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A Regulatory Reform Agenda for FERC

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Deregulation was a major theme during the first year of the Trump administration, with President Donald Trump calling on agencies to strike two regulations for each one they added. Many have taken up this call for regulatory reform, and the Federal Energy Regulatory Commission (FERC) could soon join their ranks. FERC is an independent agency that regulates the electric utility and natural gas pipeline industries; its core mission of ensuring that rates are just and reasonable remains vital. But there are areas in which FERC's regulations arguably impose significant burdens without advancing its mission in a meaningful way. Some of these regulations were sensible when implemented but may have become outmoded, while others were considered ill-advised from the beginning. Several could be targeted for reform if the administration pursues its agenda as we expect.

Create New Limits on Section 203 Reviews

Under Section 203 of the Federal Power Act (FPA), FERC approval is required if "a public utility seeks to sell, lease, or otherwise dispose of jurisdictional facilities." FERC has interpreted this authority broadly, requiring Section 203 approval for a wide variety of transactions.

The main idea behind Section 203 is that FERC should review changes in the control of facilities subject to its jurisdiction and their potential effects on the markets it regulates. However, the current regulatory framework requires Section 203 approval for a number of transactions that do not involve changes in the day-to-day management or operation of such facilities and would not affect markets subject to FERC's jurisdiction. For instance, large financial services companies and investment management firms that acquire and hold interests in public utilities generally act as passive investors with no intent or ability to control the public utility. But many transactions involving these companies may nonetheless trigger Section 203 approval requirements, imposing unnecessary costs and delays, acting as a barrier to investment in energy infrastructure, and taking up FERC resources.

FERC may look for ways to minimize Section 203 requirements for transactions that do not involve meaningful changes in control over day-to-day management and operations. FERC recently took a step in this direction by clarifying that such approval is not required to issue or transfer control of passive tax equity interests in public utilities. In addition, the agency has issued a notice of inquiry about potential modifications to its analysis of market power under FPA Sections 203 and 205, opening the door to broader reforms in this area.

FERC has already established "blanket authorizations" exempting certain categories of transactions from review. It could ease the burdens associated with Section 203 by expanding such authorizations, which currently include holding companies acquiring less than 10 percent of the outstanding voting securities of a public utility. FERC has previously considered increasing the threshold for this blanket

This article is from Skadden's *2018 Insights*.

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authorization to 20 percent so long as the company acquiring securities affirms that it does not intend to change or influence the control of the public utility. FERC could implement this increase or go even further by adopting a blanket authorization allowing investment management firms to acquire larger percentages of the voting shares of public utilities so long as they agree not to exercise control.

Additionally, FERC could create new blanket authorizations for relatively minor transactions that do not merit Section 203 scrutiny. Congress is considering a bill that would exempt all transactions involving facilities valued at less than $10 million from Section 203 review. If that bill is not enacted, FERC could create a blanket authorization for such transactions. It also could create one for transfers of new interconnection transmission assets from the companies that construct them to the intended owners.

Finally, for transactions that still require Section 203 approval, FERC could streamline the review process. For instance, when conducting Section 203 reviews of transactions that result in de minimis changes in market power, FERC has determined that detailed competitive analysis screens are unnecessary. FERC could similarly waive this requirement for other types of transactions that do not raise market power concerns, such as transfers of new generation facilities after testing but before commercial operation and transactions that deconcentrate facility ownership.

Cut Back on Filing Requirements

Compliance with FERC regulations typically requires submitting numerous and often voluminous filings. While some amount of paperwork is unavoidable, FERC could look for ways to reduce filing burdens, such as by eliminating requirements that provide few substantive benefits. For instance, FERC could consider expanding the "broker or dealer" exclusion in the Public Utility Holding Company Act of 2005 to cover holdings connected to investment management and advisory functions. This change would eliminate the need for many firms to file notifications regarding their holding company status.

Ensure That Enforcement Is Conducted Fairly

Enforcement provides other prime opportunities for reform. FERC could make both procedural and substantive changes to ensure that it is protecting competitive markets while treating the subjects of its investigations fairly.

FERC has adopted a number of controversial positions on procedural rules for enforcement cases. For instance, those targeted for penalties under the FPA have the option to seek immediate *de novo* review in a federal district court. FERC has argued that such review should be limited to the administrative record. This interpretation has prompted pushback, with critics arguing that it does not give the responding party adequate opportunity to develop and present its case. Several federal courts have rejected FERC's narrow interpretation of *de novo* review. FERC Commissioner Neil Chatterjee, who served as chairman from August 2017 until December 2017, when Kevin McIntyre became the new chairman, recently said he thinks FERC needs to re-examine this issue. In addition to rethinking its position on the nature of *de novo* review, FERC may also reconsider its position that such review is not available under the Natural Gas Act.

Several other procedural practices could be reviewed. For example, in 2009 FERC authorized the director of the Office of Enforcement to issue a public notice of alleged violations once enforcement staff has completed an investigation and given the subject an opportunity to respond to preliminary findings. While FERC has argued that these notices promote transparency, they impose significant costs on those who are publicly identified and accused of wrongdoing. For individuals, even if later vindicated, the taint can follow them and impact their future employment prospects.

FERC also could adjust its approach to penalties in enforcement cases. It could do away with its civil penalty guidelines, which often call for harsh fines exceeding what is necessary to incentivize compliance. It also could follow the lead of the Commodity Futures Trading Commission by dramatically increasing the incentives for self-reporting violations and cooperating with investigations. Additionally, FERC could assess lighter penalties on companies — since those are ultimately borne by shareholders — and instead impose penalties directly on employees who act in unsanctioned ways.

Finally, FERC could make substantive changes to its enforcement strategy regarding market manipulation. FERC has taken an expansive view of market manipulation in recent years, punishing conduct that takes advantage of market design flaws or violates the spirit of market rules. In addition to raising fairness concerns, this approach may discourage participation in FERC-jurisdictional markets, undermining the competitiveness and liquidity of these markets. FERC could reconsider its aggressive stance and concentrate its enforcement resources on conduct that violates clearly established market rules.

Eliminate the 'Shipper-Must-Have-Title' Rule

Under FERC's "shipper-must-have-title" rule, companies transporting natural gas on interstate pipelines must have title to the gas they are shipping when it is delivered to the pipeline and while it is in transit. The rule originated in the late 1980s as a tool to prevent unauthorized capacity brokering and ensure transparency as the industry transitioned to an open-access regime. However, in light of intervening changes — such as the creation of capacity release regulations — some in the industry think that the rule has become an unnecessary encumbrance to economically efficient transfers of pipeline capacity. In the years after FERC's authority to assess civil penalties was expanded in the Energy Policy Act of 2005, many of the agency's enforcement cases focused on violations of the shipper-must-have-title rule and related restrictions. While enforcement has shifted away from these types of cases in recent years, the rule continues to act as a restraint on competition. FERC could consider eliminating the rule and allowing pipeline capacity to be used by those who value it most highly.