

November 16, 2007

Enforcement Policy – the Practitioners' View

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Presented at the FERC Conference on Enforcement

Issue: Due Process

I. Investigation Stage

A. Privilege

An investigated party should not be required to waive attorney-client privilege. Staff respected attorney-client privilege in a case in which I was involved and should make it a policy to continue this practice. This is important for many reasons including the fact that related civil litigation may be ongoing.

B. Open-Minded Investigations

In a case in which I was involved, at the beginning of the process, I found the Staff to be more prosecutorial than investigative. It seemed as if OE Staff was trying to prove that my client had engaged in wrongful conduct instead of conducting an open-minded investigation. However, as the investigation progressed, we found OE Staff to be open to receiving any information that we wanted to submit and to meeting as often as we requested. In the end, we were able to convince the Staff on a number of important factual and legal issues. Although I recognize that the "Report on Enforcement" issued on November 14, 2007 describes the role of OE Staff as prosecutorial, I suggest that during the investigative stage, OE should be less prosecutorial and more investigative. I also suggest that care be taken not to make public statements about matters pending before the Commission because this can give an impression of pre-judgment by the Commission or its senior staff.

C. Related Civil Litigation

As mentioned above, in some cases, a company being investigated by the Commission may also be involved in civil litigation involving the same or related issues. The Commission should be aware that private litigants have a very different agenda. They are not concerned with compliance with the Commission's rules and regulations, but rather with obtaining a financial judgment. This means that the OE Staff must be careful that it not become a tool for plaintiffs to obtain discovery and understand the need for the investigated company to coordinate actions on the FERC investigative side with what is also best for the civil litigation. In particular, if a settlement is reached, OE Staff should accommodate the need for careful drafting so as not to cause an adverse impact in the related civil litigation. In my recent case, OE Staff was very cooperative on this front.

II. Post-Investigation

A. Wells Submission

First, if a case is not settled following non-public investigation by OE Staff, the party being investigated should have the opportunity to submit its views in writing to the Commission on a confidential basis before (as opposed to after) the Commission issues a Notice of Proposed Penalty. This process has been used by the SEC ("Wells Submission") for the last 35 years. (SEC Reg Section 202.5(c).

SEC practitioners report that this has been very helpful and that it has increased the basic fairness of the process. I understand that the Commission considered, but rejected this option when it issued its "Statement of Administrative Policy Regarding the Process for Assessing Civil Penalties." The Commission should reconsider this decision.

B. Non-Public Settlement Procedures

Second, if a settlement cannot be reached during the investigative part of the case, the Commission should be open to the use of settlement procedures on a non-public basis. This would include use of a settlement judge or the Commission's ADR staff. Utilization of an independent third party who could assess the positions of OE Staff versus the investigated company could prove to be very valuable. Protracted litigation could be avoided and the Commission's goal of obtaining compliance could be more expeditiously achieved. Given the Commission's well known support for the use ADR and other settlement procedures, I assume that the Commission will endorse the use of such procedures in the context of OE matters.

C. Notice of Proposed Penalty

Third, if case is not settled, the Commission's Statement of Process provides for the issuance of a Notice of Proposed Penalty and the opportunity for the subject of the Notice to respond to the proposed penalty. However, in the Amaranth and ETP cases, the Commission did not just issue a Notice of Proposed Penalty. It also issued an Order to Show Cause. In both of these cases, the Order seems to adopt the allegations of OE Staff as fact and places the burden on the subject of the investigation to prove that a violation has not occurred.

A better procedure would be to issue a brief order that simply sets forth the allegations and sets the matter for hearing (note – I am not addressing whether the hearing is before an ALJ or a federal district court because this issue is pending before the Commission in the ETP case). If the investigated party has previously been given the opportunity to make a Wells Submission, there would be no need to issue a Show Cause Order at this stage. This procedure also would avoid the appearance of “pre-judging” whether a violation has occurred (which has been a criticism in both the ETP and Amaranth cases).

The current practice of simply calculating the maximum possible penalty also should be reconsidered. First, if the Commission is setting the allegations for hearing, it is premature to address what level of penalty would be appropriate. Second, the practice of simply calculating the maximum possible penalty may make settlements harder to achieve. The concern is that when the Commission starts the process with very high proposed penalties, it will be very difficult to convince the Commission (or its Staff) that a much smaller or even no penalty is appropriate. (Note – this is know as “anchoring”- *i.e.*, when a party becomes wedded to its initial position and is unwilling to change even when presented with new facts).

Finally, I note that the SEC follows the practice that I am suggesting – *i.e.*, it issues an order that simply sets forth the allegations. The order does not make preliminary findings of fact and does not set forth a proposed penalty. *See e.g.*, Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, File No. 3-12738 (Aug. 24 2007).

Issue: Compliance/Self reporting

The Commission's Notice asked this panel to address the issue of self-reporting. Schiff Hardin strongly encourages our clients to implement comprehensive internal compliance programs that include training. We have been involved in creating and implementing compliance programs for clients and believe that these programs have been very successful in increasing compliance and in identifying areas where improvement is needed. We have definitely seen an increase in the instances in which advice is sought on how to proceed.

The Commission should be aware, however, that there is a perception that even a self-report with no harm to the public and no gain to the self-reporter will still “cost” the client \$500,000 to \$1 million. This is not helpful when you are urging a client to self-report. It is also contrary to the Commission's primary objective, which is to encourage compliance.

The Staff Report takes a step in the right direction by reporting on the number of cases that have not resulted in penalties. The Commission also should consider other options such as warning letters, cease and desist orders, expanded use of no action letters, and offers of amnesty in order to encourage self-reporting.

About the Author

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She is Past President of the Energy Bar Association (EBA), a national professional association of approximately 2,100 attorneys and other energy professionals. She also is a past Delegate for the EBA to the American Bar Association's House of Delegates.

Ms. Heffernan has represented numerous clients before the Federal Energy Regulatory Commission (FERC) and the federal courts for almost 30 years on a variety of matters concerning the regulation of natural gas and electricity:

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