United States Senate

WASHINGTON, DC 20510

September 12, 2014

The Honorable Gregory Friedman
Inspector General
Department of Energy
1000 Independence Avenue, SW
Washington, D.C. 20585

Dear Inspector General Friedman:

We write to ask you to determine facts related to allegations surrounding the Federal Energy Regulatory Commission's (FERC) enforcement program with respect to fairness and transparency. We note that Senator Casey has already sent a letter seeking answers about FERC's enforcement program, and we submit additional questions for your consideration.

Our letter is prompted by information recently placed in the public record about aspects of FERC's enforcement work in recent years. We support enforcement of all federal laws, including those that are intended to protect participants in the vital energy markets regulated by FERC. However, questions and allegations have been raised about the fairness and transparency of FERC's enforcement program following a Senate Energy and Natural Resources Committee hearing[1] and the publication of an *Energy Law Journal* article.[2]

FERC's decisions have significant impacts. By one rough measure of economic impact, the energy transmitted over FERC-regulated pipes and wires is worth over $400 billion per year or about three percent of the gross domestic product. Most Americans, including our constituents, feel the impact of FERC's decisions. Ultimately at stake are the quality of energy service and billions of dollars that are paid by energy consumers. Although Congress has jurisdiction over the laws that FERC administers, and FERC itself is organized as an independent multi-member commission, the FERC Chairman and staff have considerable authority on their own.

Given your office's expertise in investigating allegations of abuse, we ask you to inquire into the underlying facts as illuminated by the record of the hearing and advise Congress and the public as soon as possible on the following points:

1. There are allegations that the public, including FERC-regulated entities and their employees, are not being given actionable notice by FERC of the conduct, which under current law, FERC precedent, and applicable tariffs constitutes market manipulation. It has been further suggested that certain parties who do not otherwise appear frequently before FERC are held to different standards. The record of the referenced hearing, the *Energy Law Journal* article, and the attached materials[3] contain a number of factual

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[1] *See, e.g.*, Testimony of Norman Bay before Committee on Energy & Natural Resources, United States Senate (May 20, 2014); #1-4 from Sen Lee (pp. 33-40), #1-3 from Sen Barrasso (pp. 40-45), #3-6, 11, 43, 45 from Sen Murkowski (pp. 49-54, 62-66, 100-106); http://www.energy.senate.gov/public/index.cfm/files/serve?File_id=198f6249-394c-482d-9c7e-0d0ec80692

[2] Scherman, William S., Brandon C. Johnson, and Jason J. Fleischer. "The FERC Enforcement Process: Time For Structural Due Process and Substantive Reforms". *Energy Law Journal* 35.1 (2014): 101-49. Print. http://www.felj.org/sites/default/files/docs/elj351/18-101-Scherman%20et%20al._Final%205.13.14.pdf

[3] See Attachment A.

assertions and counterpoints on these claims. For example, the record contains conflicting assertions: on the one hand, it suggests that there is adequate notice, but on the other hand it suggests that market participants have no way to know the conduct that is proscribed. Is there a lack of actionable notice with regard to market manipulation? Is FERC holding certain parties to different standards with regard to market manipulation?

2. There are allegations that the targets of FERC investigations and their employees are not afforded an opportunity to:
    a. Defend themselves and communicate directly with FERC Commissioners before proceedings become public;
    b. Shield their identities from disclosure and thus protect their reputations until proceedings against them have progressed to an appropriate stage (*e.g.*, until they have been formally "charged");
    c. Gain timely access to exculpatory materials known to the government;
    d. Obtain prompt access to the transcripts of their depositions;
    e. Secure *de novo* Federal Court review of FERC enforcement action that is consistent with the Federal Power Act and FERC precedent; and
    f. Receive penalties (if and when penalties are warranted) that are proportionate to the civil infraction at issue and their relative role in energy markets.

    With respect to each of the foregoing, have the targets of FERC investigations and their employees been afforded the process required by FERC's own regulations and precedents? To what extent have the targets of FERC investigations and their employees been afforded the level of process provided under law by other federal enforcement agencies, such as the Securities and Exchange Commission, the Commodity Futures Trading Commission, and the Department of Justice?

3. During his confirmation hearing, the former Director of the Office of Enforcement was asked about the connection between FERC's enforcement settlement with Constellation Energy and its approval of Constellation's merger with Exelon. FERC approved the settlement agreement with Constellation on the same day as it approved the Exelon-Constellation merger. The settlement agreement (FERC Docket No. IN12-7-000)—which the Director signed—directly references[4] the merger with Exelon. When the Director was asked whether he would be concerned about the appearance of a quid pro quo between merger reviews and enforcement, the Director said he "would be concerned about the appearance of a quid pro quo…between merger reviews and enforcement."[5] When asked whether he or anyone else at FERC suggested to the parties of the pending merger that it would be prudent to settle the pending enforcement action, he testified that "[t]o the best of my recollection, I did not indicate to the parties in the Exelon-Constellation merger that it would be prudent to settle the pending enforcement matter to get the merger approved. I do not know whether anyone else at FERC did so."[6] At the time, the settlement agreement with Constellation was the largest settlement in FERC's history and the Exelon-Constellation merger created one of the nation's largest electric utilities.

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[4] See Attachment B (paragraph #44).

[5] Testimony of Mr. Norman Bay (Answers for the Record) before the Committee on Energy and Natural Resources, United States Senate (May 20, 2014); Question for the Record #5 from Sen. Lisa Murkowski (pg. 51); http://www.energy.senate.gov/public/index.cfm/files/serve?File_id=198f6249-394c-482d-9c7e-0d0ec80692cf

[6] Ibid.

Given these circumstances, did the former FERC Chairman or any member of FERC's staff suggest or actively or effectively require that a regulatory approval would be contingent upon the "voluntary" settlement of an enforcement dispute, *e.g.*, in the matter of Constellation Energy? If so, does such a practice represent any conflict of interest or wrongdoing?[7]

4. The attached document from the Office of Personnel Management denies the request to reclassify the position of FERC's Director of the Office of Enforcement within the Senior Executive Service as a career position and then to install the non-career incumbent in the career position.[8] Given that this was rebuffed by the Office of Personnel Management and deemed impermissible under federal law and regulation, we ask that you investigate the circumstances surrounding the request for such a reclassification.

It is important to establish facts that can be the basis of good decision making by Congress. We look forward to your prompt response.

Sincerely,

Susan M. Collins
United States Senator

John Barrasso, M.D.
United States Senator

[7] See Attachment C.
[8] See Attachment D.

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OPINION

The Investors at War With Political Power

How a once-obscure federal agency targeted two brothers, and what happened when they decided to fight back in the age of Obama.

By JOSEPH RAGO

May 2, 2014 6:45 p.m. ET

West Chester, Pa.

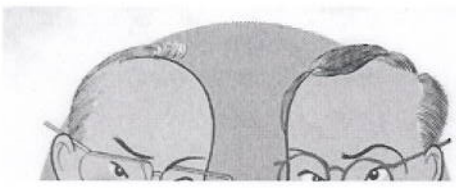
There's a quote hanging on the wall of Rich Gates's office, here in a suburb west of Philadelphia: "No person, in any culture, likes to be bullied. No person likes living in fear because his or her ideas are different. Nobody likes being poor or hungry, and nobody likes to live under an economic system in which the fruits of his or her labor go unrewarded." President Obama, in his book "The Audacity of Hope," meant those words as inspirational; for Mr. Gates, they are ironic.

Late last summer Mr. Gates and his identical-twin brother, Kevin, learned in a letter from the government that they were being accused of having manipulated electricity markets, a serious fraud violation. After a three-year investigation, federal energy regulators had concluded that two of their investment partnerships, known as Powhatan and Huntrise, had "profited, intentionally so" from sham power trades. The Gates's reply to the 28-page document, in its entirety:

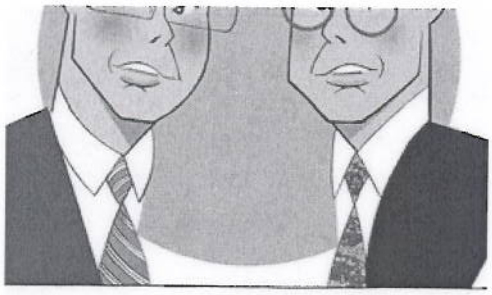
"Your preliminary findings make no sense. Should you choose to proceed with a public notice against Powhatan and/or Huntrise, please be advised they will respond publicly and forcefully." The Gates brothers debated whether the second sentence was redundant. By then, they had decided they wouldn't be bullied any longer.

The brothers went public with an earth-scorching campaign against their treatment by the Federal Energy Regulatory Commission, or FERC. They've released hundreds of pages of internal documents that aren't normally disclosed during an ongoing investigation, and FERC is not pleased. This is not supposed to happen, and never has.

Rich Gates says he was "completely dumbfounded" by FERC's legal and financial reasoning. "We wanted to go open kimono," Kevin Gates adds, "and just provide full transparency into the process to the public at large."



The Gates case offers a rare glimpse into FERC's prosecutorial method and the workings of the larger regulatory state in the Obama era. Since 2009, the commission has transformed itself from the boring regulator nobody ever heard of into a fearsome scourge of Wall



Ken Fallin

Street and U.S. business. To great political acclaim, FERC's Office of Enforcement has pursued everybody from big financial institutions like Barclays and Deutsche Bank down to individual traders and even Maine paper mills, making market-manipulation charges much like those lobbed at Powhatan and Huntrise.

FERC's most notable scalp so far is a $410 million settlement last year with J.P. Morgan that happened to land amid the London Whale and mortgage securities political pile-on. The White House thinks well enough of the enforcement division's work that the administration wants to promote its director, Norman Bay, to FERC chairman.

The problem is that no one understands what FERC's definition of "market manipulation" is, only that, like Justice Potter Stewart, Mr. Bay knows it when he sees it. Though the financial stakes for the Gateses aren't high in the scheme of things—$4.7 million in allegedly ill-gotten profits, by FERC's reckoning—the brothers think that their reputations are worth defending. Alone among FERC's targets, they're doing what they promised, publicly and forcefully.

"This particular adventure began in 2008 when we cold-called Alan Chen, " Kevin Gates says. Dr. Chen was a Houston energy trader with a Ph.D. in power engineering, and his strategy appealed to the Gates brothers. They and their friends and family set up a fund, Huntrise, which would reflect Dr. Chen's plays.

The fund was a side investment for their personal portfolios. Their day jobs are managing a midsize advisory firm called TFS Capital. Rich Gates is among the heroes of Michael Lewis's "Flash Boys," and the Securities and Exchange Commission considers him a Dodd-Frank whistleblower for his role in exposing some high-frequency trading practices.

The trades on FERC trial are less exotic. Megawatts can be bought and sold like any other stock or commodity in about half the country where competitive wholesale power has replaced the old state utility monopolies. Dr. Chen was trading in a large regional market called PJM Interconnection, a transmission grid organization that covers all or most of 13 mid-Atlantic states out to Ohio.

He was placing bets on the spread between the day-ahead and real-time price of electricity, focused on rare but very profitable events that could not be known in advance. Think of a batter swinging for a home run on every pitch even if he strikes out most of the time.

Then one day in November 2009, Dr. Chen received a surprise reimbursement from PJM, retroactively paying him an honorarium for some of his past trades. He was the beneficiary of a running debate within FERC over "fairness" and who should pay for the fixed costs of electric transmission.

FERC favors the bafflingly complex over the straightforward and efficient, but to oversimplify, all buyers and sellers pay various tariff charges to participate in PJM. The process is designed to collect more of these up-front fees than transmission costs in practice. "Basically there's a big pot of money left over that PJM has to allocate," Kevin Gates explains.

This redistribution largely had gone to grid operators that physically flowed power through the transmission lines. But then FERC decided that since traders like Dr. Chen were also required to prepay the tariff charges, they deserved to be cut in on the rebates too. He realized—it takes a doctorate in the sciences to understand the formula's technicalities—that at certain predictable geographical hubs in PJM

and at certain predictable times, the rebates would be significant and higher than the tariff charges. As it turned out, the system would sometimes pay him to make trades.

"We liked the investment to begin with, that's why we had money with Alan," Kevin Gates says. "Now we have this tailwind. We were collecting rebates in addition to the normal exposure we were getting. Therefore the natural, logical response is, let's increase our exposure."

Another way of putting it is that since the cost of swinging was lower, the Gates brothers could try for more home runs. Around this time they founded Powhatan and ramped up their trading volume over six months in 2010. Of the Gates brothers' initial $2 million investment, Dr. Chen lost over $400,000 in the first two days, though he went on to grow the investment to $7 million in a matter of weeks.

That drew the ire of FERC's enforcement division, which began demanding information and taking depositions in fall 2010. At first, the Gates brothers tried to adhere to the insider playbook and hired an attorney from White & Case, a D.C.-based law firm that does frequent business in front of FERC. The insular Washington energy bar trafficks in political connections, but those aren't so useful for clients who maintain their innocence.

Things started to turn for Kevin Gates, he recalls, during his second full-day deposition with the lead FERC enforcement lawyers on the Powhatan matter, Steven Tabackman and Thomas Olson. "I would suggest that it was intimidation tactics, aggressive behavior, which I guess is natural for a federal prosecutor, maybe what you would expect," he says. "But there were also a lot of questions asked and behavior that suggested to me that we were seeing the world very differently and—I would suggest—they didn't know what they were talking about."

Mr. Gates was asked to leave the room and sat in the hallway while his lawyer conferred with the feds. The lawyer emerged to relate what the FERC enforcement team had proposed: "Kevin's a businessman, isn't he? He knows that it's cheaper to settle than it is to fight this investigation." Right then, Mr. Gates says, "I realized that we had a big problem on our hands. This was unlike anything we'd ever seen before at a regulatory agency."

The Gates brothers fired the white-shoe practice and brought on Bill McSwain of Drinker Biddle, a Philadelphia-area lawyer who "didn't interface much with FERC. He also used to be a Marine sniper, so he had a different approach to the world." Mr. McSwain introduced himself to FERC by calling their conduct contrary to "established law, as well as common sense," and that was one of his subtler letters.

Ultimately FERC claimed that Powhatan was making trades merely to harvest the PJM rebates, not transactions that had a legitimate economic purpose or generated real value. FERC calls them "wash trades."

Yet FERC doesn't seem to understand the difference between a wash trade and a washing machine. By definition wash trades make no money and entail no risk—a trader makes near-simultaneous purchases and sales of the same security. They can be self-dealing or used to trick another investor or inject bad information into the market. As Rich Gates put it, "Alan Chen's trades were very different. They were spread trades that were designed to make money by themselves, they didn't benefit some other entity, they weren't designed to deceive. They were designed with the sole purpose of making money."

More to the point, the Gates brothers make a compelling argument about due process. FERC debated the transmission rebates, vetted the consequences, and then wrote rules that opened the PJM rebates to traders. The commission itself had expressly predicted in a 2008 ruling that if arbitrageurs "can profit

from the volume of their trades," they "may make trades that would not be profitable based solely on price differentials alone."

In other words, even if the Gates brothers were trying to amass rebates and nothing else, that was not illegal or illegitimate at the time, and FERC never gave fair notice suggesting otherwise. Instead, years later, the commission decided that it didn't like the outcomes that it anticipated from the incentives it created, and decided to selectively punish some investors ex post facto. If in hindsight FERC thinks the results of obeying its rules are undesirable, then the commission should either make better rules or else give investors like the Gates brothers a public-service medal for exposing its own mistakes.

FERC did end up changing the rules, again. The rebates for traders stopped. But the assault on Dr. Chen and the Gates brothers has continued. FERC even views their efforts to exonerate themselves as compounding the original offense, such as it is.

The Gates brothers hired as consultants an all-star roster of experts in power and securities law to independently examine the facts of the case. They include Harvard's Bill Hogan and Richard Tabors, formerly of MIT, who were the architects of the electric-deregulation movement. Another is Craig Pirrong of the University of Houston, probably the world's leading authority on commodity-market manipulation. With their own credibility to maintain, not one supported FERC.

One of the experts, Susan Court, FERC's former enforcement director, had "a very short meeting" with her successor, Mr. Bay, as a gesture of good faith. She informed him of what the Gates brothers were up to. Ms. Court reported that Mr. Bay "was very upset and taken aback." Perhaps he let that cloud his judgment, Kevin Gates says.

The brothers concluded, Mr. Gates continues, that "we can't communicate effectively with the FERC," so they'd try to persuade "our neighbors, our investors, our business partners." They've uploaded all of their case files and correspondence to a public website, Ferclitigation.com. Mr. Gates says that, "It's never good as a money manager or even just a citizen to have your name in the paper as a market manipulator, but we know we're not going to settle."

FERC still hasn't brought public charges or formally closed the investigation. The Gates brothers have filed Freedom of Information Act requests for records relevant to their case so that they can disclose more, and they're more or less daring FERC to sue. The brothers seem like they'd be delighted to vindicate themselves in a court of law.

Still, their treatment does raise troubling questions about Mr. Bay's fitness and competence to lead the larger Federal Energy Regulatory Commission. Congress gave FERC market-manipulation oversight powers with teeth—including penalties of $1 million per day per violation—only in 2005, but those powers did not receive a real work-out until Mr. Bay joined FERC in 2009. He was formerly U.S. attorney for New Mexico.

Mr. Bay expanded the Office of Enforcement to some 200 staffers from 20 a decade ago, bringing in the likes of Mr. Tabackman, who was most recently a partner at Butzel Long Tighe Patton, where from 2002 to 2005 he was a consultant to the legal-defense team of 9/11 conspirator Zacarias Moussaoui.

These former criminal prosecutors and litigators have specialized in retroactive punishments for conduct that was legal at the time. Most of these cases never go to court and end with settlements against politically disfavored defendants like J.P. Morgan (that one, like Powhatan, was led by Mr. Olson). Most companies roll over because their future business interests depend on preserving good regulatory

graces and favorable FERC rulings. The Gates brothers are unusual in that their livelihoods are elsewhere, but the illogic, intimidation tactics and erosion of due process in their investigation are typical.

The larger point is that the Gates case shows Mr. Bay and FERC are really undermining the electricity markets in the name of defending them. Ad hoc settlements win political plaudits, but because companies usually neither admit nor deny wrongdoing, the settlements set no meaningful or coherent legal precedents. Aside from mind readers and fortune tellers, no one can know what the rules—or, rather, what FERC's subjective backward-looking interpretation of market manipulation—will be, depriving the markets of liquidity and price discovery. "Shooting random people for following the law," says Rich Gates, "that sets the markets and the world back."

Mr. Rago is a member of the Journal editorial board.

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REVIEW & OUTLOOK

Harry Reid's Personal Prosecutor

A paper mill may pay $5.3 million for breaking a rule that didn't exist.

June 22, 2014 6:48 p.m. ET

The trail of evidence from most political crime scenes eventually traces back to Harry Reid's Capitol chambers these days, as the Majority Leader and the White House plot to keep the Senate. But an energy nomination fight seems to be producing more innocent casualties than usual.

Mr. Reid and President Obama have weaponized the formerly obscure Federal Energy Regulatory Commission in the name of their anticarbon agenda, and their nominee to lead FERC is prosecutor Norman Bay. Mr. Bay cleared the Senate Energy Committee last week on a chaotic 13-9 vote that departed from regular order, and his nomination may reach the floor this week.

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Mr. Reid is moving with unusual dispatch because many Democrats are scrutinizing Mr. Bay's record of prosecutorial abuse as the head of FERC's enforcement office. Mr. Bay's skeletons long ago filled up the closet, and Senators should meet one of them: Keith Van Scotter.

For 10 years Mr. Van Scotter has run a paper mill in the northern Maine town of Lincoln, population 3,000. Mr. Bay accuses Lincoln Paper and Tissue of having manipulated in 2007-08 a federal program meant to promote energy conservation. If a court doesn't dismiss the case later this month or the company loses at trial, Lincoln Paper may be liable for a $5 million civil penalty and $379,016.03 in disgorgement, plus interest.

U.S. Senate Majority Leader Harry Reid *Reuters*

That's about twice its annual capital spending and could force the mill out of business. Yet Lincoln Paper broke no known law. Meanwhile, last month a federal appeals court confirmed that the government had no jurisdiction over energy savings programs of this type and the attempt to regulate them was an abuse of power. "The whole process has been through-the-looking-glass bizarre," says Mr. Van Scotter.

Lincoln Paper chose to participate in "demand response" on the New England electric grid, where large power users were paid for the electricity they didn't use. Such energy efficiency incentives are a key feature of the anticarbon agenda at the Environmental Protection Agency and FERC.

The problem is that no one knows how to value the cost of not buying something a customer might or

might not otherwise buy over time. Establishing the "right" amount of electricity off which to measure savings is an inherent voodoo science.

Lincoln Paper had an aging steam-powered generator on site that supplied a minority of the mill's energy needs and took the remainder from the regular grid. Mr. Bay claims that Mr. Van Scotter intentionally ran this generator less than he normally would when the baseline was being created. Then he ramped the generator back up to make it seem as if he was drawing less energy off the meter and thus stealing the demand payments.

Given the age and unreliability of the unit, Lincoln Paper made a good-faith effort to try to reflect "normal" operations, whatever that may be. In fact, Lincoln Paper reduced its consumption from the grid, i.e., conserved energy, by more than what was required by the program Lincoln is accused of manipulating.

But more to the point, FERC never defined "baseline" and made no rules about the right way to set one or how equipment should be operated during the measurement period. As Mr. Bay recently told the Senate in a letter, "the absence of a violation of market rules is not a defense to market manipulation."

That's Orwellian enough, but the D.C. Circuit Court of Appeals also tossed the demand-response programs last month as "arbitrary and capricious." FERC is still trying to deny Mr. Van Scotter his day in court by asking a district judge to decline to hear the case de novo and simply rubber-stamp Mr. Bay's punishment. Yet Lincoln Paper is entitled to no discovery during FERC investigations or even to know the identity of its accusers. Seven of the nine deposed witnesses remain anonymous under Mr. Bay's rules. He wants to play prosecutor, jury and executioner.

So Mr. Bay may ruin a small-business owner unsophisticated in the ways of Washington for running a machine at somewhat less than maximum capacity in a now defunct program that was extralegal because FERC lacked jurisdiction. In the process the feds are devastating a rural community. One of the largest employers in the region, Lincoln Paper was recently forced to lay off half of its 400 workers—with the overhang of litigation and the risk of fines and penalties "a contributing factor," notes Mr. Van Scotter.

The American paper industry may still be carbon-intensive, but it has survived global competition through innovation and specialization. Lincoln Paper manufactures a product called deep-dye tissue and it is merely one out of *four* Maine paper concerns or industry consultants Mr. Bay has pursued at FERC. One went bankrupt.

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This record suggests Mr. Bay would be a FERC chairman who will act as a law unto himself, which seems to be what Messrs. Reid and Obama want. FERC is already capably led by acting Chairman Cheryl LaFleur, a Democrat and Obama nominee whom the Energy Committee supported for a new term last week on a 21-1 vote. Yet Mr. Reid has openly said he wants to demote her because she sometimes disagreed with his previous man at FERC, former Chairman Jon Wellinghoff. That is, she tends to obey statutes rather than rewrite them.

The White House also boxed out Ms. LaFleur with an unusual personnel order limiting the powers of the "acting" FERC Chairman, which would otherwise broadly resemble those of a CEO. Senators who vote to confirm Mr. Bay will be endorsing the FERC injustice against Mr. Van Scotter—and all the others likely to come.

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138 FERC ¶ 61,168
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
and Cheryl A. LaFleur.

Constellation Energy Commodities Group, Inc. — Docket No. IN12-7-000

ORDER APPROVING STIPULATION AND CONSENT AGREEMENT

(Issued March 9, 2012)

1. The Commission approves the attached Stipulation and Consent Agreement (Agreement) between the Office of Enforcement (Enforcement) and Constellation Energy Commodities Group (CCG). This order is in the public interest because it resolves the investigation into whether CCG violated the Commission's Anti-Manipulation Rule, 18 C.F.R. § 1c.2, and the Commission's regulation prohibiting the submission of inaccurate information, 18 C.F.R § 35.41(b). CCG has agreed to pay a civil penalty of $135,000,000 and to disgorge unjust profits of $110,000,000, including interest. In addition, CCG has instituted and will continue to institute additional compliance measures such as: (1) regular monitoring of profit and loss concentrations in virtual transactions and physical schedules of electric energy; and (2) reviewing and documenting the purpose of virtual transactions. CCG is required to monitor and preserve for no less than five years trader communications, including but not limited to Instant Messages (IMs), emails, and telephone calls. CCG must also submit compliance monitoring reports.

Background

2. In January 2008, Enforcement opened a preliminary, non-public investigation pursuant to Part 1b of the Commission's regulations of CCG's physical power trading in and around the New York Independent System Operator's (NYISO) control area after receiving two anonymous hotline calls related to that trading. After commencing that investigation, Enforcement observed through its own surveillance activities that CCG was engaging in virtual trading in the NYISO that was unprofitable. In addition, on February 19, 2009, the NYISO Department of Market Monitoring and Performance (MMP) informed Enforcement that it had decided to apply mitigation measures against CCG related to its virtual bidding behavior in the NYISO, because its virtual load trading

in NYISO Zone A had contributed to an unwarranted divergence of locational based marginal prices between the day-ahead (DA) and real-time (RT) markets. Based on Enforcement's surveillance observations and the NYISO's information, Enforcement opened another preliminary, non-public investigation pursuant to Part 1b to determine whether, in violation of 18 C.F.R. § 1c.2, CCG employed a scheme of trading in the NYISO virtual market to move DA prices in a direction that would benefit its financial contract for differences (CFD) positions. Enforcement thereafter conducted the two investigations jointly.

3. In its investigation, Enforcement examined certain of CCG's: virtual trading in the NYISO and ISO-New England (ISO-NE); physical DA scheduling between the NYISO and ISO-NE, PJM Interconnection (PJM) and Ontario Independent Electric System Operator (IESO); and CFD positions in the NYISO and ISO-NE. Enforcement examined certain data related to CCG's East Power Trading Group from January 1, 2007 through February 28, 2009 and, as a result, focused its investigation on trading activity by certain members of the East Power Trading Group over a sixteen month period from September 2007 through December 2008 (the Months of Interest). The members of the East Power Trading Group whose activity was investigated were Joseph Kirkpatrick, Michael Pavo, and Jason Hughes (Kirkpatrick, Pavo and Hughes together the East Traders). Kirkpatrick was the supervisor of Pavo and Hughes. In addition, Enforcement investigated the activity of Maxim Duckworth, CCG's Managing Director of Portfolio Management and Trading, and Kirkpatrick's direct supervisor and Pavo and Hughes' indirect supervisor.

4. During the Months of Interest, CCG participated in energy trading in markets including the NYISO, ISO-NE and PJM. In the Months of Interest, the East Power Trading Group participated in the virtual markets in the NYISO and PJM and in the scheduling of DA physical power between the NYISO and ISO-NE, PJM and IESO, as detailed in the Agreement.

5. CCG's East Power Trading Group also held CFDs during the Months of Interest, including: swaps that priced off the average DA prices in the NYISO and ISO-NE; swaps that priced off the RT price in PJM; financial transmission rights (FTRs) in ISO-NE and PJM; and transmission congestion contracts (TCCs) in the NYISO. The swap positions investigated by Enforcement settled off the monthly average of the DA price of the Zone/region for which the swap was held. As further described in the Agreement, Enforcement found the size of the swap positions to be substantial. The FTR/TCC positions similarly settled off the DA price for the ISO Zone/region in which they were held. The CFDs investigated by Enforcement in the NYISO predominantly settled off the monthly average DA price in Zones A and G and the CFDs investigated by Enforcement in ISO-NE predominantly settled off the monthly average DA price at Mass Hub.

6. For the period of September 2007 through December 2008, the swap positions entering a month ranged in size from approximately 395 MW/h to approximately 12,274 MW/h in NYISO Zone A, from approximately 125 MW/h to approximately 3,682 MW/h in NYISO Zone G, and from 88 MW/h to 3,350 MW/h in ISO-NE Mass Hub. Over that same time frame, the TCC positions ranged in size from 25 MW/h to 936 MW/h in Zone A and 450 MW/h to 931 MW/h in Zone G.

7. As detailed in the Agreement, Enforcement found a repetitive pattern to the virtual and DA physical trading during the Months of Interest. While the practice varied somewhat from month-to-month and zone-to-zone, the trading behavior can be summarized as follows: (i) when the net CFD position which settled off the average DA price of a region was short, the CCG traders at issue entered virtual supply in the Zone/region on which the CFD settled and/or scheduled the import of DA power into the region on which the CFD settled; and (ii) when the net CFD position which settled off the average DA price of a Zone/region was long, the CCG traders at issue entered virtual load in the Zone/region on which the CFD settled and/or scheduled an export of DA power from the region on which the CFD settled to a neighboring ISO.

8. During the Months of Interest the virtual and physical transactions scheduled by the East Traders were routinely unprofitable.

9. CCG's compliance training materials recognized that behavior which was uneconomic on a stand alone basis in order to benefit positions in other markets should not be engaged in by its traders and that the Commission would likely consider this market manipulation.

10. When the NYISO investigated CCG's virtual trading activity in its markets for purposes of examining unwarranted divergence, CCG stated in its communications with the NYISO, that its decisions to participate in the NYISO virtual market were based on market fundamentals and omitted the fact that the virtual trading was directly related to its CFDs.

Investigation

A. Commission Anti-Manipulation Rule

11. Enforcement concluded that from September 2007 through December 2008, CCG violated the Commission's Anti-Manipulation Rule, 18 C.F.R. § 1c.2, which prohibits any entity from: (1) using a fraudulent device, scheme or artifice, or making a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule or regulation, or engaging in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite scienter; and (3) in connection with a transaction subject to the jurisdiction of the Commission.

12. Enforcement determined that during the Months of Interest, CCG violated the Anti-Manipulation Rule by entering into virtual transactions and DA physical schedules without regard for their profitability, but with the intent of impacting DA prices in the NYISO and ISO-NE to the benefit of certain significant CFD positions held by CCG.

13. Enforcement also determined that as part of this scheme, CCG combined the use of virtual transactions with DA physical schedules to impact DA prices in NYISO and ISO-NE to benefit the CFD positions that priced off a component of those impacted DA prices.

14. Enforcement determined that CCG's virtual transactions and DA physical schedules were often large in volume and were scheduled with regularity and persistency. By way of example, Enforcement found that in on-peak Zone A during the Months of Interest the East Traders' virtual trading represented between approximately 24 and 79 percent of all virtual activity in the Zone when the East Traders placed a trade. Enforcement also concluded that in approximately half of the on-peak Zone A months, the East Traders bid virtually in 100 percent of available hours and only three times did their activity drop below 60 percent of available hours. In half of the on-peak Zone A activity identified in the Months of Interest, Enforcement found that virtual trading comprised between 30 and 40 percent of the Zone's actual physical load when the East Traders placed a trade. During this same time frame, the East Traders flowed DA on-peak physical power between the NYISO and PJM in 100 percent of the hours in two of the four months identified by staff and their flows represented over 50 percent of the limit of the intertie when it flowed. The East Traders' DA, on-peak physical flows between the NYISO and Ontario ranged in frequency from approximately 20 to 80 percent in the four months identified and averaged between approximately 20 to 80 percent of the available capacity of the intertie when they flowed.

15. Enforcement also found that CCG impacted the DA price in the various markets in which they engaged in this trading behavior to the benefit of their CFD positions.

16. Based on these findings, Enforcement determined that: (1) CCG's virtual and physical trading activities during the Months of Interest constituted a fraudulent device, scheme or artifice and that CCG engaged in a course of business that operated as a fraud upon the NYISO and ISO-NE markets; (2) CCG intended to manipulate the NYISO and ISO-NE DA markets for the benefit of its CFD positions during the Months of Interest; and (3) CCG's manipulative scheme was in connection with transactions subject to the jurisdiction of the Commission all in violation of 18 C.F.R. § 1c.2.

17. Enforcement determined that this manipulation of the physical and virtual markets and the respective DA prices resulted in widespread economic losses to market participants who bought and sold energy in the DA markets of ISO-NE and the NYISO. In addition, this manipulation distorted price discovery for all market participants, which contributes not only to trading decisions, but to a variety of industry-wide determinations.

B. Commission Accurate Information Provision

18. Enforcement concluded that CCG violated 18 C.F.R. § 35.41(b), which requires sellers, such as CCG, to "provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with . . . Commission-approved independent system operators, or jurisdictional transmission providers, unless Seller exercises due diligence to prevent such occurrences."

19. Enforcement determined that Section 35.41(b) of the Commission's regulations applies to CCG because it is a power marketer that is authorized by the Commission to sell – and it does sell – energy, capacity and certain ancillary services at market-based rates in the NYISO, ISO-NE and PJM.

20. Enforcement determined that CCG violated 18 C.F.R. § 35.41(b) by providing inaccurate and misleading information to the NYISO. Specifically, Enforcement determined that CCG denied that its virtual transactions were related to its CFD positions and instead told the NYISO that the transactions were independent of the CFD positions and were entered into based on market fundamentals.

Stipulation and Consent Agreement

21. Enforcement and CCG have resolved Enforcement's investigation by means of the attached Agreement. CCG neither admits nor denies that the trading behaviors examined by Enforcement violated the Commission's rules, regulations, or policies. Also, upon the Effective Date of the Agreement, as that term is defined in the Agreement, the investigation of CCG and of Kirkpatrick, Pavo, Hughes, and Duckworth will terminate.

22. The Agreement requires CCG to pay a $135,000,000 civil penalty to the United States Treasury within ten business days of the Effective Date of the Agreement. CCG will pay disgorgement and interest of $110,000,000, such amount representing unjust profits. The disgorgement shall be paid as follows: (i) $6,000,000 to be divided equally among and paid directly to the NYISO, ISO-NE, PJM, the Midwest ISO, Southwest Power Pool, and the California ISO for use in the enhancement of their surveillance capabilities; and (ii) to a fund set up for the benefit of electric energy consumers in the affected states and from which state agencies in those affected states may make requests for apportionment by a Commission Administrative Law Judge. That fund will be divided among the affected states in the ISOs as follows: NYISO ($78,000,000); ISO-NE ($20,000,000); and PJM ($6,000,000). This distribution is based on the results of staff's investigation and its assessment of the relative harm imposed on each organized market as a result of CCG's trading. Specifically, the allocation was based on the megawatts associated with DA schedules flowing between the ISOs and virtual transactions within NYISO that were part of what staff determined to be CCG's manipulative scheme.

23. Since the onset of Enforcement's investigation, CCG instituted additional procedures to monitor the profit and loss concentrations in virtual transactions and DA physical schedules of electric energy and to document the purpose of virtual transactions.

24. The Agreement requires CCG and any successor company to retain communications by its traders, including, but not limited to, IMs, emails and telephone calls, for a period of no less than five years and to regularly monitor those communications for irregularities or illegalities.

25. The Agreement requires CCG and any successor company to submit semi-annual compliance monitoring reports to Enforcement staff for two years following the Effective Date of the Agreement, with the option of a third year of compliance monitoring reports at Enforcement's discretion. Each compliance report shall describe any new and existing compliance program measures, including training, and alert Enforcement staff to any violations that may occur.

26. Under the Agreement, Pavo, Hughes, and Duckworth will not hold a position which involves physical and financial energy trading at CCG or a successor company in the future. CCG has also agreed that Kirkpatrick will not hold any such position at CCG or a successor company in the future.

Determination of the Appropriate Civil Penalty

27. Pursuant to section 316A(b) of the FPA, the Commission may assess a civil penalty up to $1,000,000 for each day that the violation continues.[1] In determining the appropriate remedy, Enforcement considered the factors described in section 316A(b) of the FPA and in the Revised Policy Statement on Penalty Guidelines.[2] Specifically, Enforcement considered that: CCG's conduct was serious and was committed willfully and intentionally; CCG's conduct was committed through the participation or oversight of CCG's Managing Director of Portfolio Management and Trading and therefore involved upper management; the conduct involved more than 100,000 MWh of electricity and continued for more than 250 days; CCG's compliance program was not effective at the time; and CCG's actions caused harm and impacted the DA price in the Commission's jurisdictional markets.

28. We conclude that the penalties, disgorgement, the enhanced compliance measures, and the compliance monitoring reports set forth in the Agreement are a fair and equitable

[1] 16 U.S.C. § 825o-1(b) (2006).

[2] *Enforcement of Statutes, Orders, Rules and Regulations*, 132 FERC ¶ 61,216 (2010).

resolution of this matter and are in the public interest, as they reflect the nature and seriousness of CCG's conduct.[3]

The Commission orders:

The attached Stipulation and Consent Agreement is hereby approved without modification.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

[3] The civil penalty falls within a range consistent with the Penalty Guidelines. Application of the Penalty Guidelines in this case furthers the goal of "add[ing] greater fairness, consistency, and transparency to our enforcement program." *Id.* at P 2. We have considered the factors set forth in the Revised Policy Statement on Penalty Guidelines and have concluded that the penalty in this case is appropriate.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Constellation Energy Commodities Group, Inc.	))	Docket No. IN12-7-000

STIPULATION AND CONSENT AGREEMENT

I. Introduction

1. The staff of the Office of Enforcement (Enforcement) of the Federal Energy Regulatory Commission (Commission) and Constellation Energy Commodities Group, Inc. (CCG) enter into this Stipulation and Consent Agreement (Agreement) to resolve an investigation conducted under Part 1b of the Commission's regulations, 18 C.F.R. Part 1b (2011). The investigation examined CCG's physical and financial electric energy trading activities in and around the New York Independent System Operator's (NYISO) Control Area, and in other RTOs, as described herein. Specifically, the investigation examined potential violations of the Commission's Anti-Manipulation Rule, 18 C.F.R. § 1c.2, and of the Commission's regulation prohibiting the submission of inaccurate information, 18 C.F.R. § 35.41(b).

II. Stipulations

Enforcement and CCG hereby stipulate and agree to the following facts:

2. In January 2008, Enforcement was contacted anonymously by two entities who questioned whether CCG may have manipulated the prices of electric energy in the NYISO for the period December 2007 through January 2008. Upon review, Enforcement determined that this information warranted further investigation. Enforcement opened a preliminary, non-public investigation pursuant to Part 1b of the Commission's regulations of CCG's physical power trading in and around the NYISO.

3. After commencing that investigation, Enforcement observed through its own surveillance activities that CCG was engaging in virtual trading in the NYISO that was unprofitable. In addition, on February 19, 2009, the NYISO Department of Market Monitoring and Performance (MMP) informed Enforcement that it had decided to apply mitigation measures against CCG related to its virtual bidding behavior in the NYISO. Specifically, the NYISO determined that from October 1 to November 18, 2008, CCG's virtual load trading in NYISO Zone A had contributed to an unwarranted divergence of locational based marginal prices (LBMP) between the day-ahead (DA) and real-time

(RT) markets. Based on Enforcement's surveillance observations and the NYISO's information, Enforcement opened a preliminary, non-public investigation pursuant to Part 1b of the Commission's regulations to determine whether, in violation of 18 C.F.R. § 1c.2, CCG employed a scheme of trading in the NYISO virtual market to move DA prices in a direction that would benefit its contract for differences (CFD) positions. Due to similarities in the geographical regions and trading behavior at issue, Enforcement jointly conducted the two investigations. The Enforcement examination, as described in greater detail in Sections I and II herein, constitutes the Investigation.

4. In its Investigation, Enforcement examined certain of CCG's: virtual trading in the NYISO and ISO-New England (ISO-NE); physical DA scheduling between the NYISO and ISO-NE, PJM Interconnection (PJM) and Ontario Independent Electric System Operator (IESO); and CFD positions in the NYISO and ISO-NE. Enforcement examined certain data, submitted pursuant to 18 C.F.R. §1b.9, related to the East Power Trading Group from January 1, 2007 through February 28, 2009 and, as a result, focused its Investigation on trading activity by certain members of the East Power Trading Group over a sixteen month period from September 2007 through December 2008 (the Months of Interest). Enforcement initially considered data related to virtual trading and DA physical schedules by certain members of the East Power Trading Group in the Midwest Independent System Operator (MISO) from January 1, 2007 through December 31, 2008, but did not discover conduct in MISO that warranted further investigation.

5. During the Months of Interest, CCG participated in speculative energy trading in markets including the NYISO, ISO-NE and PJM. In the Months of Interest, CCG's East Power Trading Group participated in the virtual markets in the NYISO and PJM and in the scheduling of DA physical power between the NYISO and ISO-NE, PJM and IESO.

6. In the Months of Interest, CCG's East Power Trading Group also held CFDs, including: swaps that priced off the average DA prices in the NYISO and ISO-NE; swaps that priced off the RT price in PJM; financial transmission rights (FTRs) in ISO-NE and PJM; and transmission congestion contracts (TCCs) in the NYISO.

7. The CFDs investigated by Enforcement were held either in the books of Joseph Kirkpatrick, Managing Director of East Power Trading, or, when Kirkpatrick was stopped-out of his books on at least two occasions, Maxim Duckworth, whose title was Managing Director of Portfolio Management and Trading for all but two of the Months of Interest and of which East Power Trading was a part, placed and held those CFD positions in his book. While the CFDs were in Duckworth's book on these occasions, the virtual and DA physical schedules remained in Kirkpatrick's books.

8. The virtual transactions and DA physical schedules investigated by Enforcement were placed or ordered to be placed predominantly by Michael Pavo, Vice President in East Power Trading, and Jason Hughes, Associate in East Power Trading. Kirkpatrick was Pavo and Hughes' direct supervisor (Kirkpatrick, Pavo and Hughes, collectively, the

East Traders). Duckworth was Kirkpatrick's direct supervisor and the indirect supervisor to Pavo and Hughes.

9. The swap positions held in Kirkpatrick's or Duckworth's books and investigated by Enforcement settled off the monthly average of the DA price of the Zone/region for which the swap was held. The FTR/TCC positions similarly settled off the DA price for the ISO Zone/region in which they were held. The CFDs investigated by Enforcement in the NYISO predominantly settled off the monthly average DA price in Zones A and G and the CFDs investigated by Enforcement in ISO-NE predominantly settled off the monthly average DA price at Mass Hub.

10. For example, for the period of September 2007 through December 2008, the swap positions entering a month ranged in size from approximately 395 MW/h to approximately 12,274 MW/h in NYISO Zone A, from approximately 125 MW/h to approximately 3,682 MW/h in NYISO Zone G, and from 88 MW/h to 3,350 MW/h in ISO-NE Mass Hub. Over that same time frame, the TCC positions held by or for the benefit of Mr. Kirkpatrick's books ranged in size from 25 MW/h to 936 MW/h in Zone A and 450 MW/h to 931 MW/h in Zone G.

11. Enforcement found a repetitive pattern to the virtual and DA physical trading scheduled by the East Traders during the Months of Interest. While the practice varied somewhat from month-to-month and zone-to-zone, the trading behavior can be summarized as follows: (i) when the net CFD position which settled off the average DA price of a region was short, the East Traders entered virtual supply in the Zone/region on which the CFD settled and/or scheduled the import of DA power into the region on which the CFD settled; and (ii) when the net CFD position which settled off the average DA price of a Zone/region was long, East Traders entered virtual load in the Zone/region on which the CFD settled and/or scheduled an export of DA power from the region on which the CFD settled to a neighboring ISO.

12. Thus, for example, when there was an on-peak or off-peak net long CFD position in NYISO Zone A during the Months of Interest, the East Traders generally bid virtual load in Zone A and/or Zone B. In addition, the East Traders also scheduled DA exports of physical power from the NYISO to IESO or from NYISO to PJM. Conversely, when there was an on-peak or off-peak net short CFD position in NYISO Zone A, the East Traders generally offered virtual supply in Zone A. In addition, the East Traders also scheduled DA imports of physical power into New York from IESO and/or into NYISO from PJM.

13. During most of the Months of Interest in which Kirkpatrick held CFD positions in Zone A, he also held a spread between Zone G in the NYISO and ISO-NE. For example, when Kirkpatrick was net long Zone G swaps (and often net short ISO-NE swaps), the East Traders generally bid virtual load in Zones G or H or scheduled DA physical flows from the NYISO to ISO-NE. In some months the East Traders combined these strategies,

for example, by bidding virtual load in Zones G or H at the same time or by combining virtual load bids in Zones G or H with physical flows from the NYISO to ISO-NE.

14. During the Months of Interest the virtual and physical transactions scheduled by the East Traders were routinely unprofitable.

15. CCG's compliance training materials recognized that behavior which was uneconomic on a stand alone basis in order to benefit positions in other markets should not be engaged in by its traders and that the Commission would likely consider this market manipulation.

16. When the NYISO investigated CCG's virtual trading activity in its markets for purposes of examining unwarranted divergence, the NYISO's MMP conducted a conference call with and received written correspondence from CCG. In its communications with the NYISO, CCG stated that its decisions to participate in the NYISO virtual market were based on market fundamentals and omitted the fact that the virtual trading was directly related to its CFDs. Participants on behalf of CCG in the conference call between CCG and the NYISO's MMP included Pavo and Hughes.

III. Violations

A. Enforcement Determined that CCG Engaged in Market Manipulation

17. Enforcement determined that, during the Months of Interest, CCG violated the Commission's Anti-Manipulation Rule, 18 C.F.R. § 1c.2. Specifically, Enforcement determined that CCG entered into virtual and DA physical schedules with the intent of impacting DA prices in the NYISO and ISO-NE to the benefit of the CFD positions held in Kirkpatrick's or Duckworth's books. The Commission's Anti-Manipulation Rule prohibits any entity from: (1) using a fraudulent device, scheme or artifice, or making a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule or regulation, or engaging in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite *scienter*; (3) in connection with a transaction subject to the jurisdiction of the Commission.

18. Enforcement determined that the size of the swap positions held in Kirkpatrick's or Duckworth's books was significant.

19. Enforcement found that Kirkpatrick, Duckworth, Pavo and Hughes each did not concern himself with the profitability of the virtual trades or the DA physical schedules.

20. Enforcement determined that CCG's virtual and DA physical schedules were entered into without regard to their economics or market fundamentals and were instead

entered into solely with the intent to impact DA price in the NYISO and ISO-NE to the benefit of the CFD positions.

21. Specifically, Enforcement determined that during the Months of Interest, when the net CFD position which settled off the monthly average DA price in a region was short, the CFD (and thus CCG) would benefit from a decrease in DA price in that region. Enforcement concluded that the East Traders usually entered virtual supply in and/or imported into the region on which the CFDs were priced. Enforcement found that the price impact of the East Traders' virtual and/or physical behavior was to decrease the DA price in that region, to the benefit of the CFD position.

22. Further, Enforcement determined that during the Months of Interest, when the net CFD position which settled off the monthly average DA price in a region was long, the CFD (and thus CCG) would benefit from an increase in DA price in that region. Enforcement concluded that the East Traders usually entered virtual load in and/or exported out of the region on which the CFDs were priced. Enforcement found that the price impact of the East Traders' virtual and/or physical behavior was to increase the DA price in that region, to the benefit of the CFD position.

23. Enforcement observed evidence of this pattern in the virtual trading and scheduling of DA physical power engaged in by CCG, which demonstrated that the virtual and physical trading behavior supported the CFDs in the Months of Interest. For example, in January 2008 Zone A on-peak, Duckworth's books held a net long CFD position of approximately 7,114 MW/h on average. Beginning in early January 2008, Kirkpatrick's CFDs had been transferred to Duckworth's books when Kirkpatrick was stopped out. Also, at this time, the East Traders bid and cleared approximately 500-800 MW/h of virtual load bids. In addition, the East Traders exported more than 1000 MW/h of day-ahead physical power from the NYISO to Ontario for six on-peak days. Moreover, CCG cleared approximately 400-500 MW/h in virtual load bids for four on-peak days in Zone B. On the other hand, in February Zone A on-peak, the net CFD position became short approximately 2600 MW/h on average and the East Traders cleared an average of approximately 589 MW/h of virtual supply offers. In addition, the East Traders scheduled imports of approximately 397 MW/h on average of DA physical power from IESO to the NYISO for most of the month. For six out of the nineteen on-peak days, those imports were up to 1000 MW/h.

24. Enforcement determined that the NYISO virtual transactions and DA physical trades scheduled by the East Traders for the benefit of Kirkpatrick were often large in volume and were scheduled with regularity and persistency. By way of example, Enforcement found that in on-peak Zone A during the Months of Interest the East Traders' virtual trading represented between approximately 24 and 79 percent of all virtual activity in the Zone when the East Traders placed a trade. Enforcement also concluded that in approximately half of the on-peak Zone A months, the East Traders bid virtually in 100 percent of available hours and only three times did their activity drop

below 60 percent of available hours. In half of the on-peak Zone A activity identified in the Months of Interest, Enforcement found that virtual trading comprised between 30 and 40 percent of the Zone's actual physical load when the East Traders placed a trade. During this same time frame, the East Traders flowed DA on-peak physical power between the NYISO and PJM in 100 percent of the hours in two of the four months identified by staff and their flows represented over 50 percent of the limit of the intertie when it flowed. The East Traders' DA, on-peak physical flows between the NYISO and Ontario ranged in frequency from approximately 20 to 80 percent in the four months identified and averaged between approximately 20 to 80 percent of the available capacity of the intertie when they flowed.

25. During the Months of Interest, Enforcement determined that the East Traders also combined the use of virtuals with scheduling DA physical trading. For example, while the virtuals in Zone A on-peak were being bid 100 percent of the time in January 2008, at a total that represented approximately 27 percent of the Zone's actual load and approximately 48 percent of all virtuals in the Zone, the East Traders were also flowing DA power from the NYISO to Ontario at an amount that approached 80 percent of the available capacity for the intertie when the East Traders flowed for about 30 percent of the hours. And again, for example, in on-peak February 2008, while the East Traders' virtual trading was close to 100 percent of all of the virtuals in Zone H, they also participated in 100 percent of the hours available for flowing power between the NYISO and ISO-NE at an average level that was over 80 percent of the intertie limit when it flowed.

26. Enforcement determined that the DA price was the ultimate arbiter of profitability of the CFD positions held by Kirkpatrick and/or Duckworth, as each of these CFD positions priced off a component of the DA price. In addition, as the volume of the virtual and physical trading engaged in by CCG was so large and so persistently repetitive -- despite the fact that the trades were unprofitable -- Enforcement concluded that CCG intended to impact the DA price in the Zones/regions in which the trading was engaged. Enforcement also determined that through their actions CCG affirmatively impacted the DA price in the various markets in which they engaged in this activity to the benefit of their CFD positions.

27. Enforcement alleged that Kirkpatrick intended to and did manipulate the DA markets in the NYISO and ISO-NE from September 2007 through at least September 2008. Kirkpatrick left the physical employ of CCG in October 2008 although he still remained in a consulting arrangement until late February 2009. Enforcement alleged that Kirkpatrick knew that: (i) physical transactions impact DA price and that he intended to impact price with physical transactions scheduled for his benefit; (ii) virtual transactions impact DA price and that he intended to impact price with virtual transactions scheduled for his benefit; and (iii) the virtual and physical transactions together impact DA price

and that he intended to impact DA price with physical and virtual transactions scheduled for his benefit.

28. Enforcement alleged that Pavo and Hughes intended to and did engage in a scheme to manipulate the DA markets in the NYISO and ISO-NE during the Months of Interest. Enforcement alleged that evidence adduced during the investigation demonstrated that Pavo and Hughes each understood that the DA physical schedules and virtual transactions impacted DA price and that each intended to impact DA price through the placement of those schedules.

29. Enforcement alleged that Duckworth actively participated in the trading scheme to manipulate DA prices in the NYISO and ISO-NE during the Months of Interest. Enforcement alleged that Duckworth took proactive steps to ensure that the East Traders could and would continue to trade virtually and physically to improve the value of Kirkpatrick's CFD positions.

30. Based on these findings, Enforcement determined that CCG intended to and did manipulate the NYISO and ISO-NE DA markets for the benefit of its CFDs during the Months of Interest. Enforcement also determined that Duckworth was a member of upper management and thus CCG's upper management understood the relationship between the virtual and DA physical strategy and the CFDs. Enforcement also determined that information concerning the manner in which the East Traders were trading was available to Duckworth and other CCG senior managers through CCG's electronic database. However, Enforcement determined that no one in upper management, including Duckworth, reviewed these virtual trades and DA physical schedules. In addition, Enforcement determined that while CCG's Risk Management Group was concerned about the size of Kirkpatrick's positions and brought those concerns to the level of upper management, the concerns were not addressed.

31. Enforcement determined that this manipulation of the physical and virtual markets and the respective DA prices resulted in economic losses to market participants who bought and sold energy in the DA markets of ISO-NE and the NYISO. In addition, this manipulation distorted price discovery for all market participants, which contributes not only to trading decisions, but to a variety of industry wide determinations.

32. Enforcement determined that these actions were a fraudulent device, scheme or artifice and that CCG engaged in a course of business that operated as a fraud upon the NYISO and ISO-NE in the Months of Interest in violation of 18 C.F.R. § 1c.2.

B. Enforcement Determined that CCG Violated Accuracy Provisions

33. Enforcement determined that CCG violated the accuracy requirements of Commission regulations, 18 C.F.R. § 35.41(b). Section 35.41(b) of the Commission's regulations applies to CCG because it is a power marketer that is authorized by the

Commission to sell -- and it does sell -- energy, capacity and certain ancillary services at market-based rates in the NYISO, ISO-NE and PJM. This section requires CCG to "provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with…Commission-approved independent system operators, or jurisdictional transmission providers, unless Seller exercises due diligence to prevent such occurrences."

34. Enforcement determined that CCG violated 18 C.F.R. § 35.41(b) by affirmatively providing misleading information to the NYISO. Specifically, Enforcement determined that CCG denied that its virtual transactions were related to its CFDs and instead told the NYISO MMP that the transactions were independent of the CFD positions and were entered into based on market fundamentals.

35. Enforcement further determined that CCG's failure to provide accurate information to the NYISO MMP provided additional evidence to Enforcement of CCG's scheme to manipulate the virtual and physical markets to impact DA price.

IV. Remedies and Sanctions

36. For purposes of settling any and all civil and administrative disputes arising out of, related to, or connected with Enforcement's Investigation, CCG agrees with the facts as stipulated in Section II of this Agreement but neither admits nor denies the violations described in Section III of this Agreement. CCG agrees to take the following actions:

A. Disgorgement

37. CCG shall disgorge unjust profits and interest of $110,000,000 within ten business days after the direction set forth in subpart (g) below. The entirety of the $110,000,000, which is not a civil penalty, shall be distributed as follows:

a. a total of $6,000,000 will be distributed directly to and equally among the NYISO, ISO-NE, PJM, Midwest-ISO, Southwest Power Pool and the California ISO for the purposes of purchasing computer hardware and/or software that improves their respective surveillance and analytic capabilities, in consultation with the Commission's Director of the Office of Enforcement;

b. the remaining funds will be deposited, as follows, into a fund for the benefit of electric energy consumers in the affected states within the NYISO ($78,000,000), ISO-NE ($20,000,000) and PJM ($6,000,000) (the Fund);

c. any requests for apportionment of the monies in the Fund by the affected states within the NYISO, ISO-NE and PJM may only be

made by the appropriate state agency or agencies of those respective states, including, for example, state public service commissions, state attorneys general, or state consumer advocates, for the benefit of electric energy consumers;

d. these requests will be filed with and decided by a Commission Administrative Law Judge (ALJ);

e. the apportionment process will be determined by the ALJ;

f. neither CCG nor any of its successors or affiliates, or their agents officers, directors or current or former employees, or related entities shall have any role, including, but not limited to the role of intervenor or amicus, in the ALJ's apportionment of the funds or any proceedings concerning the requests made for apportionment of the monies in the Fund;

g. CCG will deposit the monies for the Fund into a United States Treasury account, as directed by the Commission's Director of the Office of Enforcement, and CCG will provide the monies specified above in subparagraph (a) to the ISOs and RTOs pursuant to the direction of the Commission's Director of the Office of Enforcement; and

h. the final disposition of the Fund, including the amount of each allocation and identity, to the extent known, of the recipient(s) shall be made public by the ALJ.

B. Civil Penalty

38. CCG shall pay a civil penalty of $135,000,000 to the United States Treasury, by wire transfer, within ten business days after the Effective Date of this Agreement, as defined below.

C. Compliance

39. Since the onset of Enforcement's investigation, CCG has taken steps to implement enhancements to its compliance program. Specifically, CCG instituted a new policy and process to monitor profit and loss concentrations in virtual transactions and physical schedules of electric energy and to review and document the purpose of virtual transactions. This monitoring had not been done previously. The monitoring is to be performed in a manner such that improper trading may be readily identified by CCG should it occur in the future.

40. In addition to the enhancements already in effect at CCG as described above, CCG agrees that CCG, and any successor companies, develop and enforce policies which require that communications by its traders, including but not limited to instant messaging (IMs), email, and phone calls, will be retained by CCG for a period of no less than five years. In addition, CCG agrees that CCG, and any successor companies, set up a system whereby such communications will be regularly monitored by its compliance group for potential irregularities or illegalities. CCG agrees that these policies will be made fully effective within 90 days after the Effective Date of this Agreement.

41. CCG shall adopt or maintain compliance measures and procedures related to its trading of jurisdictional products, including virtual transactions, scheduling of physical power, TCCs and FTRs. These measures shall include improved training for its traders, supervisors, and managers regarding the Commission's regulations prohibiting manipulation of jurisdictional energy markets and the Commission's regulations governing energy trading, including the adherence to the tariffs in the organized markets in which CCG participates and providing accurate information to the Commission, RTOs and ISOs. CCG shall make semi-annual compliance monitoring reports to Enforcement for two years following the Effective Date of this Agreement. The first semi-annual compliance monitoring report shall be submitted no later than ten days after the end of the second calendar quarter after the quarter in which the Effective Date of this Agreement falls. The period covered by the report shall consist of the six months ending one calendar month prior to the date of such report. The second semi-annual compliance monitoring report shall be submitted six months thereafter for the six month period succeeding the prior reporting period. The third and fourth semi-annual compliance monitoring reports shall follow the same schedules.

42. Each compliance monitoring report shall: (1) advise Enforcement whether violations of Commission regulations have occurred during the applicable period; (2) provide a detailed update of all compliance measures and procedures instituted, and compliance training administered, by CCG in the applicable period, including a description of the compliance measures and procedures instituted, the compliance training provided to all relevant personnel concerning the Commission's energy trading, accuracy and anti-manipulation regulations, and a statement of the personnel or other evidence demonstrating that the personnel have received such training and when the training took place; and (3) include an affidavit executed by an officer of CCG that the compliance monitoring reports are true and accurate. Upon request by Enforcement, CCG shall provide to Enforcement documentation to support its reports. After the receipt of the fourth semi-annual report, Enforcement may, at its sole discretion, require CCG to submit semi-annual reports for one additional year.

43. Moreover, CCG represents that by the Effective Date of this Agreement, its current employees, Duckworth, Pavo and Hughes, shall be removed from any position at CCG where any of these individuals engage in or perform any duties related to managing, directing, or engaging in wholesale physical and financial energy trading (a CCG Trading Position). CCG similarly agrees that Duckworth, Pavo and Hughes will not hold any CCG Trading Position as long as each is within the employ of CCG or any successor or affiliate. Kirkpatrick is not currently employed by CCG, and will not hold any CCG Trading Position in the future.

V. Terms

44. The Effective Date of this Agreement shall be the later of the date on which: (a) the Commission issues an order approving this Agreement without material modification; or (b) the merger pursuant to the Agreement and Plan of Merger among Constellation Energy Group, Inc., Exelon Corporation, and Bolt Acquisition Corporation, dated April 28, 2011, is consummated. When effective, this Agreement shall resolve the matters specifically addressed herein as to CCG and any affiliated entity, and their agents, officers, directors and employees, both past and present, and any successor in interest to CCG.

45. Upon the Effective Date of this Agreement, the Commission shall release CCG and any successor or affiliate, Kirkpatrick, Pavo, Hughes, and Duckworth and forever bar the Commission from holding CCG and any successor or affiliate, and their respective agents, officers, directors and employees, both past and present, liable for any and all administrative or civil claims, known or unknown, arising out of, related to, or connected with the Investigation as defined in this Agreement. Moreover, upon the Effective Date of this Agreement, the Investigation of CCG, Kirkpatrick, Pavo, Hughes, and Duckworth shall terminate.

46. CCG's failure to: (a) make a timely civil penalty payment; (b) make a timely disgorgement payment as set forth in paragraph 37 above; (c) comply with the compliance requirements specified herein; or (d) comply with any other provision of this Agreement, shall be deemed a violation of a final order of the Commission issued pursuant to the Federal Power Act, 16 U.S.C. § 792, *et seq.*, and may subject CCG and any successor companies to additional action under the enforcement and penalty provisions of the Federal Power Act.

47. If CCG fails to make the civil penalty and disgorgement payments described above at the times agreed by the parties, interest payable to the United States Treasury will begin to accrue pursuant to the Commission's regulations at 18 C.F.R. § 35.19a(a)(2)(iii)(A) (2011) from the date the payments are due, in addition to any other enforcement action and penalty that the Commission may take or impose.

48. This Agreement binds CCG and its agents, successors, and assigns. The Agreement does not create any additional or independent obligations on CCG, or any affiliated entity, its agents, officers, directors, or employees, other than the obligations identified in this Agreement.

49. The signatories to this Agreement agree that they enter into the Agreement voluntarily and that, other than the recitations set forth herein, no tender, offer, or promise of any kind by any member, employee, officer, director, agent, or representative of Enforcement or CCG has been made to induce the signatories or any other party to enter into the Agreement.

50. Unless the Commission issues an order approving this Agreement in its entirety and without material modification, the Agreement shall be null and void and of no effect whatsoever, and neither Enforcement nor CCG shall be bound by any provision or term of this Agreement, unless otherwise agreed to in writing by Enforcement and CCG.

51. In connection with the payment of the civil penalty provided for herein, CCG agrees that the Commission's order approving this Agreement without material modification shall be a final and unappealable order assessing a civil penalty under § 316A(b) of the Federal Power Act, 16 U.S.C. § 825o-1(b). CCG waives findings of fact and conclusions of law, rehearing of any Commission order approving this Agreement without material modification, and judicial review by any court of any Commission order approving this Agreement without material modification.

52. This Agreement may be modified only if in writing and signed by CCG and Enforcement. No waiver of any provision of this Agreement or departure from any term of this Agreement shall be effective unless in writing and signed by CCG and Enforcement. No modification will be effective unless any approval of the Commission that may be required with respect to such modification has been received.

53. Each of the undersigned warrants that he or she is an authorized representative of the entity designated, is authorized to bind such entity, and accepts this Agreement on the entity's behalf.

54. The undersigned representative of CCG affirms that he or she has read this Agreement, that all of the matters set forth in this Agreement are true and correct to the best of his or her knowledge, information, and belief, that he or she understands that this Agreement is entered into by Enforcement in express reliance on those representations, and that he or she has had the opportunity to consult with counsel.

55. This Agreement may be signed in counterparts.

Agreed to and Accepted:

Norman C. Bay	CCG
Director, Office of Enforcement	By: Charles A. Berardesco
Federal Energy Regulatory Commission	Its: Corporate Secretary
Date: 3.8.12	Date: 3-8-12

QUESTIONS FOR THE RECORD: Mr. Norman Bay
LAM Question #5

Question 5. On March 8, 2012, you signed a Stipulation and Consent Agreement with a subsidiary of Constellation Energy Group, a company that at that same time was a party to an Agreement and Plan of Merger for which FERC's regulatory approval was required. In fact, the Stipulation and Consent Agreement makes reference to the merger transaction. The Stipulation and Consent Agreement was approved by the Commission on March 9, 2012. Are you aware of any information that would suggest a connection between the Enforcement Settlement you signed on March 8 and the approval of both the Enforcement Settlement and the merger itself on the very next day, March 9?

A. Are you concerned about the appearance of a quid pro quo in a connection between merger reviews and enforcement?

Answer: I would be concerned about the appearance of a quid pro quo in a connection between merger reviews and enforcement.

B. Are you aware of any information that would suggest a connection between the resolution of the enforcement matter and the approval of the merger?

Answer: As your question notes, the Stipulation and Agreement makes reference to the merger. To my knowledge, the Commission resolved the Exelon-Constellation merger consistent with the requirements of section 203 of the Federal Power Act, and the Commission approved the resolution of the enforcement matter consistent with the relevant Federal Power Act provisions and implementing regulations. Moreover, the merger review was led by staff from the Commission's Offices of General Counsel and Energy Market Regulation while the investigation into Constellation Energy Commodities Group trading activities was conducted separately by staff from the Office of Enforcement.

C. Did you, then-Chairman Wellinghoff, or anyone else at FERC to your knowledge ever indicate to the parties in the Exelon-Constellation merger that it would be prudent to settle the pending enforcement matter in order to get their merger approved?

Answer: To the best of my recollection, I did not indicate to the parties in the Exelon-Constellation merger that it would be prudent to settle the pending enforcement matter to get the merger approved. I do not know whether anyone else at FERC did so.

D. Why did the enforcement settlement specifically allow the companies to not have to pay the fines until the merger was approved?

Answer: The Commission determined that accepting the settlement, including this provision, would be in the public interest.

E. What assurances will you give us that if you are confirmed there will be no such connection in merger proceedings or market power review of any kind more generally?

Answer: Section 203(a)(4) of the Federal Power Act states:
After notice and opportunity for hearing, the Commission shall approve the proposed disposition, consolidation, acquisition, or change in control, if it finds that the proposed transaction will be consistent with the public interest, and will not result in cross-subsidization of a non-utility associate company or the

pledge or encumbrance of utility assets for the benefit of an associate company, unless the Commission determines that the cross-subsidization, pledge, or encumbrance will be consistent with the public interest.

16 U.S.C. § 824b (a)(4). As such, the Commission must consider the public interest in its review of a proposed merger. Each proposed merger must be reviewed based on its own unique facts and circumstances. Thus, I cannot prejudge any matters that might be filed before the Commission. However, I can provide you assurances that if I am confirmed, Commission staff would perform merger review and market power review in a manner that is consistent with all applicable statutes, regulations, and orders.

UNITED STATES OFFICE OF PERSONNEL MANAGEMENT
Washington, DC 20415

Merit System Audit
and Compliance

MAR 08 2013

Mr. Eduardo Ribas
Chief Human Capital Officer
Federal Energy Regulatory Commission
Eduardo.ribas@ferc.gov

Dear Mr. Ribas:

On February 20, 2013, the Federal Energy Regulatory Commission (FERC) requested approval to appoint Mr. Norman Bay to the position of Director, Office of Enforcement, ES-0340. Mr. Bay currently serves under a noncareer SES appointment in the same position. The position to which he would be appointed is in the career SES.

We reviewed your request to ensure Mr. Bay's appointment is free of political influence and complies with merit system principles. As discussed below, Mr. Bay's appointment to this particular position is against regulation and, as a result, I must deny your request.

According to your request, FERC's Chairman determined that the Director, Office of Enforcement position needed to be filled by a career SES member to ensure impartiality. FERC competed the position and referred two candidates for selection, including Mr. Bay.

Since this would be Mr. Bay's initial career SES position, a Qualifications Review Board (QRB) must certify his executive qualifications prior to appointment. However, 5 CFR 317.502(e) states that an action to convert a noncareer-type employee to a career SES appointment in the employee's current position or a successor to that position cannot be forwarded to a QRB. This regulation defines a "noncareer-type" position to include a noncareer SES appointee.

We recognize that the proposed position identifies additional duties related to energy and financial market analytics and surveillance; however, these duties do not significantly alter the original position. The proposed position is identical, or a successor, to the current position. Because Mr. Bay has served in this same position under a noncareer SES appointment for the past three years, his selection cannot be forwarded to a QRB. Consequently, I must deny FERC's request because it violates 5 CFR 317.502(e).

If you or your staff have any questions or need further information about this decision, please contact Ms. Ana A. Mazzi, Deputy Director, at (202) 606-4309 or at ana.mazzi@opm.gov.

Sincerely,

Mark W. Lambert

Mark W. Lambert
Associate Director
Merit System Audit and Compliance