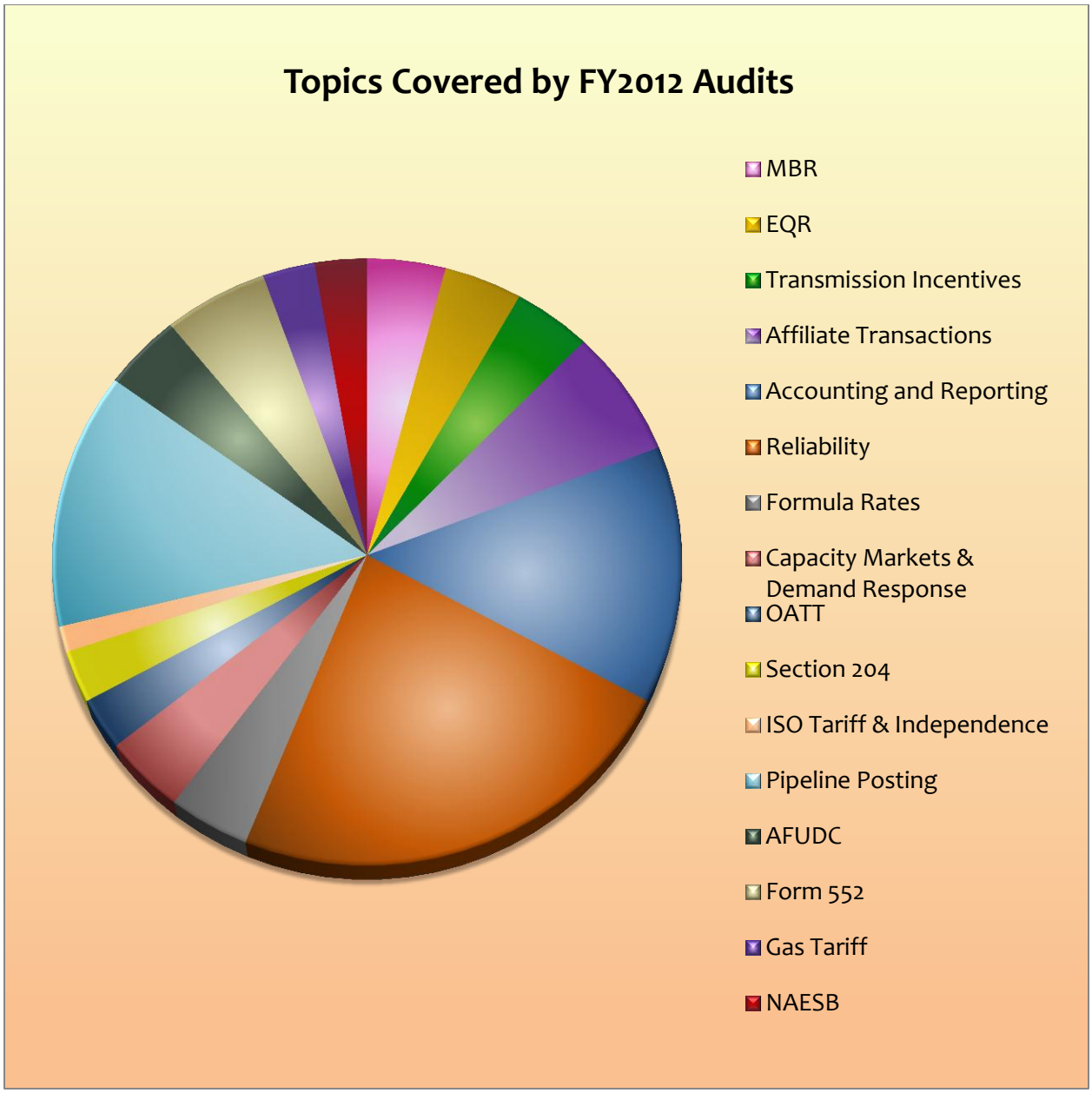
and jurisdictional entities, and in response to inquiries, DA staff helps provide regulatory certainty on audit, accounting, and reporting matters.

DA's comprehensive approach to compliance entails reviews and outreach that not only provide an opportunity to give feedback to individual companies, but also serve as a gauge of the industry as a whole. In FY2012, these reviews have provided anecdotal evidence of companies' increased awareness of the benefits of compliance programs and enhanced performance of the programs themselves. Despite these promising signs, DA sees additional room for improvement and will continue to emphasize compliance through compliance program reviews, audit and accounting programs, industry outreach, public accounting letters, and audit commencement letters and reports.

C. Significant Audit Matters

In FY2012, DA completed forty-four financial, compliance, and performance audits of public utilities, natural gas pipelines, and storage companies covering a wide variety of topics. Some audits addressed multiple topics. The audits resulted in 399 recommendations for corrective action and directed $5,838,155 in refunds. DA also directed accounting adjustments of $3,500,000 that will preclude their recovery through future rate proceedings. Other recommendations directed improvements to companies' internal processes and procedures, enhancements to the accuracy and transparency of reports and websites, and more efficient and cost-effective operations. Collectively, these recommendations and savings benefit ratepayers and market participants.

In addition to these DA-directed audits, DA jointly conducted fifteen reliability oversight audits with OER. These oversight audits were undertaken to observe and provide feedback to the REs as they conduct audits of registered entities. These audits provided the opportunity for OE and OER to participate in audits initiated and directed by each of the eight REs. During and at the conclusion of these audits, DA and OER provided feedback to the REs' audit teams concerning the audit process, techniques, and methods, as well as the technical rigor of the audit.



The following examples are selected highlights of audits completed in FY2012.

1. ITC Holdings Corporation

At ITC Holdings, DA evaluated compliance with conditions established in the Commission's December 3, 2007, order approving the acquisition of the transmission facilities of Interstate Power and Light Company (IPL).[40] DA identified three areas of noncompliance and made six recommendations. The areas of noncompliance included: (1) ITC Holdings did not obtain approval from its Board of Directors for dividend payments and equity infusions between ITC Holdings and ITC Midwest, a subsidiary, as its internal procedures required; (2) ITC Holdings did not provide timely notification to the Commission when a shareholder or shareholder group

[40] *ITC Holdings Corp., et al.,* 121 FERC ¶ 61,229 (2007).

had acquired five percent or more of its common stock; and (3) ITC Midwest improperly recovered from customers through formula rate billings amounts associated with the tax effects of amortized goodwill.[41] ITC Holdings contested the audit finding and recommendations concerning the improper reporting and recovery of the tax effects of amortized goodwill.

DA determined that ITC Midwest's inclusion of the tax effects of amortized goodwill ($128 million) in its formula rate was inconsistent with its application for authorization to purchase IPL's transmission facilities and approval of proposed transmission service rates. In 2008, 2009, and 2010, ITC Midwest passed approximately $27 million of the tax effect of amortized goodwill through its formula rate. DA recommended accounting adjustments and refunds to ITC Midwest's formula rate customers. ITC Holdings explicitly stated in its application that it is not seeking recovery of any acquisition premium in rates, which the Commission reiterated in its order. Subsequently, the Commission affirmed the audit report's finding and recommendations through a paper hearing.[42]

ITC Holdings has filed a Refund Report with the Commission describing how ITC Midwest will cease recording the tax effects of goodwill in its FERC accounts, remove the tax effects of goodwill from its FERC Form No. 1, recalculate customer rates and allowance for funds used during construction (AFUDC) using corrected equity balances and rates of return, and compute refunds as a result of the accounting adjustments.[43] ITC Midwest agreed to refund approximately $2.7 million and to formally file refund reports for Michigan Electric Transmission Company and International Transmission Company, two additional subsidiaries that used the same accounting treatment, within 90 days of the submission of the refund report for ITC Midwest, with refunds totaling approximately $10.3 million for these two companies.

2. EnerNOC, Inc.

At EnerNOC, DA evaluated compliance with ISO-NE's Transmission, Markets, and Services Tariff, and NYISO's Market Administration and Control Area Services Tariff.[44] DA identified seven areas of concern related to noncompliance, enhanced performance, and other matters, primarily focused on how EnerNOC managed the large volume of data necessary to participate as a load aggregator. The first area of concern related to EnerNOC's failure to develop an internal compliance program focused on jurisdictional operations. This failure resulted in noncompliance relating to the six additional areas: (1) its management of the data used to create resource bids into the markets; (2) its processes to determine appropriate demand reduction values; (3) its procedures for ensuring that it properly reduced load obligations; (4) its registration of distributed generator assets; (5) its processes and procedures for notifications of change of load and change of status; and (6) its procedures to ensure that Air Facility Registration Certificates for generation assets within NYISO were properly procured. These systemic issues led DA to recommend that EnerNOC develop a corporate-wide formal compliance program. EnerNOC agreed with the seven report findings and the twenty-two recommendations, and agreed to develop a formal, corporate-wide internal compliance program.

3. North American Electric Reliability Corporation

At NERC, DA conducted a performance audit evaluating NERC's budget formulation, administration, and execution, focusing on the costs and resources used to achieve program

[41] *ITC Holdings Corp.,* Docket No. PA10-13-000 (Sept. 30, 2011) (delegated letter order).

[42] *ITC Holdings, Corp.*, 139 FERC ¶ 61,112 (2012).

[43] ITC Holdings, Corp., Refund Report, Docket No. PA10-13-000 (filed Sept. 28, 2012).

[44] *EnerNOC, Inc.,* Docket No. PA11-20-000 (Jan. 13, 2012) (delegated letter order).

objectives.[45] DA identified eleven areas where performance could be enhanced and made forty-two recommendations to improve NERC's economy and efficiency. The findings related to three broad categories of concerns. The first was the level of detail at which NERC as the Electric Reliability Organization (ERO) kept its records for transparency and accountability to the Commission in its annual budgeting process. The findings in this first category related to NERC's budget process, its oversight of the REs' budgets, and its time and reporting systems. The second area of concern related to NERC's standards and procedures for ensuring that all costs incurred were just and reasonable. The audit report included findings related to NERC's support for the level of employee compensation, including retirement plans, the determination of an appropriate compensation mechanism for its Board members, and the manner in which NERC defined and implemented a "reasonableness" standard for employee expenses and rewards. The final area of concern related to NERC's functions and included findings related to its Critical Infrastructure Protection oversight duties, the scope of activities that should be funded under section 215 of the FPA, and the dual role of NERC as the ERO and the Electric Sector – Information Sharing and Analysis Center (a Department of Energy function assigned to NERC before NERC's selection as the ERO). NERC contested some of the audit findings and recommendations. Subsequently, the Commission commenced a paper hearing that is currently pending.

4. PNM Resources, Inc.

At PNM Resources (PNMR), DA evaluated compliance with the Commission's: (1) cross-subsidization restrictions on affiliate transactions; (2) accounting, recordkeeping, and reporting requirements; (3) the Uniform System of Accounts (USofA) for centralized service companies; (4) preservation of records requirements for holding companies and service companies; and (5) the FERC Form No. 60 requirements.[46] DA also evaluated PNMR's compliance with the conditions upon which the Commission granted authorization of the merger and acquisition of jurisdictional facilities.[47] Finally, DA evaluated compliance with its OATT requirements, Commission accounting regulations in the USofA, and the FERC Form No. 1 reporting regulations. The evaluation included PNMR's service company, PNMR Services Company, and its public utility, Public Service Company of New Mexico (PNM).

DA identified eight compliance findings, five applicable to PNM and three to PNMR, and made twenty-one recommendations for corrective action. DA's audit findings led to a $3.5 million reduction in PNM's utility plant account and the removal of $1.5 million in deferred income taxes.

5. Xcel Energy Services, Inc.

At Xcel, DA evaluated compliance with: (1) Order Nos. 679 and 679-A; (2) Commission regulations governing incentive-based rate treatment for transmission investments, and the conditions established in the Commission's December 21, 2007, order granting incentives, and accepting proposed rate formula modifications;[48] and (3) FERC-730, Report of Transmission Investment Activity, regarding the proper reporting and filing requirements for recovery of Commission-approved transmission incentive payments.[49] DA identified two areas of noncompliance. First, Xcel did not adequately review the rate formula template for the Northern

[45] *North American Electric Reliability Corp.,* Docket No. FA11-21-000 (May 4, 2012) (delegated letter order).

[46] *PNM Resources, Inc.*, Docket No. FA11-7-000 (Feb. 7, 2012) (delegated letter order).

[47] *See* Docket Nos. EC05-29-000, EC06-149-000, EC08-69-000, and EC08-71-000.

[48] *Xcel Energy Services, Inc.,* 121 FERC ¶ 61,284 (2007).

[49] *Xcel Energy Services, Inc.*, Docket No. PA11-11-000 (Jan. 5, 2012) (delegated letter order).

States Power Companies' 2010 true-up adjustment for accuracy before submitting it to the Midwest Independent System Operator (MISO). This resulted in a $10 million overstatement of rate base. In addition, Xcel used an incorrect percentage when calculating its pre-funded AFUDC, which increased its rate base by about $1 million. These errors overstated the 2010 revenue requirement by about $1.5 million. DA identified these errors during the course of the audit and Xcel was able to correct these errors before they impacted charges to transmission customers. The second area of noncompliance concerned Xcel's improper reporting of its FERC-730 for 2007-2010, and the late filing of two reports. Xcel accepted and has fully implemented all seven of DA's corrective actions related to these two areas of noncompliance. The audit helped prevent $1.5 million in improper charges from being recovered from ratepayers and improved the quality of data used for formula rate billings and reported in Xcel's FERC-730 filings.

6. Connecticut Light & Power Company

At Connecticut Light & Power (CL&P), DA evaluated compliance with the company's transmission formula rates under the ISO-NE OATT, transactions under the tariff, and accounting and reporting requirements in Part 101 of the Commission's regulations.[50] DA made two findings and ten recommendations. First, CL&P used depreciation rates approved by the Connecticut Department of Public Utility Control (DPUC) for the transmission portion of certain general plant accounts instead of the Commission-approved depreciation rates. The overall impact of using DPUC depreciation rates in 2009 and 2010 resulted in CL&P overstating depreciation expense by $12,329. DA recommended, among other things, that CL&P recalculate and book appropriate depreciation expenses, accumulated depreciation, and deferred income taxes for each transmission-related general plant asset by using the Commission-approved depreciation rates for all affected years in which CL&P used DPUC-approved rates. DA also recommended that CL&P establish procedures and controls to ensure that the amount of depreciation expense in its formula rate is determined based on Commission-approved depreciation rates.

DA also found that a total of $1,160,736 in expenses had been recorded in Account 426.5, Other Deductions, which pertained to promotion and strategies associated with public relations, and should not have been included in the formula rate calculation. However, the entire amount had been inappropriately identified in the footnotes to CL&P's FERC Form No. 1 income statement as public education expenses, and as such included in its formula rate. Since cost for promotion and strategies associated with public relations are not allowed in the formula rate, these amounts should not have been included. DA recommended that CL&P assess the impact of the overstatement on customer billings and issue refunds which, including interest, totaled $1,173,065.

7. Niagara Mohawk Power Corporation

At Niagara Mohawk, DA evaluated compliance with the USofA for public utilities, FERC Form No. 1 reporting requirements, and FERC Form No. 3-Q reporting requirements. DA identified eleven areas of noncompliance and made thirty recommendations. Six of the areas of noncompliance involved accounting and reporting issues that affected Niagara Mohawk's formula rate billings to wholesale customers. Niagara Mohawk agreed to refund amounts it collected inappropriately, modify its practices, establish controls and detailed written policies and procedures, and make appropriate correcting accounting entries. Niagara Mohawk is determining its refund obligation for these six areas of noncompliance. As part of this process, the audit required Niagara Mohawk to conduct three studies to ensure certain costs that were

[50] *Connecticut Light & Power Co.*, Docket No. FA11-15-000 (May 31, 2012) (delegated letter order).

incorrectly recovered from ratepayers are refunded, as appropriate. The other five areas of noncompliance involved various accounting misclassifications and numerous reporting items.

8. CenterPoint Energy Gas Transmission Company

At CenterPoint Energy Gas Transmission (CEGT), DA evaluated compliance with: (1) the requirement to file contracts with material deviations; (2) select portions of CEGT's FERC gas tariff, including governing penalties, balancing mechanisms, capacity allocation, and tracking mechanisms; (3) certain reporting requirements pursuant to Commission regulations, including portions of the FERC Form No. 2; and (4) North American Energy Standards Board (NAESB) standards.[51]

DA identified twelve areas of noncompliance: (1) refunding of penalty revenues; (2) accounting for storage under the inventory method; (3) accounting for cash-out transactions; (4) accounting for electric power costs; (5) accounting related to CEGT's fuel tracker; (6) accounting for excess shipper-supplied gas; (7) accounting for gas losses; (8) incorrect reporting on various pages of the FERC Form No. 2; (9) annual IT revenue crediting filing; (10) incorrect Index of Customers filings; (11) incorrect capacity reporting; and (12) incorrect NAESB postings. DA provided thirty recommendations, resulting in CEGT refunding $202,082 to its firm shippers.

9. Reliability Audits

During FY2012, DA coordinated the Commission's oversight of the Reliability Standards compliance auditing with staff from OER. The ERO has delegated to the REs the responsibility of conducting the required compliance audits of NERC and Commission approved standards. During these oversight audits, Commission staff from DA and OER ensure the adequacy of the RE audit process, procedures, and techniques, as well as sufficiency of the technical rigor employed in assessing the evidence presented by the registered entity. Commission staff provides a summary of its observations to NERC and the RE that conducted the audit in order to encourage sound practices, suggest needed improvements, and ensure consistency across REs. Commission staff participation in these audits furthers the Commission's statutory responsibility regarding the reliability of the nation's bulk power system through effective regulatory oversight, as established in the Energy Policy Act of 2005.

During FY2012, an important change occurred in the manner in which DA conducted certain compliance audits as a result of REs that are registered to perform reliability functions (*i.e.*, WECC, Florida Reliability Coordinating Council (FRCC) and Southwest Power Pool (SPP)) transferring the responsibility for conducting compliance oversight of their reliability functions from NERC to another RE. As a result, SERC Reliability Corporation became the Compliance Enforcement Authority (CEA) for both SPP and FRCC and Northeast Power Coordinating Council (NPCC) became the CEA for WECC. DA focused particular attention on compliance audits conducted under this new regime.

Operations and Planning Mandatory Standards Compliance Audits. During FY2012, DA and OER participated in RE audits of owners, users, and operators of the bulk power system pursuant to Order No. 693.[52] These audits evaluated compliance with Reliability Standards designed to ensure the reliable operation of the bulk power system through requirements related to, among

[51] *CenterPoint Energy Gas Transmission Co.*, Docket No. PA11-4-000 (June 22, 2012) (delegated letter order).

[52] *Mandatory Reliability Standards for the Bulk-Power System*, Order No. 693, 72 Fed. Reg. 16,416 (Apr. 4, 2007), FERC Stats. & Regs. ¶ 31,242 (2007), *order on reh'g*, Order No. 693-A, 120 FERC ¶ 61,053 (2007).

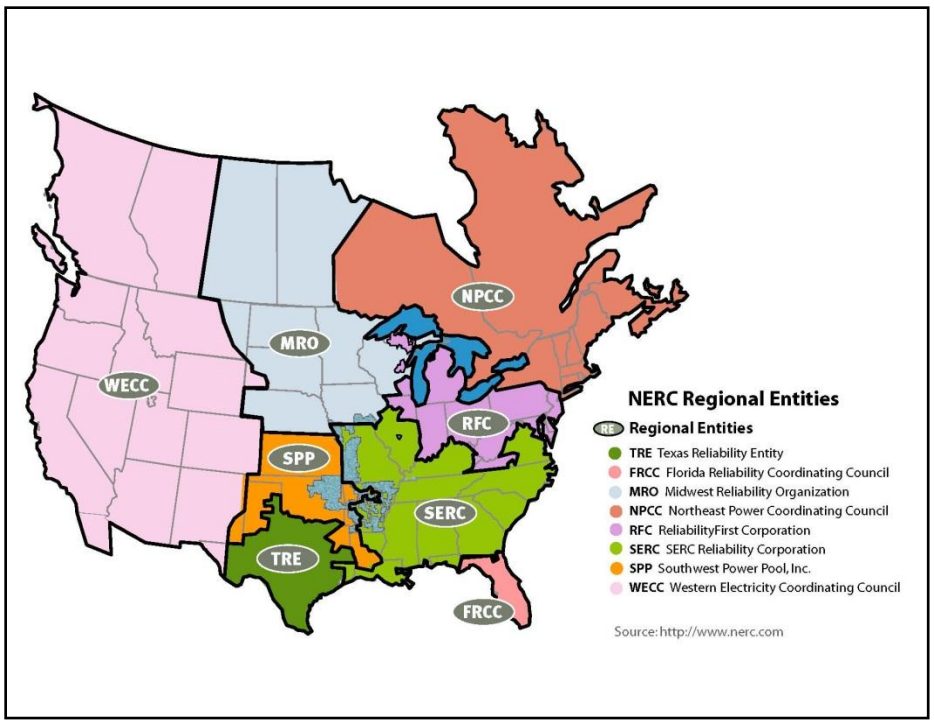
other areas, transmission planning and operation, vegetation management, and communications. Eight such audits were completed in FY2012:

- FRCC audit of the City of Homestead;
- RFC audit of Potomac Electric Power Company;
- SPP RE audit of Sunflower Electric Power Co-op;
- NPCC (as the CEA for WECC) audit of WECC as the Reliability Coordinator and Interchange Authority;
- FRCC audit of City of Vero Beach;
- SERC audit of Southern Company Services, Inc.;
- Texas RE audit of American Electric Power Service Corp. as agent for AEP Texas North Co., AEP Texas Central Co., and Public Service Co. of Oklahoma; and
- Midwest Reliability Organization (MRO) audit of Minnesota Power.

Critical Infrastructure Protection Mandatory Standards Compliance Audits. During FY2012, DA and OER participated in RE audits of owners, users, and operators of the bulk power system pursuant to Order No. 706.[53] These audits evaluate compliance with CIP Reliability Standards for the cyber and physical protection of Critical Cyber Assets identified as necessary to ensure the reliable operation of the Bulk Electric System. The following seven audits were completed in FY2012:

- Reliability*First* Corporation (RFC) audit of Duquesne Light Company;
- SERC (as the CEA for FRCC) audit of FRCC as the Reliability Coordinator;
- NPCC (as the CEA for WECC) audit of WECC as the Reliability Coordinator and Interchange Authority;
- SPP RE audit of Westar Energy;
- Texas RE audit of Center Point Energy;
- SERC audit of Tennessee Valley Authority; and
- MRO audit of Minnesota Power.

[53] *Mandatory Reliability Standards for Critical Infrastructure Protection*, Order No. 706, 73 Fed. Reg. 7368 (Feb. 7, 2008), 122 FERC ¶ 61,040 (2008), *order on reh'g,* Order No. 706-A, 123 FERC ¶ 61,174 (2008), *order on clarification,* Order No. 706-B, 126 FERC ¶ 61,229 (2009).



DA also conducts its own audits of REs and registered entities. As the Commission directed, DA conducted an audit of Southwest Power Pool, Inc. (SPP), addressing its responsibilities and performance as a Regional Entity (SPP RE). In its October 2011 audit report, DA found five issues relating to SPP RE's implementation of its Compliance Monitoring and Enforcement Plan (CMEP).[54] Specifically, DA staff identified weaknesses in the policies and procedures used to process mitigation plans, technical feasibility exception requests, and conflicts of interest for contractors. Further, DA staff identified a backlog of open violations in the SPP RE caseload and a lack of policies and procedures for SPP RE employees responsible for detecting and reporting issues specific to the performance of CMEP activities by SPP RE. The SPP RE General Manager and other SPP RE staff members conducted self-assessments in audit focus areas, and generally agreed with the audit team's fourteen recommendations for improved performance.

During FY2012, DA commenced audits of five additional REs: MRO, NPCC, RFC, SERC, and WECC.[55] These audits are evaluating the REs' budget formulation, administration, and execution, focusing on the costs and resources used to achieve program objectives. In addition, two of these audits (WECC and NPCC) are also examining the entity's responsibilities and performance as an RE.

[54] *Southwest Power Pool, Inc.*, Docket No. PA11-2-000 (Oct. 5, 2011) (delegated letter order).

[55] *Midwest Reliability Organization,* Docket No. FA12-14-000 (Apr. 10, 2012) (delegated letter order); *Northeast Power Coordinating Council, Inc.*, Docket No. PA12-10-000 (Oct. 28, 2011) (delegated letter order); *ReliabilityFirst Corporation*, Docket No. FA12-7-000 (Oct. 28, 2011) (delegated letter order); *SERC Reliability Corporation*, Docket No. FA12-6-000 (Oct. 28, 2011) (delegated letter order); *Western Electricity Coordinating Council*, Docket No. PA12-9-000 (Oct. 28, 2011) (delegated letter order).

The Commission-led audits of REs evaluate performance of, and compliance with, the requirements of Commission-approved mandatory Reliability Standards, focusing on Critical Infrastructure Protection (Order No. 706) and bulk power system operations and planning (Order No. 693). The entities being audited are Bonneville Power Administration, PJM, and the Salt River Project Agricultural Improvement and Power District. The audits are ongoing, but nearing completion.

D. Other Audit Matters

1. Transmission Incentives

ITC Great Plains, LLC and Northeast Utilities Service Company. At ITC Great Plains and Northeast Utilities Service Company (NUSCO), DA evaluated the companies' compliance with: (1) Order Nos. 679 and 679-A; (2) Commission regulations governing incentive-based rate treatment for transmission investments; (3) conditions established in Commission orders on transmission incentives for each company;[56] and (4) FERC-730 reporting and filing requirements.[57] In addition, DA also evaluated NUSCO's compliance with the requirements of its MBR authorization and EQR filing requirements. Altogether, DA identified two areas of noncompliance. DA determined that both companies had inaccurately reported actual capital expenditures in their FERC-730. In addition, DA determined that NUSCO reported incorrect Data Universal Numbering System numbers and used inconsistent customer company names in its EQR filings. DA provided one recommendation for ITC Great Plains and five recommendations for NUSCO. Both companies agreed to all recommendations.

2. Capacity Markets and Demand Response Programs

Viridity Energy, Inc. At Viridity, DA evaluated the compliance and performance of Viridity as a PJM market participant, according to the terms and conditions of PJM's OATT,[58] and the audit focused on tariff provisions relevant to Viridity's participation in PJM's Emergency and Economic Load Response Programs, which permit demand response resources to participate in PJM's capacity and energy markets, respectively. As part of the audit, DA also audited a sample of Viridity's assets to determine compliance with applicable tariff provisions. As a result of the audit, Viridity conducted an internal review of its program and identified a single area of noncompliance related to customer registration information submitted to PJM. This misreporting in customer registration led to a subsequent minor overpayment for participation by this customer in PJM's Economic Load Response Program. Although discovery of the overpayment occurred beyond the settlement period, Viridity refunded the overpayment to PJM. Audit staff recommended that Viridity increase its controls to ensure the accuracy of its future data submittals to PJM.

3. Independence Audit

California Independent Systems Operator. At CAISO, DA evaluated: (1) the independence of CAISO's governance structure and its operations from market participants; (2) CAISO's compliance with a select set of its responsibilities under its tariff, business practices, corporate bylaws, policies, codes of conduct, and so on; (3) CAISO's compliance with the Commission's

[56] *ITC Great Plains, LLC.*, 126 FERC ¶ 61,223 (2009); *Northeast Utilities Service Co.*, 124 FERC ¶ 61,044 (2008).

[57] *ITC Great Plains, LLC*, Docket No. PA11-14-000 (Mar. 26, 2012) (delegated letter order); *Northeast Utilities Service Company*, Docket No. PA11-13-000 (Dec. 8, 2011) (delegated letter order).

[58] *Viridity Energy, Inc.*, Docket No. PA12-15-000 (Aug. 6, 2012) (delegated letter order).

USofA for public utilities; (4) the FERC Form No. 1 Annual Report requirements for major electric utilities; and (5) the FERC Form No. 3-Q, quarterly financial report of electric utilities.[59]

DA identified eight areas of concern, two specifically related to independence. DA made nine recommendations designed to improve CAISO's performance, three of which strengthen CAISO's independence from market participants. Specifically, DA recommended that CAISO: (1) review and revise its policies and procedures used to ensure independence so they are consistent internally, with practices of other ISO/RTOs, and with Commission requirements; (2) revise its policy on employees accepting gifts from market participants; and (3) design better controls for monitoring potential conflicts of interest.

4. OATT

Arizona Public Service Company. At Arizona Public Service Company (APS), DA evaluated APS' compliance with the terms and conditions of its OATT.[60] DA identified six areas of noncompliance and made twenty recommendations for corrective actions. The areas of noncompliance involved: (1) non-filing and reporting of jurisdictional service agreements; (2) improper use of network transmission service with non-qualified network resources; (3) approval of deficient network transmission service; (4) incorrect determination of committed use for native load in Available Transfer Capability calculation; (5) improper firm third-party sales from designated network resources; and (6) insufficient documentation supporting designation of network resources.

One of the more significant areas of noncompliance involved APS' non-filing and reporting of jurisdictional service agreements. To date, APS has identified forty-five contracts with filing errors. It has corrected thirty contracts through EQR revisions, and filed the remaining fifteen agreements with the Commission.

5. Comprehensive Natural Gas Audits

Gulf South Pipeline, L.P. At Gulf South, DA evaluated Gulf South's compliance with: (1) certain information in the FERC Form No. 2 filed under Commission regulations; (2) NAESB standards pursuant to Commission regulations; (3) reporting requirements pursuant to Commission regulations; and (4) select portions of Gulf South's FERC gas tariff, including governing penalties and balancing mechanisms.[61]

DA identified ten areas of noncompliance: (1) accounting for system gas; (2) accounting for lost and unaccounted-for gas quantities; (3) accounting for fuel to others; (4) inability to verify accuracy of design capacity; (5) discrepancies in capacity data compared to other sources of data; (6) missing transactional postings; (7) updating design capacity on a timely basis; (8) FERC Form No. 2 filings; (9) NAESB business practices and electronic communication standards; and (10) accuracy of the Index of Customers filings. DA made thirty-two recommendations, which Gulf South did not contest.

Pipeline Postings. DA conducted ten audits of interstate natural gas pipeline companies' informational postings.[62] The audits evaluated the companies' compliance with 18 C.F.R. §

[59] *California Independent Systems Operator*, Docket No. PA11-16-000 (Oct. 17, 2011) (delegated letter order).

[60] *Arizona Public Service Co.*, Docket No. PA11-1-000 (Dec. 20, 2011) (delegated letter order).

[61] *Gulf South Pipeline, L.P.*, Docket No. PA11-3-000 (Apr. 2, 2012) (delegated letter order).

[62] *Dauphin Island Gathering Partners*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Destin Pipeline Co., L.L.C.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Empire Pipeline, Inc.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Gas Transmission Northwest Corp.*, Docket No.

284.12-13 and NAESB Business Practice Standards Version 1.9.[63] The audits focused on informational postings related to capacity, no-notice transportation, gas quality, notices, imbalances, transactional reports, Index of Customers, and tariff information. DA identified more than 500 posting errors involving incorrect data field labels and content, improper use of code values, and missing and non-functional navigational links. Each audit report contained one finding and three recommendations. Overall, these audits will improve the consistency and transparency of pipeline companies' informational postings.

6. Public Utility Holding Company Act and Affiliate Transactions

Dominion Resources, Inc., MidAmerican Energy Holdings Company, Integrys Energy Services, Inc., and Progress Energy, Inc. At Dominion Resources, MidAmerican Energy Holding Company (MEHC), Integrys and Progress Energy, DA evaluated the entities, along with their respective centralized service companies and associated companies, for compliance with the Commission's: (1) cross-subsidization restrictions on affiliate transactions; (2) USofA for centralized service companies; (3) preservation of records requirements for holding companies and service companies; and (4) FERC Form No. 60 requirements.[64]

Collectively, DA identified thirty areas of noncompliance related to: (1) misallocation of costs; (2) billing and recording of service company billings; (3) accounting for certain costs; (4) accounting misclassifications and errors; (5) reporting requirements; and (6) delinquent filings to the Commission. Some cost misclassifications and accounting errors resulted in ratepayer refunds. DA made sixty recommendations, collectively, related to the findings at these entities.

7. Formula Rates

Interstate Power and Light Company. At Interstate Power and Light Company (IPL), DA evaluated whether IPL calculated its fuel and purchase power formula rate in compliance with: (1) its RES-5 tariff on file with the Commission; (2) various accounts incorporated into the fuel and purchased power formula rate tariff; and (3) accounting regulations in the USofA.[65] Specifically, DA performed select tests of IPL's records to validate the accuracy of its wholesale fuel and purchased power formula rate. DA identified two areas of noncompliance: formula rate calculations and accounting for derivative instruments − hedges. DA made three recommendations. IPL agreed with the findings and recommendations.

Vermont Transco, LLC. At Vermont Transco (VTransco), DA evaluated whether VTransco complied with: (1) Schedule 21-VTransco and Schedule 9 of the ISO-NE Transmission, Markets, and Services Tariff, formerly known as ISO-NE's FERC Electric Tariff No. 3 and FERC Rate Schedule No. 1; (2) various accounts incorporated into its formula rate tariffs; (3)

PA11-22-000 (Dec. 20, 2011) (delegated letter order); *National Fuel Gas Supply Corp.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Northern Natural Gas Co.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Petal Gas Storage, L.L.C.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Southern Natural Gas Co.*, Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Texas Eastern Transmission*, L.P., Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order); *Transwestern Pipeline Co.,* Docket No. PA11-22-000 (Dec. 20, 2011) (delegated letter order).

[63] NAESB WGQ Business Practice Standards Booklets and NAESB WGQ Standards Books.

[64] *Dominion Resources, Inc.*, Docket No. FA11-4-000 (Sept. 20, 2012) (delegated letter order); *MidAmerican Energy Holdings Co.*, Docket No. FA11-3-000 (Jan. 5, 2012) (delegated letter order); *Integrys Energy Service, Inc.*, Docket No. FA10-4-000 (Dec. 20, 2011) (delegated letter order); *Progress Energy, Inc.*, Docket No. FA11-6-000 (Sept. 20, 2012) (delegated letter order).

[65] *Interstate Power and Light Co.*, Docket No. FA11-14-000 (Dec. 20, 2011) (delegated letter order).

accounting regulations in the USofA; and (4) transactions under the tariff.[66] DA identified two areas of noncompliance related to VTransco's calculation of its transmission revenue requirements with respect to accounting for the Bennington-Searsburg Line and its electric plant held for future use account. DA made six recommendations. One of these recommendations included a refund of $185,053 that resulted from VTransco overstating its rate base because it incorrectly included gross plant instead of net plant in its formula rate calculation.

8. Market-Based Rate Authority and Electric Quarterly Reports

Capital Power Corporation, ArcLight Capital Partners, LLC, and Cleco Corporation. At Capital Power, ArcLight Capital Partners (ArcLight), and Cleco, DA evaluated these entities and their affiliates to determine whether and how the companies complied with the requirements of the companies' MBR authorization and with EQR filing requirements.[67]

Collectively, DA identified twelve areas of noncompliance related to: (1) filing EQRs; (2) reporting of sales for resale in EQRs; (3) misreported data in EQRs; (4) inaccurate and inconsistent reporting of data in MBR filings; (5) compliance with Order No. 697; (6) price reporting; (7) change-in-status filings; and (8) aggregated data in EQRs. DA made twenty-five recommendations, collectively, related to its findings.

E. Significant Accounting Matters

The Commission requires that electric utilities, natural gas companies, centralized service companies, and oil pipelines subject to its jurisdiction keep financial and related records in accordance with the rules and regulations in the applicable USofA to aid in the establishment and monitoring of just and reasonable rates. DA develops and maintains uniform regulations and requirements for accounting, financial reporting, and preservation of records. In addition, DA advises the Commission on current accounting issues affecting jurisdictional industries, provides its accounting expertise to Commission program offices in developing Commission policies and proposed rulemakings, and advises the Commission on the disposition of electric and natural gas rate, merger, and natural gas certificate filings. In FY2012, DA reviewed approximately 250 filings to ensure that accounting was consistent with the applicable USofA.

DA also provides accounting advice to entities in the electric, gas, and oil industries subject to Commission accounting requirements, and participates in liaison meetings with these entities to stay abreast of current and emerging accounting and financial reporting issues. DA monitors and participates in projects initiated by the FASB, SEC, and IASB for issues that may impact the Commission or its jurisdictional entities.

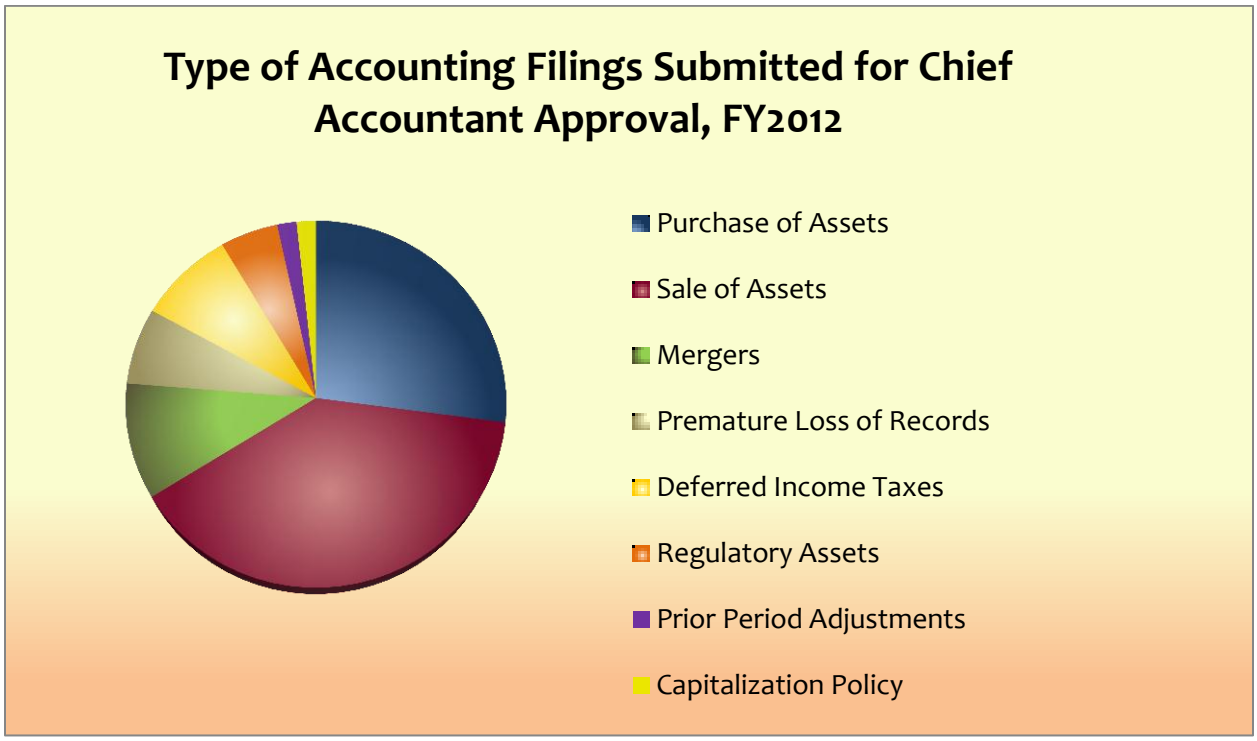
1. Requests for Approval of the Chief Accountant

In FY2012, the Chief Accountant responded to sixty-four accounting requests for approval submitted by jurisdictional entities. These requests spanned the breadth of Commission accounting and reporting requirements as well as regulations for electric, natural gas, oil, and centralized service companies. Such requests included statutorily required filings, issues of first impression, items of questionable interpretation, and implementation of new or evolving generally accepted accounting principles (GAAP). Many of these filings included accounting

[66] *Vermont Transco, LLC*, Docket No. FA11-16-000 (Dec. 8, 2011) (delegated letter order).

[67] *Capital Power Corp.*, Docket No. PA11-8-000 (Oct. 6, 2011) (delegated letter order); *ArcLight Capital Partners, LLC*, Docket No. PA11-7-000 (Feb. 29, 2012) (delegated letter order); *Cleco Corp.*, Docket No. PA11-9-000 (Oct. 6, 2011) (delegated letter order).

requests related to Commission-approved mergers, transfers of jurisdictional assets, prior period adjustments, deferred income taxes, regulatory assets, and capitalization policies.



2. Certificate Proceedings

In FY2012, the Chief Accountant reviewed thirty-three natural gas pipeline certificate applications. DA worked with the OEP, OGC and OEMR to review all items used to determine initial rates, including operation and maintenance expenses, depreciation, depletion, amortization, taxes, and return on investment to assure the Commission will set "just and reasonable" rates that are in the public interest. DA ensures that applicants follow the Commission's accounting rules and regulations related to AFUDC calculations, contributions in aid of construction, regulatory assets and liabilities, lease transactions, abandonments, and system gas accounting. DA's review of certificate applications is important because a certificate application contains, in part, cost and accounting information related to the construction and operation of natural gas facilities used to determine rates charged to customers.

3. Merger and Acquisition Proceedings

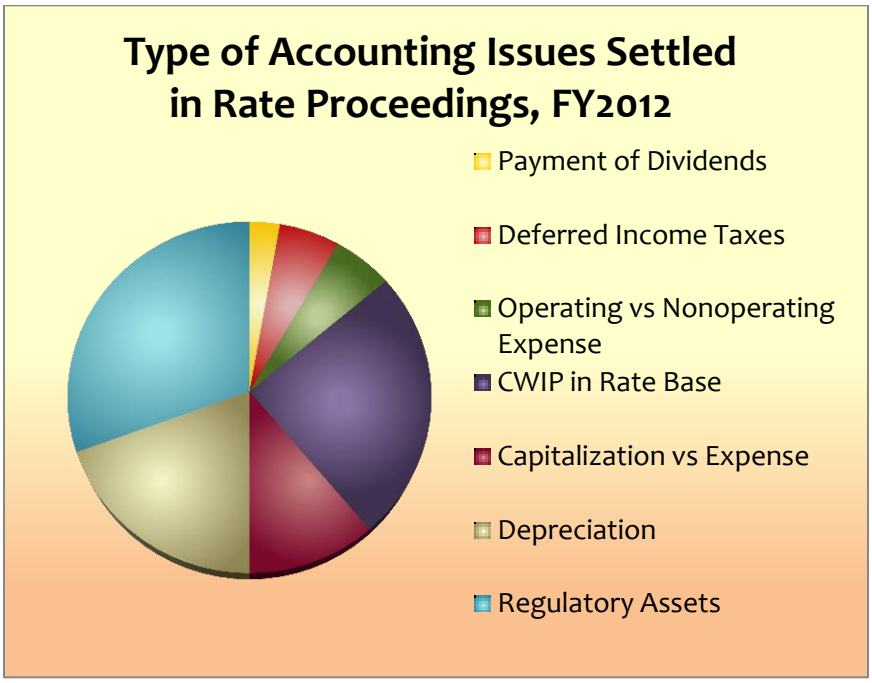
During FY2012, DA reviewed five merger filings and approximately 100 acquisition filings. DA works with OGC and OEMR in reviewing all merger and acquisition filings made under section 203 of the FPA. DA reviews the accounting entries filed by merger and acquisition applicants to ensure that these filings provide appropriate transparency to any rate implication resulting from such accounting for consideration by the Commission and all interested parties. The accounting review entails examining the proposed accounting for mergers and acquisitions for compliance with the Commission's regulations. DA also provides critical accounting direction to ensure accounting does not result in unjust and unreasonable rates.

DA provides direction on the proper accounting for merger-related costs, acquisition adjustments, and goodwill. In addition, DA ensures that filers maintain appropriate original cost

records of assets and addresses emerging accounting issues (*e.g.*, fair value accounting) for cost-of-service rate-regulated entities. For example, in recent merger proceedings DA has provided input on Commission orders which resulted in greater clarity on the accounting and rate treatment of merger related costs, acquisition premiums, and goodwill.[68] DA has observed in some acquisition filings complex accounting matters involving impairment of acquired assets and assets that have received differing regulatory treatments both under market-based and traditional cost-of-service recovery mechanisms. In these situations, DA ensures that the accounting is consistent with the Commission's ratemaking policies.

4. Rate Proceedings

During FY2012, DA participated in forty-three rate proceedings by providing accounting insight and support to OEMR in reviewing electric, natural gas, and oil pipeline rate filings before the Commission. Most significant, DA provided accounting direction on formula rate filings and transmission incentive rate filings. In formula rate filings, DA ensures that electric utilities follow the Commission's accounting requirements and that the costs are included in the formula rate appropriately. DA is concerned about new or changed accounting practices that may not be consistent with the Commission's accounting requirements, particularly those that alter the cost recovery of transmission rates without first requesting Commission authorization to make such a rate change. In transmission incentive rate filings, DA has provided accounting direction to the Commission for requests to include construction work in progress in an entity's rate base, to create a regulatory asset for pre-commercial costs and include a carrying charge, and to utilize accelerated depreciation to ensure that implementation of the rate incentives does not result in excess recoveries through formula rates. DA also advises the Commission when new accounting pronouncements, from FASB and others, involve issues that may have an effect on ratemaking. DA's input on these and other matters ensures uniform accounting and financial reporting for new and emerging issues, and aids in the development of just and reasonable rates.



[68] *See e.g.*, *Exelon Corp. and Constellation Energy Group, Inc.*, 138 FERC ¶ 61,167 (2012) (order conditionally authorizing merger and disposition of jurisdictional facilities).

5. International Financial Reporting Standards

DA continues to actively participate in matters related to the potential incorporation of International Financial Reporting Standards (IFRS) into the financial reporting system of publicly traded companies in the United States. IFRS is a body of global accounting standards that the IASB established and that the vast majority of industrialized countries have used for financial reporting. The potential incorporation of IFRS in U.S. financial reporting is very important to the Commission and its regulated entities because the Commission's accounting regulations are based on U.S. GAAP, and many accounting principles in IFRS differ from those in U.S. GAAP.[69] The most significant divergence from U.S. GAAP involves the lack of an IFRS accounting standard for the economic effects of regulation, principally, regulatory assets and liabilities.

The SEC has the ultimate responsibility for deciding whether, when, and how to adopt IFRS for financial reporting in the United States. The SEC has promoted a single set of high-quality, globally accepted accounting standards and in 2010 directed its staff to develop and execute a work plan to aid the SEC in evaluating the implications of incorporating IFRS in the United States. To execute the work plan, SEC staff performed research, sought comments from stakeholders, and conducted outreach to constituents, which provided several opportunities for the Chief Accountant to articulate the concerns of the Commission and its regulated entities related to IFRS.[70] In July 2012, SEC staff issued its Final Staff Report regarding the work plan for consideration in incorporating IFRS into the U.S. financial reporting system.[71] Among other matters, the SEC Staff Report discussed the potential effects of IFRS on U.S. regulators, including energy regulators. The SEC Final Staff Report included many concerns the Commission's Chief Accountant provided to the SEC staff and acknowledged an international accounting standard to recognize regulatory assets and liabilities is much needed. However, the SEC Final Staff Report did not provide a recommendation on whether to incorporate IFRS in the United States. The SEC has stated that such a decision will follow, but did not provide a time frame for the decision.

The Chief Accountant has also continued to be engaged with the IASB. In November 2011, the Chief Accountant submitted comments to the IASB's initial agenda consultation, which sought input on its strategic direction in setting the IASB's work plan and the projects and areas of financial reporting to which it should give priority. The Chief Accountant recommended that the IASB undertake a medium-term project to address the accounting for regulatory assets and liabilities, and stressed the value of such a standard for regulators, regulated entities, and investors. As a result of these comments and other similar comments from U.S. rate-regulated entities, the IASB decided in May 2012 to address regulatory assets and liabilities as a priority project.[72] The Chief Accountant intends to participate in this project on regulatory assets and

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[69] U.S. GAAP includes various standards, conventions, and rules for recording and summarizing transactions and in the preparation of financial statements. GAAP was first set forth by the Accounting Principles Board of the American Institute of Certified Public Accountants, which was superseded by the Financial Accounting Standards Board in 1973. GAAP has been the standard for accounting in the United States for more than half a century.

[70] The Chief Accountant participated in the SEC Work Plan through submitting white papers and comment letters, attending meetings with SEC staff, and participating in public roundtable discussions.

[71] Sec. Exch. Comm'n, Office of the Chief Accountant, Work Plan for the Consideration of Incorporating International Financial Reporting Standards into the Financial Reporting Standards for U.S. Issuers, (2012) *available at* www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf.

[72] Concerns that the Chief Accountant and others raised are encompassed in the IASB's project entitled Rate-regulated Activities.

liabilities as it develops.

Finally, DA continues to be actively involved in ongoing discussions with the regulated community, state regulators, and other stakeholders on the potential impact of adopting IFRS on Commission accounting regulations and its regulated entities. DA also continues to communicate these concerns to Commissioners and Commission staff.

6. Energy Storage Assets

On June 22, 2012, the Commission issued a Notice of Proposed Rulemaking (NOPR) to solicit comments on proposed revisions to certain aspects of its current MBR regulation, ancillary services requirements under the pro forma OATT, and accounting and reporting requirements for energy storage assets.[73] DA provided technical assistance to other program offices to develop proposed revisions to the Commission's accounting and reporting requirements pertaining to the Commission's oversight of jurisdictional services from new energy storage assets. Energy storage assets can have operating characteristics of each traditional primary business function – production, transmission, and distribution – and some may be capable of performing multiple functions simultaneously.[74] Accordingly, entities using energy storage assets may seek multiple methods of cost recovery for their investments in and use of a single energy storage asset to provide various utility services. The Commission proposed accounting and financial reporting changes because it determined that the current requirements do not provide sufficiently transparent information on the activities and costs of new energy storage operations. The transparency improvements achieved through revisions to the existing accounting and reporting requirements will enhance the Commission's and other form users' ability to make a meaningful assessment of cost of service and rates of public utilities using energy storage technologies in the provisioning of utility services, and will enable the Commission and others to better monitor for cross-subsidization.

[73] *Third-Party Provision of Ancillary Services; Accounting and Financial Reporting for New Electric Storage Technologies*, 139 FERC ¶ 61,245 (2012).

[74] *Id.*

DIVISION OF ENERGY MARKET OVERSIGHT

A. Overview

The Division of Energy Market Oversight within Enforcement is responsible for monitoring and overseeing the nation's wholesale natural gas and electric power markets. Market Oversight continuously examines and monitors the structure and operation of these markets to identify market anomalies, flawed or inadequate market rules, tariff and rule violations, and other unlawful behavior. Staff performs daily oversight of the nation's wholesale natural gas and electric markets and related fuel and financial markets, identifying market events and trends. Market Oversight analyzes and reports its observations to the Commission and, as appropriate, to the public, and proposes policy options and regulatory strategies for addressing the issues identified. Staff assesses factors that relate to the competitiveness, fairness, and efficiency of wholesale energy markets. Market Oversight administers, analyzes, and ensures compliance with the filing requirements for EQRs and various Commission financial forms. Market Oversight advises the Commission on the efficacy of its current regulatory policies in light of evolving energy markets and ensures the Commission has the information needed to effectively administer and monitor those markets.

B. Market Monitoring

Market Oversight staff continuously examines the structure, operation, and interaction of natural gas and electric markets. On an ongoing basis, Market Oversight staff accesses data from a variety of sources to review market fundamentals and emerging trends.

As developments warrant, Market Oversight staff initiates projects designed to evaluate market trends, and to assess participant behavior.Staff also presents analyses at Commission meetings. During FY2012, such analyses included the following.

1. 2011 State of the Markets Report, April 19, 2012

Each year, Market Oversight presents a State of the Markets report assessing the significant events of the past year. In 2011, staff observed that natural gas production reached an all-time record, surpassing levels last seen in the 1970's. Growing supply outpaced demand, which led to low natural gas prices not seen since the early 2000's and record high natural gas storage going into the 2011/2012 winter. The electric markets consequently experienced low prices from these lower fuel costs combined with stable demand. Changes in the pricing relationship between natural gas and coal-fired generators caused a fundamental shift in the utilization of these plants, with natural gas plant production increasing and coal plant output falling.[75]

2. Seasonal Market Assessments

Market Oversight prepares seasonal assessments presented at Commission meetings and made available to the public on the Commission website. In FY2012, Market Oversight staff presented the following assessments.

2011/2012 Winter Energy Market Assessment, October 20, 2011. Market Oversight staff presented the outlook for natural gas markets and noted that market conditions going into the winter were generally positive. Despite a 2.6% increase in natural gas demand for power production, prices remained among the lowest in the past decade due to continued production

[75] This presentation is available at http://www.ferc.gov/market-oversight/reports-analyses/st-mkt-ovr/som-rpt-2011.pdf.

growth and new pipelines transporting gas from the producing areas to consumers. Gas-fired electric generation benefited from the lower gas prices, raising expectations for continued demand growth from this sector in the upcoming winter.[76]

Summer 2012 Energy Market and Reliability Assessment, May 17, 2012. This assessment reviewed the outlook for the electric market for the coming summer. The Office of Electric Reliability contributed a summary of NERC's market review, which raised little concern for reliability for the coming season. On the market side, staff examined electric grid operations and electricity market prices, particularly in Southern California and the San Diego area, given the outage of two San Onofre nuclear units. Staff stated that the situation warranted close attention if the two units were to remain offline during high load periods during the summer. Staff further stated that the generation supply in Texas could be strained should the state experience a hot summer similar to 2011.[77]

3. Market Oversight's Energy Primer: A Handbook of Energy Market Basics

In FY2012, Market Oversight released its *Energy Primer*. The *Primer* explores the workings of the wholesale markets for the electric and gas industries as well as energy-related financial markets. The *Primer* gives the reader a comprehensive overview of both gas and electric markets while going into detail on specific market product segments. Along with a national perspective, the *Primer* also looks at regional and local markets. In addition to examining supply and demand in the gas market, the *Primer* covers trends in shale gas, liquefied natural gas (LNG), and end-user consumption. In the electric markets, each of the RTOs (and an overview of their market segments) and non-RTO regions is discussed. The financial markets chapter covers trading mechanisms and products related to natural gas and electricity. Finally, the *Primer* includes a chapter broadly discussing manipulation.

C. Outreach and Communication

Market Oversight makes available to the public its analyses by posting reports on the Market Oversight website and in monthly snapshot presentations. Staff also briefs visiting industry participants, state and federal officials, and foreign delegations.

1. Website

Market Oversight publishes data and analyses on the Market Oversight website, at http://www.ferc.gov/market-oversight/market-oversight.asp, organized into pages for (a) national overviews of electricity and natural gas markets and (b) ten regional electricity and five regional natural gas markets. The regional market pages provide charts, tables, and maps displaying market characteristics and outcomes. The Market Oversight website also has information on several other relevant markets, including liquefied natural gas (LNG), coal, and emissions markets.

[76] This presentation is available at http://www.ferc.gov/market-oversight/reports-analyses/mkt-views/2011/10-20-11.pdf.

[77] This presentation is available at http://www.ferc.gov/market-oversight/reports-analyses/mkt-views/2012/05-17-12.pdf.

2. Snapshot Calls

Market Oversight holds monthly conference calls with representatives of state agencies in four main regions of the country: Northeast, Midwest and SPP, Southeast, and West. These calls provide a current "snapshot" of energy markets.

Regional Snapshot Reports are compiled monthly and serve as the basis for discussion on the calls. The reports include data on electricity, natural gas, LNG, weather, and other market-affecting developments. In addition, the Snapshot Report occasionally incorporates reports on special topics. Snapshot Reports are available on the Market Oversight website at http://www.ferc.gov/market-oversight/mkt-snp-sht/mkt-snp-sht.asp, and are archived back to 2007.

3. Domestic and Foreign Delegation Briefings

Market Oversight periodically hosts visitors, including foreign and domestic delegations of regulators and industry participants, interested in energy markets and how staff monitors these markets. In FY2012, Market Oversight conducted a number of briefings in the Market Monitoring Center (MMC), including twenty-three domestic briefings to Congressional delegations, groups of delegates from federal or state agencies, delegations from industry, and eleven presentations to foreign delegations.

Market Oversight also briefs new Commission employees, summer interns, and special visitors on how Market Oversight maintains constant monitoring of market fluctuations and manages the Market Monitoring Center resources and applicable data to support oversight functions.

D. Forms Administration and Filing Compliance

Market Oversight staff administers and ensures compliance with the Commission's filing requirements. The Commission requires companies subject to its jurisdiction to submit annual and quarterly reports regarding jurisdictional sales, financial statements, and operational data. The Commission uses these reports for analyses, including evaluation of whether existing rates continue to be just and reasonable. Industry participants also use these reports for a variety of business purposes. Accordingly, accurate reporting is a critical aspect of monitoring markets.

Electric Quarterly Reports

Section 205 of the FPA, 16 U.S.C. § 824d (2006), and 18 C.F.R. Part 35 (2012), require, among other things, that all rates, terms, and conditions of jurisdictional service be filed with the Commission. In Order No. 2001, the Commission revised its public utility filing requirements requiring public utilities, including power marketers, to file EQRs summarizing the contractual terms and conditions in their agreements for all jurisdictional services (including market-based power sales, cost-based power sales, and transmission service) and providing transaction information (including rates) for short-term and long-term power sales during the most recent calendar quarter.[78]

[78] *Revised Public Utility Filing Requirements,* Order No. 2001, FERC Stats. & Regs. ¶ 31,127 (2002), *reh'g denied,* Order No. 2001-A, 100 FERC ¶ 61,074 (2002), *reh'g denied,* Order No. 2001-B, 100 FERC ¶ 61,342 (2002), *order directing filing,* Order No. 2001-C, 101 FERC ¶ 61,314 (2002), *order directing filing,* Order No. 2001-D, 102 FERC ¶ 61,334 (2003), *order refining filing requirements,* Order No. 2001-E, 105 FERC ¶ 61,352 (2003), *order on clarification,* Order No. 2001-F, 106 FERC ¶ 61,060 (2004), *order revising filing requirements,* Order No. 2001-G, 120 FERC ¶ 61,270 (2007), *order on reh'g and clarification,* Order No. 2001-H, 121 FERC ¶ 61,289 (2007), *order revising filing requirements,* Order No. 2001-I, FERC Stats. & Regs. ¶ 31,282 (2008).

Commission staff reviewed nearly 7,300 EQR submittals from over 1,500 individual respondents. Commission staff determines whether sellers have timely complied with the requirements set forth in Order No. 2001 and whether the data is accurate and reliable. During FY2012, Commission staff contacted nearly 500 non-compliant filers and assisted these filers to come into compliance with Commission requirements. The vast majority of these issues were resolved and, as appropriate, the filings were revised to address staff's concerns. When necessary, Market Oversight advises the Commission on remedial action to be taken in response to uncorrected EQR deficiencies. On January 31, 2012, the Commission issued an order announcing its intent to revoke the market-based rate authority of eight public utilities should the utilities fail to comply with EQR filing requirements within fifteen days of the issuance of the order.[79] Those utilities failed to meet this compliance deadline and the Commission revoked their market-based rate authority and terminated their electric market-based rate tariffs.[80]

E. Agenda Items and Rulemakings

Market Oversight advises the Commission on the efficacy of its current regulatory policies in light of evolving energy markets and ensures the Commission has the information needed to administer and monitor the markets effectively. During FY2012, Market Oversight staff continued to support Commission efforts to increase electric market transparency under section 220 of the FPA. Market Oversight continuously reviews the monitoring program to ensure that it is comprehensive and systematic, and also reviews reporting requirements to ensure that appropriate and accurate information is collected. Market Oversight seeks to enhance market transparency and efficiency while balancing the regulatory burden on market participants. As such, Market Oversight initiated, or provided significant support for, the following.

1. Revisions to Electric Quarterly Report Filing Process

On June 21, 2012, the Commission issued a NOPR to change the process for filing EQRs.[81] The current EQR filing mechanism uses Microsoft Visual FoxPro, which Microsoft has discontinued. Visual FoxPro also is constrained by data size limitations that will soon restrict the Commission's ability to add data fields in the EQR. The Commission, therefore, proposed a new filing system that would provide EQR filers with two new options for filing EQRs: a web-based interface or an Extensible Mark-Up Language (XML) format.

The Commission proposed that any changes to the process for filing EQRs would apply to EQR filings beginning with the third quarter 2013 EQR, providing data for July through September 2013. The Commission also convened a staff-led technical conference on July 11, 2012, to demonstrate the two new options for filing EQRs to industry participants and to assist participants in preparing their comments to the NOPR.

2. Revisions to FERC Form No. 6

On September 20, 2012, the Commission amended the instructions on page 700 of FERC Form No. 6 (Form 6) to ensure that oil pipelines report interstate-only barrel and barrel-mile data

[79] *Electric Quarterly Reports*, 138 FERC ¶ 61,071 (2012).

[80] *Electric Quarterly Reports*, Docket No. ER02-2011-017, *Notice of Revocation of Market-Based Rate Tariff*, February 16, 2012.

[81] *Revisions to Electric Quarterly Report Filing Process*, *Notice of Proposed Rulemaking*, 77 Fed. Reg. 39,447 (Jul. 3, 2012), 139 FERC ¶ 61,234 (2012).

on lines (11) and (12) of page 700 and not a combination of interstate and intrastate throughput.[82] The Commission directed pipelines that reported combined interstate and intrastate data in any field on lines (1) through (12) of page 700 of their 2010 Form 6 or page 700 of their 2011 Form 6 to file, within 90 days of the final rule's publication in the Federal Register, revised page 700 data containing only interstate data for the years 2009, 2010, and 2011. Market Oversight worked with OGC and OEMR in providing technical review of changes to the Form.

[82] *Revision to Form No. 6*, 77 Fed. Reg. 59,739 (Oct. 1, 2012), 140 FERC ¶ 61,218 (2012).

DIVISION OF ANALYTICS AND SURVEILLANCE

A. Overview

The Commission created the Division of Analytics and Surveillance in February 2012. DAS develops surveillance tools, conducts surveillance, and analyzes transactional and market data to detect potential manipulation, anticompetitive behavior, and other anomalous activities in the energy markets. DAS consists of four branches that focus on three areas: (1) natural gas surveillance; (2) electric surveillance; and (3) transactional analysis. The analysts and economists in DAS participate in investigations with attorneys from DOI, providing detailed transactional analysis, market event analysis, and subject matter expertise. As part of its surveillance function, DAS determines what information is necessary to assess and oversee the energy markets. Using that information, DAS develops and refines surveillance tools to perform continuous surveillance and analysis of market participant behavior, economic incentives, operations, and price formation on both the natural gas and electric markets, to detect anomalous activities in the markets and identify potential investigative subjects.

In FY2012, the Commission issued two final rules that greatly enhance DAS's ability to conduct surveillance of the electric markets and to analyze individual market participant behavior, Order Nos. 760 and 768.

Order No. 760. The Commission issued Order No. 760, entitled *Enhancement of Electricity Market Surveillance and Analysis through Ongoing Electronic Delivery of Data from Regional Transmission Organizations and Independent System Operators*, on April 19, 2012.[83] This final rule amends the Commission's regulations to require each jurisdictional RTO/ISO to electronically deliver to the Commission, on an ongoing basis and in a form and manner consistent with its own data collection and acceptable to the Commission, data related to the markets the RTOs/ISOs administer. Specifically, this data includes physical and virtual bids and offers, market awards, resource outputs, marginal cost estimates, shift factors, financial transmission rights, internal bilateral contracts, uplift, and interchange pricing.

Order No. 768. The Commission issued Order No. 768, entitled *Electricity Market Transparency Provisions of Section 220 of the Federal Power Act*, on September 21, 2012.[84] This final rule amends the Commission's regulations, pursuant to section 220 of the FPA, to facilitate price transparency in markets for the sale and transmission of electric energy in interstate commerce by requiring market participants that are excluded from the Commission's jurisdiction under FPA section 205, and have more than a *de minimis* market presence, to file EQRs with the Commission. The rule also revises the existing EQR filing requirements applicable to market participants in the interstate wholesale electric markets by adding new fields for: (1) reporting the trade date and the type of rate; (2) identifying the exchange used for a sales transaction, if applicable; (3) reporting whether a broker was used to consummate a transaction; (4) reporting electronic tag (e-Tag) ID data; and (5) reporting standardized prices and quantities for energy, capacity and booked-out power transactions. In addition, the rule also standardizes the unit for reporting energy and capacity transactions, omits the time zone from the contract section, and eliminates the Data Universal Numbering System requirement.

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[83] *Enhancement of Electricity Market Surveillance and Analysis through Ongoing Electronic Delivery of Data from Regional Transmission Organizations and Independent System Operators*, Order No. 760, 139 FERC ¶ 61,053 (2012).

[84] *Electric Market Transparency Provisions of Section 220 of the Federal Power Act,* Order No. 768, 140 FERC ¶ 61,232 (2012).

B. Natural Gas Surveillance

The Natural Gas Surveillance Branch within DAS conducts surveillance and analysis of physical natural gas market behavior and related financial markets to detect potential manipulation and anti-competitive behavior. Natural Gas Surveillance developed and implemented analytical tools, or "screens," that use publicly available data including trade prices, volumes, times, and other transaction characteristics, to detect anomalous activity. The screens cover the majority of physical and financial trading hubs in the United States. The screens alert staff to a variety of market conditions and market participant actions, such as price changes, volume levels, timing of trades, and decoupling of financial, physical, and relative valuations, among other things.

When a screen issues an alert, staff conducts a series of analyses to gain information about the activity that caused the screen alert. First, staff compares the trading to that at other hubs and reviews supply, demand, pipeline utilization, operational notices, and physical and financial trading to determine whether there is a fundamentals-based explanation for the screen alert. If these follow-up analyses fail to explain the screen alert, staff obtains granular transactional data to perform a more in-depth analysis of the specific trading behavior underlying the alert. Under some circumstances, staff will also contact the market participant for additional transactional details or explanations of the trading activities to better understand the purpose of the transactions. If staff continues to be concerned about the market activities underlying the screen alert, DAS will recommend that DOI open an investigation. When surveillance inquiries develop into investigations, DAS staff become part of the investigative team.

C. Electric Surveillance

The Electric Surveillance Branch within DAS analyzes and identifies anomalies and potential market manipulation in the electric markets. The Electric Surveillance Branch regularly accesses data from a variety of sources to review market fundamentals and screen for emerging trends. During FY2012, staff ran monthly screens to identify market participants' financial transmission rights positions that benefited from persistent locational marginal price (LMP) spreads. In addition, staff designed and developed analytic tools and screens for (i) determining uneconomic and unusually profitable virtual transactions by node, zone, and constraint; (ii) detecting day-ahead market congestion manipulation that would benefit FTR and financial swap positions; and (iii) identifying anomalies in physical offer patterns.

In addition, throughout FY2012, the Electric Surveillance Branch worked to develop and improve its surveillance capabilities by identifying and gaining access to new data sources and conducting outreach. In August 2012, the Commission began receiving data under Order No. 760 from the RTOs/ISOs on an ongoing basis. Electric Surveillance is using the data, which provide additional market-participant level details from each organized market, to enhance its existing screens and to develop new screens. Staff also conducted extensive outreach to the MMUs of each RTO and ISO during FY2012, which involved site visits to each ISO/RTO and MMU and discussions of their surveillance screens and techniques.

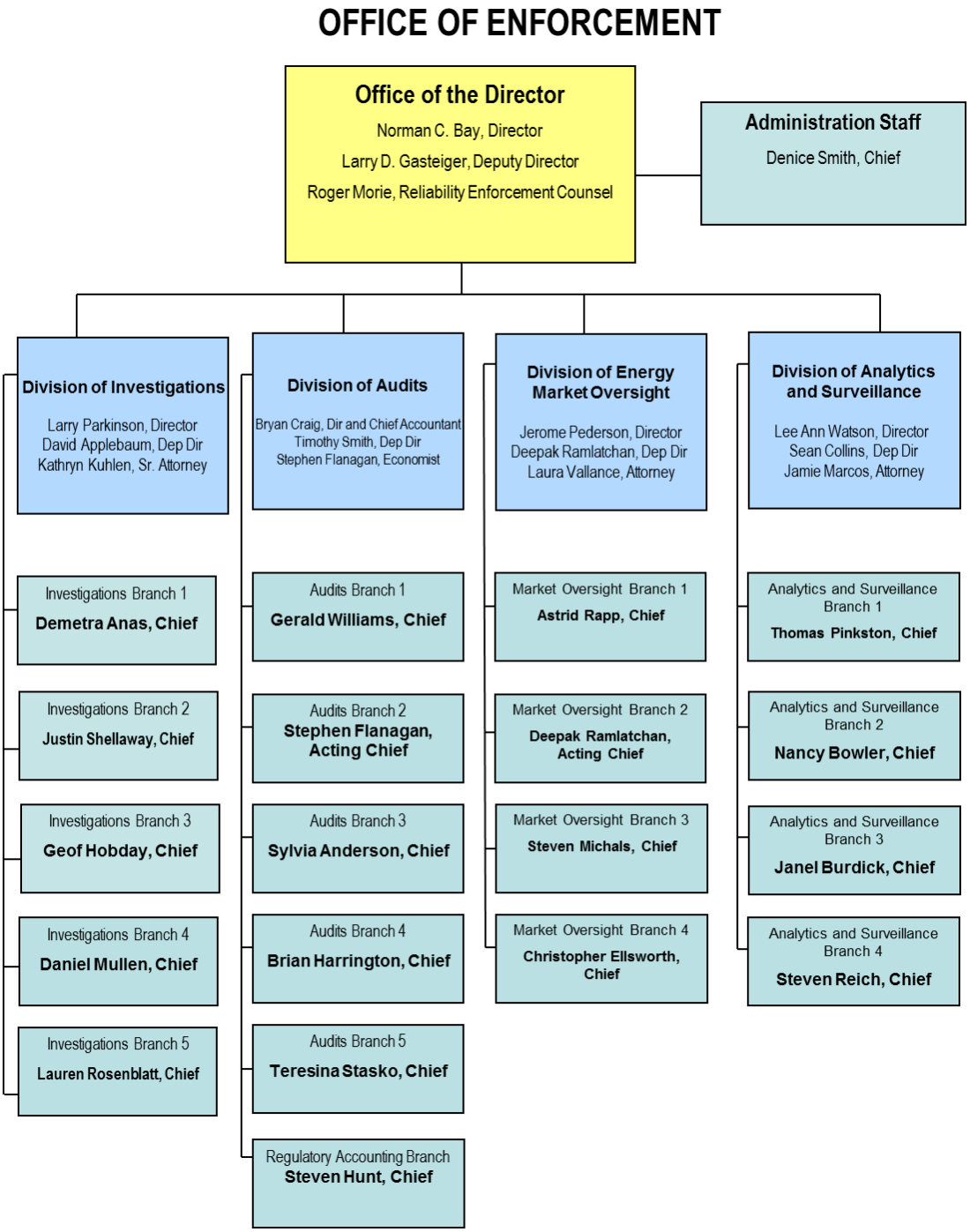
D. Analytics

The Analytics Branches within DAS have worked on more than 20 investigations since the creation of DAS in February 2012, some of which are discussed above in the DOI section. These investigations typically involve allegations of manipulation in the Commission-jurisdictional electric and natural gas markets or violations of tariff provisions that are intended to foster open, competitive markets. DAS's activities in investigations generally include: (1) assessing market conditions during periods of suspected manipulation; (2) identifying patterns of market activity that could indicate market manipulation; (3) identifying time periods in which potentially manipulative activities occurred; and (4) fully reconstructing and analyzing companies' trading portfolios. Upon completion of the analytical process, staff develops data-based explanations to inform the structure and substance of further investigation, settlement discussions, and Commission actions. Additionally, staff calculates the amount of unjust profits resulting from violations and assists with formulating a civil penalty recommendation under the Commission's penalty guidelines.

CONCLUSION

The information in this Report is provided to promote transparency and to encourage entities subject to Commission requirements to develop strong internal compliance programs. As discussed in this Report, Enforcement promotes compliance with the Commission's statutes, orders, rules, and regulations by investigating a wide variety of matters, auditing regulated entities for both compliance and performance issues, and actively overseeing the gas and electric markets to assist the Commission in ensuring reliable, efficient, and sustainable energy for consumers. The DOI will continue to focus its efforts on keeping markets transparent and competitive and helping to ensure the reliability of the bulk power system. The DA will work closely with entities to improve compliance, while Market Oversight will examine and monitor the structure and operation of natural gas and electric markets. The newly-created DAS will conduct surveillance and analyze transactional and market data to detect potential manipulation, anticompetitive behavior, and other anomalous activities in the energy markets.

APPENDIX A: OFFICE OF ENFORCEMENT ORGANIZATIONAL CHART



APPENDIX B: FY2012 CIVIL PENALTY ENFORCEMENT ACTIONS[85]

Subject of Investigation and Order Date	Total Payment	Explanation of Payments and Compliance Plans
In re Missouri Gas Energy, 140 FERC ¶ 61,135 (August 23, 2012)	$35,000 Civil Penalty	Civil penalty plus compliance monitoring resulting from violation of certain capacity release policies, 18 C.F.R. section 284 (posting and bidding requirements), the shipper-must-have-title requirement, and the prohibition against buy/sell transactions.
In re Vista Energy Marketing, L.P. 139 FERC ¶ 61,154 (May 24, 2012)	$350,000 Civil Penalty; two-years of market participation restrictions	Civil penalty plus a two-year restriction on market participation for Vista Energy and Michael P. Whalen, Jr., resulting from violations of order granting Vista MBR authority and 18 C.F.R. § 35.41(b) (prohibition of submission of false or misleading information or the omission of material information).
Constellation Energy Commodities Group, Inc., 138 FERC ¶ 61,168 (March 9, 2012)	$135,000,000 Civil Penalty; $110,000,000 Disgorgement	Civil penalty, disgorgement, and compliance monitoring, resulting from violation of 18 C.F.R. § 1c.2 (prohibition of electric energy market manipulation) and 18 C.F.R. § 35.41(b) (prohibition of submission of false or misleading information or the omission of material information).
Xcel Energy, Inc., 138 FERC ¶ 61,026 (January 17, 2012)	$2,000,000 Civil Penalty	Civil penalty and compliance monitoring resulting from the misuse of network transmission service in violation of the OATT.
In re Joseph Polidoro, 138 FERC ¶ 61,018 (January 11, 2012)	$50,000 Civil Penalty; two-year ban from participation in PJM's Demand Response markets	Civil penalty and two-year ban from participation in PJM's Demand Response markets resulting from violations of 18 C.F.R. § 1c and various PJM OATT provisions (1.7.4(a) and (d), 1.7.20(a), 1.8.2, and 3.3A.5(c) of Attachment K, sections A(2), (3) and (7) and provision I of Attachment DD-1).
ConocoPhillips Company, 138 FERC ¶ 61,004 (January 4, 2012)	$545,000 Civil Penalty; $3,174,900 Disgorgement	Civil penalty, disgorgement, and compliance monitoring resulting from violations of 18 C.F.R. § 1c.1 (capacity release policies), 18 C.F.R. § 284.8 (posting and bidding requirements), the shipper-must-have-title requirement, and a single violation of the prohibition of buy/sell transactions.

[85] A list of all EPAct 2005 civil penalty orders is available at http://www.ferc.gov/enforcement/civil-penalties/civil-penalty-action.asp.

Atmos Energy Corporation, 137 FERC ¶ 61,190 (December 9, 2011)	$6,364,029 Civil Penalty; $5,635,971 Disgorgement	Civil penalty and disgorgement resulting from violations of 18 C.F.R. § 1c.1 (capacity release policies), 18 C.F.R. § 284.8 (posting and bidding requirements), and the shipper-must-have-title requirement.
PacifiCorp, 137 FERC ¶ 61,176 (December 1, 2011)	$3,925,000 Civil Penalty ($1,962,500 to each FERC and NERC)	Civil penalty, reliability enhancement measures, and compliance monitoring resulting from multiple violations of reliability standards related to its functions as a Balancing Authority and Transmission Operator, surrounding a February 14, 2008 disturbance, including: BAL-002-0, R4, R6; EOP-001-0, R1, R8; EOP-002-0, R1, R7; EOP-002-2, R1, R2, R5, R6, R7; EOP-003-1, R1, R8; PER-001-0, R1; PER-002-0, R1; PRC-005-1, R2; PRC-008-0, R2; PRC-011-0, R2; PRC-017-0, R2; PRC-STD-005, WR1; TOP-001-1, R2, R8; TOP-004-1, R1, R2, R4; and WECC BAL-STD-002-0, WR1.
Holyoke Gas and Electric Department, 137 FERC ¶ 61,159 (November 29, 2011)	$336,367.86 Disgorgement	Disgorgement and compliance monitoring resulting from violations of 18 C.F.R. § 1c.2 (prohibition of electric energy market manipulation). Holyoke took three separate units out of service without notifying the ISO-NE or scheduling with the ISO-NE as required by the tariff, offered the three units' energy into the day-ahead and real-time markets, and submitted GADS data indicating the units had been available for dispatch during the outages, even though Holyoke knew the units could not have provided energy if dispatched.

APPENDIX C: FY2012 NOTICES OF ALLEGED VIOLATIONS[86]

Issue Date	Subject of Investigation	Description of Alleged Misconduct	Dates of Alleged Misconduct
October 1, 2012	Florida Power Corporation d/b/a Progress Energy Florida (PEF)	Alleged violations of Section 205 of the Federal Power Act and the Commission's order granting MBRA, specifically the misreporting of 1,300 transactions and the execution of 11 transactions at rates in excess of those permitted under PEF's cost-based rate tariffs.	2004-2009
September 21, 2012	PacifiCorp	Alleged violations of sections 17.1 and 18.1 and Schedule 11 of PacifiCorp's Open Access Transmission Tariff (OATT) and Part 37.6(e) of the Commission's regulations.	July 2009–February 2011
September 13, 2012	California Independent System Operator Corporation	Alleged violations of two Mandatory Reliability Standards approved by the Commission, PER-002-0 (Operating Personnel Training) Requirements R1 and R3; and TOP-002-2a (Normal Operations Planning) Requirements R1 and R6, in connection with its management of a local reliability requirement in the San Diego area. These violations resulted in CAISO erroneously and unnecessarily issuing directives to shed firm Load in the San Diego area on the night of March 31–April 1, 2010.	Certain dates through and including March 31–April 1, 2010
April 5, 2012	Barclays Bank PLC, Daniel Brin, Scott Connelly, Karen Levine, and Ryan Smith	Alleged violations of 18 C.F.R. § 1c.2 of the Commission's regulations by engaging in a coordinated scheme of trading day-ahead fixed-price physical electricity to benefit Barclays' fixed-for-floating financial swap positions in those markets.	Certain months in the period November 2006 to December 2008
January 30, 2012	Constellation Energy Commodities Group, Inc.	Alleged violations of 18 C.F.R. § 1c.2 and 18 C.F.R. § 35.41(b) of the Commission's regulations by engaging in virtual transactions in the NYSIO and scheduling day-ahead physical flows between the NYISO and PJM, in order to benefit financial positions.	September 2007 to December 2008

[86] A list of all Notices of Alleged Violations is available at http://www.ferc.gov/enforcement/alleged-violation/notices.asp.

December 20, 2011	Vista Energy Marketing, L.P.	Alleged violation of section 35.41(b) of the Commission's regulations and a Commission Order by making misleading or untrue statements to the Commission in connection with its application for market-based rate authority.	April 10, 2009 to July 3, 2010
December 15, 2011	Deutsche Bank Energy Trading, LLC	Alleged violation of the Commission's Prohibition of Electric Market Manipulation by scheduling and trading energy in California in order to benefit its Congestion Revenue Rights positions.	January 2010 through March 2010