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FERC Enforcement

The Federal Energy Regulatory Commission is finally ramping up its enforcement efforts, using new powers in the 2005 Energy Policy Act. The investigative approach now resembles that of other agencies policing trading markets, such as the SEC and the CFTC. Many companies have yet to adjust to the new reality, however, especially FERC's increasing focus on individual targets, authors Steven F. Reich, James J. Benjamin and J. Porter Wiseman of Akin Gump Strauss Hauer & Feld, LLP write.

Things can get particularly fouled up when a company fails to realize the need to retain separate counsel for affiliated individuals caught up in a FERC probe.

New Perils of Joint Representation of Corporations, Individuals in FERC Enforcement Proceedings

BY STEVEN F. REICH, JAMES J. BENJAMIN AND J. PORTER WISEMAN

Federal Energy Regulatory Commission ("FERC") enforcement has become increasingly aggressive and sophisticated in the nine years since the Energy Policy Act of 2005 ("EPAct")¹ vested the agency with authority to investigate and prosecute manipulation of the electricity and natural gas markets. Although

¹ 42 U.S.C. §§ 15801- 16538 (2012).

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it took time for FERC to ramp up its enforcement efforts, today its investigative approach to enforcement proceedings increasingly resembles that of other government agencies responsible for policing trading markets, such as the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC").

FERC has expanded its Office of Enforcement to more than 200 staff members, and in the past two years assessed the two largest penalties in its history, totaling nearly \$900 million in fines and disgorgement.² Moreover, FERC has begun to pursue individuals in addition to companies, in one case imposing penalties of \$1 million on each of three energy traders and \$15 million on the supervising trader.³

Despite the dramatic expansion of FERC's enforcement authority and the agency's increasing focus on individuals, targets of that authority have yet to fully embrace certain defense practices that are standard outside the FERC context. One such area is the retention

² FERC Office of Enforcement, *2012 Report on Enforcement 4*, (Nov. 15, 2012), available at <http://www.ferc.gov/legal/staff-reports/11-15-12-enforcement.pdf>; FERC Office of Enforcement, *2013 Report on Enforcement 2*, 14 (Nov. 21, 2013), available at <http://www.ferc.gov/legal/staff-reports/2013/11-21-13-enforcement.pdf>.

³ *Barclays Bank PLC*, 144 FERC ¶ 61,041 (2013).

of separate counsel for affiliated individuals caught up in agency investigations. Companies facing SEC and CFTC investigations routinely hire separate counsel to represent directors, officers and employees rather than rely on corporate counsel to represent both the company and those individuals.

This standard defense approach has been slow to catch on in FERC enforcement investigations, however, even though simultaneous representation of a company and its constituents poses many of the same risks existing in SEC or CFTC proceedings. As discussed below, the SEC has identified the joint representation of companies and their personnel as a concern in its own proceedings and we see little reason why those same concerns do not apply in FERC matters.

Whether counsel for a company can also represent individual employees of the company in the same matter is a question that arises in a number of different legal contexts. In criminal investigations, the representation of multiple defendants potentially raises both constitutional and ethical concerns.⁴ Courts may disqualify attorneys representing multiple clients if a conflict of interest exists, and prosecutors are ethically obligated to voice concerns if they perceive conflicts among a defense attorney's clients.⁵

Risks of Joint Representation. Although civil (*i.e.*, non-criminal) investigations do not raise the same constitutional concerns, simultaneous representation of companies and their personnel nevertheless may be ethically problematic and create strategic problems that can outweigh the perceived benefits of a unified defense. Indeed, it is not unheard of for counsel to be disqualified by a government agency from simultaneously representing a company and its constituents in an administrative proceeding.⁶

To be sure, separate counsel for a company and its constituents is not necessary in every FERC matter. In some cases, the interests of the company and its personnel will be sufficiently aligned that joint representation may be permissible. However, we believe greater attention to the risks of multiple representation in FERC enforcement proceedings is appropriate in light of the changing regulatory landscape⁷ and that, consistent with standard practice in enforcement matters conducted by other regulatory agencies, a company should retain separate counsel for affected individuals when

⁴ See *e.g.*, *United States v. Curcio*, 680 F.2d 881 (2d Cir. 1982) (representing multiple defendants in a single matter may implicate the Sixth Amendment right to effective assistance of counsel).

⁵ See *id.*; ABA, MODEL RULES OF PROF'L CONDUCT R. 3.8 cmt. ("ABA Model Rules") (discussing a prosecutor's ethical obligation to ensure that a defendant is afforded procedural justice).

⁶ In re Blizzard, SEC Release No. 2032, 77 SEC Docket 1335, 2002 WL 714444 (Apr. 24, 2002) (disqualifying attorney from representing any witness that might be called against the existing client, although no actual conflict yet existed).

⁷ A 2004 New York City Bar Association formal opinion on the subject of multiple representations is essential reading for lawyers confronting these issues. See Association of the Bar of the City of New York, *Formal Op. 2004-02: Representing Corporations and Their Constituents in the Context of Government Investigations* (2004).

the company's interests appear likely to diverge from those of its directors, officers or employees.⁸

Recent Exercises of FERC's Enforcement Authority Have Changed the Joint Representation Calculus

When a company becomes the target of an investigation conducted by FERC's Office of Enforcement, the question typically arises whether the company will provide counsel for individuals who become embroiled in the matter. Depending on the nature of the investigation, the positions within the company held by the affected individuals, and the state in which the company is incorporated, the provision of counsel may actually be mandatory under controlling state law and/or the company's bylaws. In other instances, although not mandatory, the provision of counsel for individuals may be a wise decision both as a legal and as a business matter. Once the decision is made that individuals should be provided with counsel, however, a further question arises as to whether counsel for the company can also serve as counsel for its directors, officers and employees.

Prior to the passage of EPAct, joint representation of individuals by company counsel in most FERC matters made sense.

Prior to the passage of EPAct, joint representation of individuals by company counsel in most FERC matters made sense. Before 2005, FERC enforcement actions were rare, and because its civil penalty authority was limited, FERC largely relied on its regulatory powers to remedy misconduct.⁹ Back then, FERC "enforcement" was usually conducted through complaint procedures, and utility employees rarely, if ever, faced personal legal consequences as a result of FERC action.

Perceived Advantages of Joint Representation. Given this regulatory landscape, companies subject to FERC jurisdiction understandably became comfortable relying on the same counsel to represent both its interests and those of its constituents when FERC-related inves-

⁸ The extent to which conflicts of interest may or may not be curable by obtaining conflict waivers from the affected parties is beyond the scope of this article.

⁹ Even as late as 2002, FERC's Office of General Counsel, then responsible for enforcement, was conducting a grand total of only 37 ongoing investigations, 30 of which were non-public and preliminary. See Suedeem G. Kelly, Comm'r, FERC, *Administrative Law Implications of Protecting Consumers in a Changing Regulatory Landscape, Presentation Before the Institute on Natural Resources and Environmental Administrative Law and Procedure* (Sept. 16, 2004). Those 37 investigations would have included FERC's probes into Enron and the Western Energy Crisis of 2000-2001. Currently, FERC does not report the number of ongoing investigations. However, it reported opening 24 new investigations and resolving 29 investigations in 2013 alone. FERC Office of Enforcement, *2013 Report on Enforcement 2*, 14 (Nov. 21, 2013), available at <http://www.ferc.gov/legal/staff-reports/2013/11-21-13-enforcement.pdf>.

tigations arose. At first glance, joint representation of a company and its personnel seems efficient, particularly because fewer lawyers will have to be engaged to learn the same set of facts.

Joint representation can also avoid creating the impression with regulators that meaningful differences exist between the interests of the company and those of its constituents. And, perhaps the greatest perceived advantage of joint representation is control of strategy and information: company counsel has access to all of the major players in the investigation as well as the information in their possession and, unless the agency objects, will be able to attend all of the agency's constituent interviews.¹⁰

Whatever truths these perceptions may have reflected prior to the passage of EAct, FERC's recent ramp-up of its enforcement efforts, together with its new-found focus on individual culpability, has altered the relevant legal considerations. Generally speaking, over the past few years there has been a noticeable increase in the attention paid by market regulators to the issue of joint representations. For example, a 2011 speech by Robert S. Khuzami, then director of the SEC's Division of Enforcement, criticized the practice of joint representations when the company and its constituents have differing interests. Khuzami cautioned that going forward, the SEC was likely to raise concerns about situations in which joint representations were undertaken when the agency believed they should not have been.

A market manipulation investigation will often focus on the state of mind of the individuals involved.

The concerns expressed by Khuzami are equally applicable to market manipulation investigations undertaken by FERC under EAct. A market manipulation investigation will often focus on the state of mind of the individuals involved.¹¹ As FERC has made clear, "legal trading activities, standing alone, are insufficient to state a manipulation claim; such activities must be willfully combined with something more. And it is often scienter—i.e., manipulative intent—that is the only factor that distinguishes legitimate trading from improper manipulation."¹²

In market manipulation cases, FERC will therefore be deeply interested in the knowledge and intent of the corporate constituents who allegedly carried out a manipulative scheme, because, legal fictions aside, only individuals and not their corporate employer can have manipulative intent. Given this investigative focus, the interests of the company and of implicated individuals

¹⁰ FERC's procedural rules do not allow the counsel for another witness to be present during witness interviews, unless that counsel also represents the witness being interviewed. 18 C.F.R. § 1b.16(b).

¹¹ *Prohibition of Energy Mkt. Manipulation*, 114 FERC ¶ 61,047, at P 49, 52 (2006) ("Market Manipulation Order").

¹² *Barclays Bank PLC*, 144 FERC ¶ 61,041, at P 55 (2013) (internal quotations omitted).

may diverge sharply. If a trader is accused of market manipulation, then key questions for FERC are likely to be whether that individual was acting on direction, explicit or implicit, from the company, and whether she was properly trained and supervised.

This new conflict between the interests of the company and its personnel may be amplified because FERC,¹³ like the SEC,¹⁴ the CFTC,¹⁵ and the DOJ,¹⁶ rewards cooperation with its inquiries. As a result, in some instances it may be in the interests of the company to portray the individuals (if they engaged in manipulative trading) as "rogue traders" and to cooperate with a FERC enforcement inquiry. Alternatively, individuals may claim that they were following direction from their superiors, or that they lacked proper training and supervision, and likewise seek to cooperate with the investigation against their employer. Either way, the potential for conflict is greatly heightened in this new investigative era, as is the need for separate counsel for companies and their constituents.

Market Regulators Disfavor Joint Representations and Few Companies Will View a Fight Over the Issue as Worthwhile

Apart from the legal and ethical concerns discussed above, there are purely practical reasons why targets of FERC enforcement actions (as well as their counsel) should consider separate counsel for affected personnel early in the investigative process. Most significantly, government regulators may perceive a company's decision to authorize joint representation as a "circling of the wagons" intended to impede the agency's access to information and thereby impede its enforcement efforts.

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To address the potential for such conflicts, FERC's procedural rules already require that counsel representing more than one client inform the agency of that fact and identify his or her multiple representations:

When counsel does represent more than one person in an investigation, for example, where the counsel is counsel to the witness and his employer, said coun-

¹³ *Revised Policy Statement on Penalty Guidelines*, 132 FERC ¶ 61,215, at PP 145, 152, 154 (2010) ("Revised Policy Statement"); FERC Penalty Guidelines § 1C2.3(g)(3) (attached to Revised Policy Statement).

¹⁴ See SEC Division of Enforcement, Enforcement Manual § 6 (Oct. 9, 2013), available at <http://www.sec.gov/divisions/enforce/enforcementmanual.pdf>.

¹⁵ See CFTC, PR296-07, Enforcement Advisory: Cooperation Factors in Enforcement Division Sanction Recommendations (Mar. 1, 2007), <http://www.cftc.gov/ucm/groups/public/cpdisciplinaryhistory/documents/file/enfcooperation-advisory.pdf>.

¹⁶ U.S. Dep't of Justice, United States Attorneys' Manual 9-28.700, 720 (2014), http://www.justice.gov/usao/eousa/foia_reading_room/usam/index.html.

sel shall inform the Investigating Officer and each client of said counsel's possible conflict of interest in representing that client and, if said counsel appears with a witness giving testimony on the record in an investigation, counsel shall state on the record all persons said counsel represents in the investigation.¹⁷

FERC also has the power to disqualify counsel for misconduct and unethical behavior,¹⁸ and that may include the power to exclude counsel with irresolvable conflicts, although that authority is not expressly stated in the agency's procedural rules.¹⁹

Thus, a company's insistence on joint representation can undermine the credibility of both the company and

its counsel with the agency. Few companies caught up in a FERC market manipulation investigation will want to undertake a separate fight over these representation issues at the same time they are attempting to persuade the agency that they are fully cooperating with the review. For this very practical reason, companies are well-advised to seek separate counsel for their personnel in these matters when conflicts appear likely.

Conclusion

FERC's recent aggressive use of its investigative authority under EPAct, and its increased focus on individuals, have changed the landscape for joint representations in FERC enforcement matters. Targets of FERC's Office of Enforcement and their counsel would be well-advised to consider—early in the investigative process—whether company personnel caught up in the review should be provided with separate counsel.

¹⁷ 18 C.F.R. § 1b.16(b).

¹⁸ *Id.* at §§ 1b.16(c)(4), 385.2101

¹⁹ *Id.*