

147 FERC ¶ 61,130  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Cheryl A. LaFleur, Acting Chairman;  
Philip D. Moeller, John R. Norris,  
and Tony Clark.

BP America Inc.  
BP Corporation North America Inc.  
BP America Production Company  
BP Energy Company

Docket No. IN13-15-000

ORDER ESTABLISHING HEARING

(Issued May 15, 2014)

1. This order establishes a hearing to determine whether BP America Inc., BP Corporation North America Inc., BP America Production Company, and BP Energy Company (collectively, BP) violated section 1c.1 of the Commission's regulations, 18 C.F.R. § 1c.1 (2013), and section 4A of the Natural Gas Act (NGA), 15 U.S.C. § 717c-1 (2012), and to ascertain certain facts relevant for any application of the Commission's Penalty Guidelines.<sup>1</sup>

**I. Background**

2. On August 5, 2013, the Commission issued an Order to Show Cause (Show Cause Order)<sup>2</sup> directing BP to show cause why the Commission should not find that BP manipulated the next-day, fixed-price natural gas market at Houston Ship Channel from September through November 30, 2008. In the staff report accompanying the Show Cause Order (Staff Report), staff of the Office of Enforcement (OE Staff) allege that BP made uneconomic sales at Houston Ship Channel and took steps to increase its market share at Houston Ship Channel as part of a manipulative scheme to suppress the Houston Ship Channel *Gas Daily* index, and that this scheme was motivated by a desire to benefit certain physical and financial positions held by BP whose price was set by the same

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<sup>1</sup> *Revised Policy Statement on Penalty Guidelines*, 132 FERC ¶ 61,216 (2010).

<sup>2</sup> *BP America Inc.*, 144 FERC ¶ 61,100 (2013) (Show Cause Order).

index.<sup>3</sup> OE Staff further alleges that BP's transport and trading of gas was done with scienter, and was in connection with jurisdictional transactions.<sup>4</sup>

3. In particular, OE Staff alleges that BP devised this scheme after it discovered that some of its financial positions had benefited when the spread between daily physical gas prices at Houston Ship Channel and Henry Hub grew wider in the aftermath of Hurricane Ike in September 2008, and that, if the spread persisted, such financial positions had the potential to be worth millions of dollars.<sup>5</sup> To further this scheme, BP allegedly increased its net long physical gas positions and engaged in trading and transport of gas from Katy to Houston Ship Channel (e.g., BP sold gas shipped from Katy to Houston Ship Channel at prices that did not meet or exceed the variable cost to transport).<sup>6</sup> BP allegedly began a pattern of early and heavy fixed-price trading of physical gas at Houston Ship Channel at prices consistently below the Houston Ship Channel and Katy daily averages.<sup>7</sup> As OE Staff states, BP focused its trading early in the day in order to "frame the [Houston Ship Channel] market" and influence the development of the volume-weighted average price on which the Houston Ship Channel *Gas Daily* index was based.<sup>8</sup> Thus, BP's traders allegedly "were hitting bids more often than waiting to have their offers lifted" at Houston Ship Channel, and traded even before the Katy market opened or at lower prices when Katy physical gas prices were higher, in order to suppress prices at Houston Ship Channel and, therefore, the Houston Ship Channel *Gas Daily* index.<sup>9</sup>

4. The Show Cause Order further directed BP to show why it should not pay NGA civil penalties in the amount of \$28,000,000 and disgorge \$800,000 in unjust profits, plus interest, resulting from market manipulation, or a modification to these amounts as warranted.

5. On October 4, 2013, BP filed an answer and motion to dismiss (BP Answer). BP moved for dismissal of this proceeding with no further action on grounds that the Staff

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<sup>3</sup> *Id.* P 2.

<sup>4</sup> *Id.*, Staff Report at 35, 69.

<sup>5</sup> *Id.* at 1.

<sup>6</sup> *Id.* at 25-27.

<sup>7</sup> *Id.* at 31.

<sup>8</sup> *Id.* at 31-34 & n.110.

<sup>9</sup> *Id.* at 40-41.

Report fails to state a *prima facie* case of market manipulation. BP argues, among other things, that the Staff Report: (i) takes out of context a taped conversation by BP's traders; (ii) is based on circumstantial evidence and misconstrued, unreliable, or flawed data; (iii) misapplies the Commission's Penalty Guidelines; (iv) incorrectly asserts the Commission's jurisdiction over this matter; and (v) fails to state a claim under section 1c.1 of the Commission's regulations (Anti-Manipulation Rule).<sup>10</sup>

6. On December 4, 2013, OE Staff filed a reply to BP's Answer (OE Staff Reply). OE Staff urges the Commission to find that: (i) BP failed to rebut the Staff Report's allegations of market manipulation; (ii) BP's behavior described in the Staff Report constitutes prohibited market manipulation; (iii) BP's behavior falls within the Commission's jurisdiction pursuant to section 4A of the NGA; and (iv) the Staff Report properly applied the Commission's Penalty Guidelines and reasonably calculated pecuniary losses and disgorgement. OE Staff also asks the Commission to reject BP's argument that BP had insufficient notice that its alleged conduct potentially violated federal law. OE Staff requests the Commission therefore find that BP violated the Commission's Anti-Manipulation Rule and order BP to pay the proposed penalty and disgorgement. In the alternative, OE Staff requests the Commission set for hearing the factual question of whether BP violated the Anti-Manipulation Rule with requisite intent and that the Commission reserve for itself the determination of any penalty amount and methodology for disgorgement of any unjust profits.

7. On December 18, 2013, BP moved for leave to file a response to the OE Staff Reply (BP Response). BP contends OE Staff bases its allegations on implausible and incorrect factual assumptions and theories that are entitled to no deference. Among other things, BP offers an affidavit from one of its employees, who avers that BP was charged for natural gas transportation between the Katy Enstor and Katy Oasis storage facilities, and therefore that trades between those places should be separated. BP reiterates that: (i) the Commission lacks jurisdiction over the natural gas transactions at issue in this proceeding; (ii) OE Staff failed to allege conduct within the scope of the Anti-Manipulation Rule; (iii) BP did not receive proper notice of what constitutes market manipulation; and (iv) OE Staff misapplied the Penalty Guidelines with respect to BP's settlements in other contexts and the market harm caused by the alleged scheme.

8. On January 3, 2014, OE Staff filed an answer to BP's Response along with a request to reject BP's Answer for lack of good cause (OE Staff Sur-Reply). Should the Commission accept BP's Response, OE Staff asserts that: (i) it made reasonable inferences about BP's conduct based on the factual record; (ii) BP's wholesale sales of natural gas, not from its own production but by an interstate pipeline affiliate, fall under the Commission's jurisdiction; (iii) BP's traders did not need a perfect hedge between its

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<sup>10</sup> 18 C.F.R. § 1c.1 (2013).

physical and financial natural gas positions in order to have a motive to manipulate the Houston Ship Channel *Gas Daily* Index; and (iv) the inclusion of transportation costs does not change OE Staff's conclusion regarding BP's traders' motivations.

9. On August 16, 2013, Public Citizen, Inc. (Public Citizen) filed comments in this proceeding, directing the Commission's attention to BP's settlements associated with other enforcement proceedings brought by the Commission and the Department of Justice relating to BP's participation in natural gas and propane markets. Public Citizen asks the Commission to: (i) request copies of reports from the independent compliance monitor hired by BP as a consequence of one of those settlements; (ii) disclose such reports publicly; and (iii) consider suspending or revoking BP's blanket natural gas marketing certificates in light of BP's conduct.<sup>11</sup>

10. On August 27, 2013, BP filed an answer to Public Citizen's comments, asking the Commission to strike Public Citizen's comments because Public Citizen lacks party status in this proceeding. BP also argues that Public Citizen's requests are based on settlements with no precedential value to this proceeding.<sup>12</sup>

## **II. Procedural Issues**

11. Rule 213(a)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(1) (2013), required BP to file an answer to the Show Cause Order, and in the Show Cause Order the Commission not only asked for an answer by BP but also allowed a reply by OE Staff. In addition, however, BP filed a further response and OE Staff filed a further reply. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2013), prohibits an answer to an answer unless otherwise ordered by the decisional authority. We are not persuaded to accept these latter two pleadings, BP's Response and OE Staff's Sur-Reply, and will, therefore, reject them.

12. Rule 211(a)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.211(a)(1) (2013), permits any person to file a protest to an order to show cause. Although Public Citizen labels its filing "Comments," Public Citizen has proposed a penalty on BP that is different from the penalty suggested by OE Staff by suggesting that the Commission should withdraw BP's natural gas marketing blanket certificate authority. We regard these comments as a protest to the Show Cause Order. However, Public Citizen's filing of a protest does not make it a party to this proceeding under

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<sup>11</sup> See Public Citizen Comments at 2-3.

<sup>12</sup> See BP Answer to Public Citizen at 2-6.

Rule 214 of the Commission's Rules of Practice and Procedure.<sup>13</sup> While we thus will place this protest in the public file associated with this proceeding,<sup>14</sup> Public Citizen's protest will not be considered part of the record of the hearing we establish in this order.<sup>15</sup>

### **III. BP's Motion to Dismiss**

13. BP argues that the Staff Report fails to meet the Commission's standard for complaints alleging market manipulation and should be dismissed.<sup>16</sup> In particular, BP asserts that the Show Cause Order should be dismissed because: (i) the Commission has no jurisdiction over the claims asserted; and (ii) the Staff Report fails to state a claim of market manipulation under section 1c.1 of the Commission's regulations, with the requisite notice and supporting evidence of proscribed conduct and scienter. We deny BP's motion to dismiss.

14. As discussed below, market participants are on notice of the broad reach of the Commission's anti-manipulation authority, and OE Staff has presented sufficient evidence—including trading and transport data, a taped conversation, and deposition testimony—to substantiate its allegations of market manipulation within the jurisdiction of the Commission. While BP also presented evidence and arguments in its defense, including a written expert report, these materials do not, as a threshold matter of law, rebut the alleged violation. Rather, based upon our review of the Staff Report and the filings in response to the Show Cause Order, we find that there are genuine issues of material fact in dispute that warrant a hearing before an administrative law judge (ALJ).

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<sup>13</sup> See 18 C.F.R. § 385.214 (2013)(a)(4) (2013) (“No person . . . may intervene as a matter of right in a proceeding arising from an investigation pursuant to Part 1b of this chapter.”); see also *id.* § 385.211(a)(2) (“The filing of a protest does not make the protestant a party to the proceeding.”).

<sup>14</sup> *Id.* § 385.211(a)(3).

<sup>15</sup> *Id.* § 385.211(a)(4).

<sup>16</sup> BP Answer at 100 (citing *Nat'l Energy & Trade, LP v. Texas Gas Transmission, LLC*, 121 FERC ¶ 61,064 (2007) (“[w]hen a case is unsupported by facts and circumstances satisfying the elements of a bona fide manipulation claim . . . we will . . . dismiss the complaint” and “[u]nsubstantiated allegations without more do not provide the basis, either in law or in fact, for ordering a hearing”)).

## A. Jurisdiction

### 1. Sufficiency of Notice of Allegations

15. BP contends that this proceeding should be dismissed because the Show Cause Order and the Staff Report do not meet the Commission's pleading standards with respect to jurisdiction.<sup>17</sup> BP reads our rules as subjecting the Show Cause Order and the Staff Report to the same requirements as Rules 203 and 206 of the Commission's Rules of Practice and Procedure,<sup>18</sup> which require pleadings to contain "[t]he relevant facts," "the basis in fact and law,"<sup>19</sup> and to "state a legally recognizable claim that the Commission has the statutory or regulatory power to address."<sup>20</sup> BP further argues that OE Staff's allegations do not meet this standard with respect to jurisdiction because the Staff Report contains only a "bald assertion" and "does not contain a *single* factual allegation to support [its] conclusory assertion of jurisdiction."<sup>21</sup>

16. In reply, OE Staff states that orders to show cause are governed by Rule 209 of the Commission's Rules of Practice and Procedure,<sup>22</sup> which states that "an order to show cause will contain a statement of the matters about which the Commission is inquiring, and a statement of the authority under which the Commission is acting. The statement is tentative and sets forth issues to be considered by the Commission."<sup>23</sup> OE Staff argues that the Show Cause Order satisfied Rule 209 "by alerting BP to both the conduct underlying the alleged manipulation and the NGA § 4A authority under which it acts."<sup>24</sup> OE Staff states that the Staff Report alleged that BP had used its transportation capacity

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<sup>17</sup> BP Answer at 101.

<sup>18</sup> 18 C.F.R. §§ 385.203, 385.206 (2013).

<sup>19</sup> BP Answer at 101 (citing 18 C.F.R. § 385.203(a) (2013)).

<sup>20</sup> *Id.* (emphasis omitted) (quoting *Californians for Renewable Energy, Inc. v. Calif. Pub. Utils. Comm'n*, 129 FERC ¶ 61,075, at P 11 (2009), *reh'g denied*, 131 FERC ¶ 61,102 (2010)).

<sup>21</sup> *Id.* at 102.

<sup>22</sup> 18 C.F.R. § 385.209 (2013).

<sup>23</sup> OE Staff Reply at 54 (quoting 18 C.F.R. § 385.209(b) (2013)).

<sup>24</sup> *Id.*

to sell physical gas with intent to suppress prices at Houston Ship Channel, and that the alleged manipulation affected jurisdictional transactions.<sup>25</sup>

17. We agree with OE Staff that, pursuant to our rules, Rule 209 provides the relevant standards of pleading for orders to show cause. Moreover, we find that the allegations made in the Staff Report and in the Show Cause Order met those standards. In summary, Rule 209(b) requires a statement of the matters into which the Commission will be inquiring, and a statement of the Commission's legal authority to act.<sup>26</sup> In the Staff Report, OE Staff alleges that "BP's trading of jurisdictional and first sale gas at [Houston Ship Channel] and Katy was in connection with jurisdictional transactions, because BP's sales artificially altered the [Houston Ship Channel] *Gas Daily* index, which affected the jurisdictional purchases or sales of other market participants."<sup>27</sup> Similarly, the Show Cause Order cited the legal authority upon which we have ordered BP to show cause as to the matters alleged in the Staff Report.<sup>28</sup> In its Reply, OE Staff included additional factual allegations indicating that the conduct affected jurisdictional transactions at Houston Ship Channel.<sup>29</sup> OE Staff's pleadings satisfy the Rule 209 standards for identifying the matters into which we will be inquiring in this proceeding and a statement of our jurisdiction to act.

## **2. Jurisdiction over Alleged Conduct**

18. BP also contends that the Commission does not have jurisdiction over the alleged conduct, and that the conduct is not "in connection with" jurisdictional activity.<sup>30</sup> BP notes that the Commission's NGA jurisdiction is limited by the provisions of NGA section 1(b)<sup>31</sup> to the transport or sale for resale of natural gas in interstate commerce.<sup>32</sup>

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<sup>25</sup> *Id.* at 55.

<sup>26</sup> 18 C.F.R. § 385.209(b) (2013).

<sup>27</sup> Staff Report at 71 & n.207.

<sup>28</sup> Show Cause Order, 144 FERC ¶ 61,100 at PP 1-3.

<sup>29</sup> OE Staff Reply at 53-56.

<sup>30</sup> BP Answer at 103, 111-12.

<sup>31</sup> 15 U.S.C. § 717(b) (2012).

<sup>32</sup> BP Answer at 104 (citing *Panhandle E. Pipe Line Co. v. Pub. Serv. Comm'n of Ind.*, 332 U.S. 507, 516 (1947)).

BP posits that the Commission lacks jurisdiction because OE Staff's allegations appear to principally concern BP's transportation of natural gas on an intrastate pipeline for, among other things, end-use customers, and not a sale for resale or transportation in interstate commerce.<sup>33</sup> BP contends that OE Staff's position "that the Commission can reach activities that are outside its NGA jurisdiction, as long as those activities 'affected the jurisdictional purchases or sales of other market participants'"<sup>34</sup> is foreclosed by the D.C. Circuit's decision in *Hunter v. FERC*.<sup>35</sup> BP further argues that the "in connection with" language of section 4A of the NGA does not establish jurisdiction here.<sup>36</sup> BP states that section 4A "must be read in conjunction with the overall limiting language of section 1(b)" and that courts applying other provisions of the NGA containing the same language have not interpreted it in a manner that would provide jurisdiction to the Commission for intrastate first sales of natural gas that are not the actual sales for resale in interstate commerce.<sup>37</sup>

19. OE Staff argues that the Commission has jurisdiction over the allegedly manipulative conduct at issue here because some of BP's transactions were encompassed by section 1(b) of the NGA, and in any event all of BP's conduct was "in connection with" jurisdictional transactions.<sup>38</sup> According to OE Staff, section 4A "did not expand the Commission's traditional NGA and FPA [Federal Power Act] subject matter jurisdictions," but, pursuant to the Energy Policy Act of 2005 (EPA 2005),<sup>39</sup> "gave the Commission broad jurisdiction over the entities that engage in certain conduct affecting our subject matter jurisdiction."<sup>40</sup> OE Staff notes that, in Order No. 670, the Commission

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<sup>33</sup> *Id.* at 103-09.

<sup>34</sup> Staff Report at 71 n.207.

<sup>35</sup> BP Answer at 109-10 (citing *Hunter v. FERC*, 711 F.3d 155 (D.C. Cir. 2013) (*Hunter*), *rev'g* *Brian Hunter*, 137 FERC ¶ 61,146, *aff'g* 135 FERC ¶ 61,054 (2011)(*Brian Hunter*)).

<sup>36</sup> *Id.* at 111-12.

<sup>37</sup> *Id.* at 111 (citing *Conoco Inc. v. FERC*, 90 F.3d 536 (D.C. Cir. 1996)).

<sup>38</sup> OE Staff Reply at 57-59.

<sup>39</sup> Energy Policy Act of 2005, Pub. L. 109-58, 119 Stat. 594 (2005).

<sup>40</sup> OE Staff Reply at 59 (emphasis omitted) (quoting *Prohibition of Energy Market Manipulation*, Order No. 670, FERC Stats. & Regs. ¶ 31,202, at P 20, *reh'g denied*, 114 FERC ¶ 61,300 (2006)).

interpreted section 4A’s “in connection with” language ““as encompassing situations in which there is a nexus between the fraudulent conduct of an entity and a jurisdictional transaction”” in that ““the entity must have intended to affect, or have acted recklessly to affect, a jurisdictional transaction.””<sup>41</sup> OE Staff states that the allegations against BP are consistent with this principle because the alleged scheme directly affected jurisdictional transactions (namely, “FERC-jurisdictional natural gas sales transactions priced off the [Houston Ship Channel] index or transacted at [Houston Ship Channel]”), and so the Commission has jurisdiction to review the alleged scheme.<sup>42</sup> Finally, OE Staff avers that BP is mistaken in suggesting that the “in connection with” text of section 4A must follow judicial interpretations of the same text as used in different sections of the NGA.<sup>43</sup> OE Staff argues instead that the text of section 4A can be—and has been—interpreted in light of section 10(b) of the Securities Exchange Act, and cannot be cabined by pre-EPA 2005 decisions interpreting different sections of the NGA.<sup>44</sup>

20. We interpret BP’s arguments as posing both facial and factual challenges to our exercise of jurisdiction.<sup>45</sup> That is, BP asserts, on the one hand, that the Commission may not exercise jurisdiction here as a matter of law and, on the other, that OE Staff has presented insufficient facts to establish any such jurisdiction. As addressed below, we find that the Commission may exercise subject matter jurisdiction as a threshold legal matter in this proceeding. But we also hold that further fact-finding will be necessary to determine whether the alleged conduct at issue was, in fact, jurisdictional and/or “in connection with” jurisdictional transactions.

**a. Facial Challenge to Jurisdiction**

21. The first question is whether we may exercise jurisdiction over the conduct alleged in the Staff Report. When presented with a facial challenge to jurisdiction, we accept as

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<sup>41</sup> *Id.* at 60 (emphasis omitted) (quoting Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 22).

<sup>42</sup> *Id.* at 55.

<sup>43</sup> *Id.* at 57-58.

<sup>44</sup> *Id.* at 61-64.

<sup>45</sup> *See Smith v. United States*, 518 F. Supp. 2d 139, 145 (D.D.C. 2007) (describing facial and factual challenges to jurisdiction).

true the material allegations presented in the complaint.<sup>46</sup> Our exercise of jurisdiction under the NGA is dictated, in the first instance, by section 1(b) of that Act, subject to certain additional restrictions imposed by the Natural Gas Policy Act of 1978 (NGPA).<sup>47</sup> OE Staff alleges that BP's sales were encompassed by section 1(b) of the NGA, and that the manipulative scheme was "in connection with" jurisdictional transactions. BP disagrees, and argues that no jurisdictional transactions were affected by the alleged scheme. This dispute presents a genuine issue of material fact, and so will be addressed at the hearing. Therefore, our analysis here will focus instead on the threshold legal question of whether, pursuant to section 4A of the NGA and the Anti-Manipulation Rule, the Commission may assert jurisdiction over conduct that directly affects jurisdictional transactions. This also requires us to determine whether our "in connection with"

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<sup>46</sup> Rule 217 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.217(b) (2013), addresses summary disposition but not motions to dismiss for lack of subject matter jurisdiction. In such circumstances, we may—but are not required to—look to the Federal Rules of Civil Procedure for guidance. *See, e.g., Calif. ex rel. Brown v. Powerex Corp.*, 135 FERC ¶ 61,178, at P 116 & n.169 (2011) (noting that "the Commission is not strictly bound" by the Federal Rules) (citing *Corpus Christi Mgmt. Co.*, 28 FERC ¶ 62,284, at 63,506 (1984) (approving application of the Federal Rules when the circumstances are "sufficiently analogous . . . to serve as a guideline.")). We find BP's argument respecting jurisdiction to be sufficiently analogous to issues frequently confronted by federal courts under the Federal Rules of Civil Procedure, and so we will look to judicial opinions "to serve as a guideline." Under analogous circumstances, the courts distinguish between facial and factual challenges to jurisdiction, and we think that is an appropriate distinction to apply here. *See Price v. Socialist People's Libyan Arab Jamahiriya*, 294 F.3d 82, 93 (D.C. Cir. 2002) ("where the defendant contests only the legal sufficiency of plaintiff's jurisdictional claims, . . . dismissal is warranted if no plausible inferences can be drawn from the facts alleged that, if proven, would provide grounds for relief."); *see also Apex Digital, Inc. v. Sears, Roebuck & Co.*, 572 F.3d 440, 443 (7th Cir. 2009) ("Facial challenges [to jurisdiction] require only that the court look to the complaint and see if the plaintiff has sufficiently alleged a basis of subject matter jurisdiction."); *Martha's Vineyard/Dukes County Fishermen's Ass'n v. Locke*, 811 F. Supp. 2d 308, 313 (D.D.C. 2011) ("Where a motion to dismiss . . . makes a facial attack on the complaint, the reviewing court 'must accept as true all material allegations on the complaint, and must construe the complaint in favor of the complaining party.'").

<sup>47</sup> *See* Order No. 670, FERC Stats. & Regs. ¶ 31,202 at PP 16, 20 n.34.

jurisdiction is foreclosed by prior precedent interpreting the same language in other sections of the NGA, or by the D.C. Circuit's recent decision in *Hunter*.<sup>48</sup>

22. BP contends that “the ‘in connection with’ language of section 4A of the NGA must be read in conjunction with the overall limiting language of section 1(b)” and that “courts have held that such language does not trump section 1(b).”<sup>49</sup> By this, BP appears to assert that the Commission may not exercise section 4A jurisdiction over any transaction that is not expressly covered by section 1(b), irrespective of any nexus between a non-jurisdictional manipulation and a jurisdictional transaction.<sup>50</sup>

23. That is incorrect as a matter of law. This is not a novel question, and our response today remains the same as the position that the Commission has consistently taken in this regard. Section 4A of the NGA encompasses “any entity” that “directly or indirectly . . . use[s] or employ[s], *in connection with the purchase or sale of natural gas . . . subject to the jurisdiction of the Commission*, any manipulative or deceptive device or contrivance.”<sup>51</sup> Interpreting this provision in 2006, the Commission promulgated the Anti-Manipulation Rule<sup>52</sup> which was “patterned after the Securities and Exchange

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<sup>48</sup> *Hunter*, 711 F.3d at 155.

<sup>49</sup> BP Answer at 111.

<sup>50</sup> BP's passing assertion that there is no federal jurisdiction over first sales is incorrect. *See* BP Answer at 110 n.16. While it is uncontroverted that first sales were removed from the Commission's *NGA jurisdiction* by the NGPA and the subsequent Natural Gas Wellhead Decontrol Act of 1989, Pub. L. No. 101-60, 103 Stat. 157 (1989), nevertheless it is erroneous to suggest that Congress abandoned *all* federal jurisdiction over first sales. Indeed, the statute itself indicates that the Commission continues to exercise limited jurisdiction over first sales, albeit in a significantly different manner than under the NGA as originally adopted. *See* 15 U.S.C. § 3431(c)(2) (2012) (authorizing Commission to deny guaranteed pass-through of costs to interstate pipelines when it “determines that the amount paid was excessive due to fraud, abuse, or similar grounds”); 18 C.F.R. § 2.300 (2013) (effectuating same). In any event, sales by an interstate or intrastate pipeline, or affiliate thereof, do not qualify as first sales except to the extent that the volumes sold are attributable to the company's own production. *See, e.g., Distrigas of Mass., LLC*, 124 FERC ¶ 61,039, at P 16 n.24 (2008).

<sup>51</sup> 15 U.S.C. § 717c-1 (2012) (emphasis added).

<sup>52</sup> Order No. 670, FERC Stats. & Regs. ¶ 31,202 (codified at 18 C.F.R. §§ 1c.1, 1c.2).

Commission's (SEC) Rule 10b-5,<sup>53</sup> and [was] 'intended to be interpreted consistent with analogous SEC precedent that is appropriate under the circumstances.'"<sup>54</sup> In Order No. 670, the Commission interpreted the "in connection with" provision of section 4A of the NGA (and the corresponding text in section 222 of the FPA) "as encompassing situations in which there is a nexus between the fraudulent conduct of an entity and a jurisdictional transaction."<sup>55</sup> As explained there, EAct 2005 established authority to investigate and penalize "any entity [who] engages in manipulation and the conduct is found to be 'in connection with' a jurisdictional transaction."<sup>56</sup> To assist market participants in understanding the scope of our manipulation authority under EAct 2005, the Commission offered the following example in Order No. 670:

any entity engaging in a non-jurisdictional transaction through a Commission-regulated RTO/ISO market, that acts with intent or with recklessness to affect the single price auction clearing price (which sets the price of both non-jurisdictional and jurisdictional transactions), would be engaging in fraudulent conduct in connection with a jurisdictional transaction and, therefore, would be in violation of the Final Rule.<sup>57</sup>

The Commission addressed a similar issue in *Barclays Bank PLC*. In the order assessing civil penalties in that proceeding, the Commission explained that the anti-manipulation provisions of the FPA and related regulations "reach . . . conduct that is 'in connection with' a jurisdictional transaction, which is understood to mean that 'the entity must have intended to affect, or have acted recklessly to affect, a jurisdictional transaction.'"<sup>58</sup> As

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<sup>53</sup> 17 C.F.R. § 240.10b-5 (2005).

<sup>54</sup> Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 2; *see id.* P 22 (citing section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b)).

<sup>55</sup> *Id.* P 22.

<sup>56</sup> *Id.* P 16.

<sup>57</sup> *Id.* P 22.

<sup>58</sup> *Barclays Bank PLC*, 144 FERC ¶ 61,041, at P 113 (2013) (*Barclays*).

identical provisions of the NGA and FPA are interpreted identically,<sup>59</sup> these examples apply equally to the NGA. These examples also describe OE Staff's allegations. OE Staff has alleged that the *Gas Daily* index at Houston Ship Channel was (and is) a volume-weighted average ("which sets the price of both non-jurisdictional and jurisdictional transactions"), that BP "engag[ed] in a non-jurisdictional transaction" and acted with requisite intent "to affect" the daily price at Houston Ship Channel, and that BP's conduct therefore was "in connection with a jurisdictional transaction" in "violation of the Final Rule."<sup>60</sup> In short, setting aside the irrelevant fact that there are no markets in natural gas akin to RTOs or ISOs, the example of conduct "in connection with" a jurisdictional transaction provided in Order No. 670 is consistent with BP's alleged conduct in this proceeding.

24. In sum, BP's position cannot be squared with Commission precedent. BP has offered no persuasive reason for us to abandon the settled interpretation of EPCRA 2005, and we will not do so today. Therefore, we find that the allegations, on their face, describe conduct that potentially violated section 4A of the NGA and the Anti-Manipulation Rule.

25. Furthermore, even if BP's proposition was not foreclosed by our prior orders, we would reject it nevertheless because OE Staff's allegations are consistent with the interpretation of the "in connection with" language found elsewhere in the NGA. To be sure, *Conoco Inc. v. FERC* held that the Commission's jurisdiction does not reach activities that it "expressly found are not within its § 1(b) jurisdiction," but in so doing it did not render meaningless the "in connection with" language of sections 4 and 5 of the NGA. Far from it: the court acknowledged that the Commission might exercise what it called "stand-by jurisdiction" over non-jurisdictional activity that was "intertwined with jurisdictional activities," and "that a non-jurisdictional entity could act in a manner that would change its status by enabling" activity that directly affects jurisdictional matters.<sup>61</sup> This is consistent with the approach that the D.C. Circuit took in an opinion issued shortly after *Conoco*, in which it noted that "the Commission ordinarily has the authority to consider a matter beyond its jurisdiction *if the matter affects jurisdictional sales*—at

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<sup>59</sup> The Supreme Court has explained that "the relevant provisions of [the FPA and the NGA] 'are in all material respects substantially identical'" and therefore it is the Court's "established practice of citing interchangeably decisions interpreting the pertinent sections of the two statutes." *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

<sup>60</sup> See Staff Report at 30 n.105, 71 & n.207; OE Staff Reply at 55-56.

<sup>61</sup> *Conoco Inc. v. FERC*, 90 F.3d 536, 549, 552 (D.C. Cir. 1996).

least if there would otherwise be a regulatory gap.”<sup>62</sup> In the years since *Conoco*, the Commission has continued to follow this approach by exercising its “in connection with” authority when non-jurisdictional conduct is intertwined with, or directly affects, jurisdictional activity or sales.<sup>63</sup> As the Commission recently explained, while “the ‘in connection with’ language of sections 4 and 5 does not constitute a grant of authority to the Commission to regulate gathering [a non-jurisdictional activity] *independent of its effect on jurisdictional transportation*,”<sup>64</sup> nevertheless “Commission jurisdiction may be found where necessary to avoid a regulatory gap”<sup>65</sup> or where the non-jurisdictional conduct affects jurisdictional matters in such a way that it “would frustrate the NGA’s statutory purpose.”<sup>66</sup> Thus, the Commission

may assert NGA sections 4 and 5 “in connection with” jurisdiction over the activities of an affiliated gatherer, when (1) the gatherer has used its market power over gathering to benefit the pipeline in its performance of jurisdictional transportation or sales service and (2) that benefit is contrary to the Commission’s policies concerning jurisdictional services adopted pursuant to the NGA.<sup>67</sup>

In other words, “[w]hile the Commission does not have jurisdiction over gathering because of the exemption of [gathering found in] Section 1(b) of the NGA, it does have jurisdiction over rates charged by interstate pipelines for gathering service under

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<sup>62</sup> *Altamont Gas Transmission Co. v. FERC*, 92 F.3d 1239, 1248 (D.C. Cir. 1996) (emphasis added).

<sup>63</sup> See, e.g., *Williston Basin Interstate Pipeline Co.*, 119 FERC ¶ 61,243, at P 7 n.4 (2007) (*Williston Basin*); *Criteria for Reassertion of Jurisdiction over the Gathering Services of Natural Gas Co. Affiliates*, 118 FERC ¶ 61,114 (2007); *Equitrans, L.P.*, 109 FERC ¶ 61,209, at P 3 n.1 (2004) (*Equitrans*).

<sup>64</sup> *Criteria for Reassertion of Jurisdiction over the Gathering Services of Natural Gas Co. Affiliates*, 118 FERC ¶ 61,114 at P 42 (emphasis added).

<sup>65</sup> *Id.* P 44.

<sup>66</sup> *Id.* P 51.

<sup>67</sup> *Id.*

Section 4(a) of the NGA because gathering rates are ‘in connection with’ jurisdictional transportation.’<sup>68</sup>

26. The allegations here are that even if BP’s conduct was not jurisdictional, nevertheless it was intertwined with, and affected, jurisdictional sales. Under the alleged facts, we would rightfully assert jurisdiction under section 4A over BP’s alleged conduct even if the “in connection with” language of section 4A had been given the same meaning as used in sections 4 and 5 of the NGA. OE Staff has alleged that BP’s use of non-jurisdictional transactions and transportation to manipulate the Houston Ship Channel *Gas Daily* index affected jurisdictional transactions whose settlement price was based on that index. That establishes the necessary connection between the alleged conduct and matters directly within our jurisdiction under section 4A, and so we would rightfully invoke our “stand-by” authority to regulate (and, if necessary, to penalize) manipulative conduct that was “in connection with” jurisdictional sales. To find otherwise would not only frustrate the purpose of the NGA by allowing entities to manipulate the price of interstate natural gas, but it would leave the alleged conduct in a “regulatory gap” because the states may not regulate NGA-jurisdictional natural gas rates.

27. Finally, *Hunter* is inapposite. *Hunter* presented a dispute between two federal agencies concerning the extent of their respective jurisdictional statutes, and the court determined that Hunter’s manipulative scheme was subject to the Commodity Futures Trading Commission’s (CFTC) exclusive jurisdiction because the scheme was carried out in the futures market (where the CFTC’s jurisdiction is exclusive).<sup>69</sup> Here, BP asserts that OE Staff’s allegations relate only to BP’s transport and sale of intrastate gas, which is not subject to the jurisdiction of the NGA. BP then claims that *Hunter* prohibits the Commission from asserting jurisdiction over such intrastate gas even if BP had employed such actions “in connection” with jurisdictional transactions in a manipulative scheme. BP thus likens the CFTC’s exclusive jurisdiction to Congress’ reservation of certain natural gas matters to the states, and suggests that the *Hunter* analysis applies here because “Congress drafted Section 1(b) of the NGA to exclude from federal jurisdiction

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<sup>68</sup> *Williston Basin*, 119 FERC ¶ 61,243 at P 7 n.4; *Equitrans, L.P.*, 109 FERC ¶ 61,209 at P 3 n.1. *Cf. S. Nat. Gas Co., LLC High Point Gas Transmission, LLC*, 143 FERC ¶ 61,207, at PP 72-73 (2013) (election not to assess a rate for gathering services eliminated requirement “to submit a rate for gathering services provided in connection with its jurisdictional transmission services.”).

<sup>69</sup> *See Hunter*, 711 F.3d at 158-60 (citing *Salleh v. Christopher*, 85 F.3d 689, 691-92 (D.C.Cir.1996)).

intrastate sales, transactions on intrastate pipelines, direct consumer sales, and first sales.”<sup>70</sup> BP is mistaken.

28. As an initial matter, because the case involved “two competing governmental entities assert[ing] conflicting jurisdictional claims” the *Hunter* court did not apply *Chevron* deference to either agency’s construction of the statute.<sup>71</sup> In the absence of *Chevron* deference, the court was able to make its own *de novo* determination concerning the competing statutory provisions. Here, of course, that concern is not present, and so were this issue to arise before a court, *Chevron* deference would apply to Order No. 670’s interpretation (addressed above) of the “in connection with” statutory language of section 4A.<sup>72</sup> As addressed above, OE Staff’s allegations fall squarely within the ambit of Order No. 670.

29. Moreover, BP is incorrect that the Commission’s jurisdiction here is precluded by a grant of exclusive jurisdiction as in *Hunter*.<sup>73</sup> The NGA reserves limited jurisdiction to the states, but does not provide them with *exclusive* jurisdiction, in contrast to the CFTC’s statutory exclusive jurisdiction over future markets at issue in *Hunter*. Accordingly, a state’s jurisdiction does not prevent the Commission from exercising its authority to prohibit natural gas market manipulation even when a state is regulating transactions within its purview. Indeed, when both jurisdictional and non-jurisdictional regulatory programs are at issue, it is federal jurisdiction that prevails: the Supreme Court has repeatedly held that states may not directly regulate the price of Commission-jurisdictional transactions or “indirectly achieve the same result.”<sup>74</sup>

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<sup>70</sup> BP Answer at 110 n.16.

<sup>71</sup> *Hunter*, 711 F.3d at 157 (citing *Salleh v. Christopher*, 85 F.3d 689, 691-92 (D.C. Cir. 1996)).

<sup>72</sup> See *supra* P 23 (discussing the Commission’s interpretation of section 4A’s “in connection with” in Order No. 670).

<sup>73</sup> See BP Answer at 110.

<sup>74</sup> *N. Natural Gas Co. v. State Corp. Comm’n of Kan.*, 372 U.S. 84, 91 (1963) (citations omitted). In that case, the court ruled that the NGA prohibits states from enacting laws that would have the effect of directly regulating the prices of NGA-jurisdictional gas. *Id.* at 91-92. Similarly, states may not “bar regulated utilities from recovering FERC-mandated wholesale costs.” *Ky. W. Va. Gas Co. v. Pa. Pub. Util. Comm’n*, 862 F.2d 69, 73-74 (3d Cir. 1988). Nor may states enact rules respecting the issuance of securities that would have the direct effect of regulating jurisdictional entities. *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 300-11 (1988).

30. BP's proposal, on the other hand, risks creating a regulatory gap<sup>75</sup> in which entities potentially could escape liability for manipulating the price of jurisdictional transactions simply by restricting their manipulative conduct to non-jurisdictional activities. But our duty to protect jurisdictional markets from manipulation may not be stymied by this simple expedient. Congress directed the Commission to prevent market manipulation and provided the Commission with authority to reach otherwise non-jurisdictional conduct that is "in connection with" jurisdictional matters. Accordingly, our "in connection with" authority encompasses matters directly or indirectly affecting jurisdictional transactions.

31. Lastly, BP misconstrues *Hunter* when it asserts that the D.C. Circuit concluded that Hunter's trading was not "in connection with" Commission-jurisdictional transactions.<sup>76</sup> The court did not circumscribe the reach of FERC's Anti-Manipulation Rule to otherwise non-jurisdictional transactions. Indeed, in construing the Commission's "in connection with" authority, the court ruled "FERC is free to prohibit manipulative trading in markets outside the CFTC's exclusive jurisdiction."<sup>77</sup>

**b. Factual Challenge to Jurisdiction**

32. BP disputes whether OE Staff has alleged facts that support jurisdiction. OE Staff alleges two bases for jurisdiction—that some of BP's allegedly manipulative sales were jurisdictional, and that all of the allegedly manipulative sales were "in connection with" jurisdictional transactions.<sup>78</sup> BP and OE Staff disagree about the factual allegations necessary to establish the jurisdictional status of BP's sales as well as the alleged nexus between the alleged misconduct and jurisdictional transactions. These issues must be addressed at the hearing ordered below. Specifically, we direct the ALJ to consider the disputed facts and determine whether BP has engaged in misconduct "in connection with" jurisdictional transactions.

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<sup>75</sup> The Supreme Court has long held that, in enacting the NGA, Congress intended that "there would be no 'gaps' for private interests to subvert the public welfare." *Fed. Power Comm'n v. La. Power & Light Co.*, 406 U.S. 621, 631 (1972).

<sup>76</sup> BP Answer at 110.

<sup>77</sup> *Hunter*, 711 F.3d at 160.

<sup>78</sup> See Staff Report at 71 & n.207.

## B. Notice and Conduct within the Scope of the Anti-Manipulation Rule

### 1. BP's Position

33. BP states that “[b]asic principles of due process require any administrative agency to provide ‘notice of the actions they consider unlawful.’”<sup>79</sup> BP contends that the Staff Report failed to “provide a coherent explanation of the specific conduct it would have the Commission proscribe and punish as market manipulation.”<sup>80</sup> BP asserts that “[w]hen the Commission adopted its anti-manipulation rule in Order No. 670, it told market participants [that] ‘[w]e intend to adapt analogous securities precedents as appropriate to specific facts, circumstances, and situations that arise in the energy industry.’”<sup>81</sup> BP contends that: (i) no federal court decision has adopted the theory of “marking the open” or “framing the market,” on which the Staff Report is based;<sup>82</sup> (ii) “open-market activity, without more, cannot constitute market manipulation” under applicable precedent respecting SEC Rule 10b-5;<sup>83</sup> and (iii) open-market trading cannot be manipulative if

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<sup>79</sup> BP Answer at 112 (citing *Kourouma v. FERC*, 723 F.3d 274, 279 (D.C. Cir. 2013) (finding sufficient notice) (citation omitted)).

<sup>80</sup> *Id.* (capitalizations omitted). According to BP, “Enforcement Staff alleges in hindsight that the [BP Southeast Gas Trading Desk] team’s trades just weren’t profitable enough,” and that such a “test” for manipulation “is tantamount to the infamous definition of pornography: ‘[we] know it when [we] see it.’” *Id.* at 113 (citing *Jacobellis v. Ohio*, 378 U.S. 184, 197 (1964) (Stewart, J., concurring)).

<sup>81</sup> BP Answer at 113 (citing Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 30).

<sup>82</sup> *Id.* at 114. BP faults OE Staff for relying on a 2010 Financial Industry Regulatory Authority (FINRA) enforcement decision, which “was based not only on the timing of trades but also on specific evidence showing an intent to move prices,” and the 2011 National Association of Securities Dealers (NASD) Sanction Guidelines, both of which post-date the conduct at issue here. *Id.* (citing 2010 FINRA decision in *Dep’t. of Enforcement v. Brokaw*, 2010 FINRA Discip. LEXIS 34 (June 11, 2010) and 2011 NASD Sanction Guidelines). BP then contends the Administrative Procedure Act would not allow “the Commission [to] adopt a newly fabricated theory never adopted by any federal court decision on the strength of facially distinguishable administrative cases issued two years after the conduct at issue occurred.” *Id.* at 114-15.

<sup>83</sup> *Id.* at 115-16 (citing *ATSI Communications, Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 101 (2d Cir. 2007) (“[S]hort selling – even in high volumes – is not, by itself, manipulative.”); *In re Amaranth Natural Gas Commodities Litig.*, 587 F. Supp. 2d 513,

(continued...)

justified by a legitimate economic strategy.<sup>84</sup> BP concludes that insofar as it “has shown that the trading activity described in the [OE] Staff Report is supported by legitimate economic rationales,” the Show Cause Order should be dismissed.<sup>85</sup>

## 2. OE Staff’s Position

34. OE Staff asserts that “the Commission is not obliged to specify in advance every potential activity that could lead to a future enforcement action.”<sup>86</sup> Rather, OE Staff avers that BP’s “Texas team traders *intentionally* sold physical gas uneconomically to benefit their financial position tied to the [Houston Ship Channel] indices,” which is conduct that falls squarely within the Anti-Manipulation Rule and requires no additional notice.<sup>87</sup> OE Staff also argues that “marking the open” is “conceptually similar” to so-called “marking the close” in securities cases. In particular, OE Staff contends that the question of whether this theory has been adopted by a federal court is irrelevant because BP’s “Texas team sold gas at [Houston Ship Channel] with the intent to suppress the [Houston Ship Channel] *Gas Daily* index in several ways, not just by ‘marking the open,’ . . . [in a] multi-pronged manipulative scheme” that cannot be compartmentalized.<sup>88</sup> OE Staff further asserts that the Commission and federal securities law precedent recognize that open-market transactions, combined with the requisite *scienter*, can support a claim of market manipulation.<sup>89</sup> Finally, OE Staff disputes that evidence of

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534 (S.D.N.Y. 2008), *aff’d*, 730 F.3d 170 (2d Cir. 2013) (“[E]ntering into futures contracts or swaps, without more, cannot constitute commodities manipulation.”)).

<sup>84</sup> *Id.* at 116-17 (citing *SEC v. Masri*, 523 F. Supp. 2d 361, 372 (S.D.N.Y. 2007); *Amaranth*, 587 F. Supp. 2d at 534-35).

<sup>85</sup> *Id.* at 117-18.

<sup>86</sup> OE Staff Reply at 79-80 & nn.143 (citing *Barclays*, 144 FERC ¶ 61,041 at P 43), 145 (citing *Maynard v. Cartwright*, 486 U.S. 356, 361 (1988)).

<sup>87</sup> *Id.* at 80.

<sup>88</sup> *Id.* at 81-82.

<sup>89</sup> *Id.* at 81-83 (citing, *inter alia*, *Barclays*, 144 FERC ¶ 61,041 at PP 50-58); *id.* at 83 & n.151 (citing, *inter alia*, *Amaranth Natural Gas*, 587 F. Supp. 2d at 534 (finding under the Commodity Exchange Act that “entering into futures contracts or swaps, without more, cannot constitute commodities manipulation,” but also stating that “the additional factor need not be a misstatement or omission” and “a legitimate transaction combined with an improper motive is commodities manipulation”)).

“legitimate economic strategy” commingled with a manipulative purpose can defeat a claim for manipulation.<sup>90</sup>

### 3. Commission’s Determination

#### a. Notice

35. We find that the administrative requirement of notice of an alleged violation of the Anti-Manipulation Rule has been met.<sup>91</sup> The Staff Report appended to the Show Cause Order sets forth in detail the conduct that allegedly violated section 4A of the NGA and the Anti-Manipulation Rule. Briefly stated, OE Staff alleges that traders on BP’s Southeast Gas Trading Desk entered into uneconomic physical transport and trading of natural gas—so-called “marking” or “banging the open,” and “framing the market”—between the Katy and Houston Ship Channel hubs as part of a manipulative scheme to suppress the Houston Ship Channel *Gas Daily* index, and that this scheme was motivated by a desire to benefit certain physical and financial positions held by BP whose price was set by the same index.<sup>92</sup>

36. We find that OE Staff alleges a type of conduct that would violate the Anti-Manipulation Rule as a threshold legal matter. In Order No. 670, the Commission prohibited entities from “us[ing] a fraudulent device, scheme or artifice , . . . or engag[ing] in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity.”<sup>93</sup> Order No. 670 emphasizes that it prohibits “the use or employment of *any* device, scheme, or artifice to defraud.”<sup>94</sup> The Commission further explained that “[f]raud is a question of fact that is to be determined by all the circumstances of the case” and that “include[s] any action, transaction, or conspiracy for the purpose of impairing, obstructing or defeating a well-functioning market.”<sup>95</sup> The Commission thus gave notice that engaging in *any* scheme or device for the purpose of affecting (i.e., impairing, obstructing, or defeating) a “well-functioning market” could fall

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<sup>90</sup> *Id.* at 83 & n.152 (citing *Barclays*, 144 FERC ¶ 61,041 at P 70 (“The Anti-Manipulation Rule requires manipulative intent; it does not require *exclusively* manipulative intent.”); *Masri*, 523 F. Supp. 2d at 373-75).

<sup>91</sup> *See generally* 5 U.S.C. § 554(b) (2012).

<sup>92</sup> *See* Show Cause Order, 144 FERC ¶ 61,100 at P 2.

<sup>93</sup> Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 49.

<sup>94</sup> *Id.* P 50 (emphasis added).

<sup>95</sup> *Id.*

within the scope of the Anti-Manipulation Rule. The types of conduct prohibited in Order No. 670 include the physical trading and transport of natural gas with the intent to artificially affect prices and benefit financial positions, as OE Staff alleged here.<sup>96</sup> Nothing in the statute or our regulations requires the Commission to identify in advance every single fact pattern or scheme that could give rise to a claim of manipulation.<sup>97</sup>

37. Nor is the Commission limited to pursuing only claims based on legal theories explicitly “adopted” by the Securities and Exchange Commission, or on fact patterns already found in pre-existing securities precedent to violate Rule 10b-5 or the Securities Exchange Act of 1934 (Exchange Act), as BP suggests.<sup>98</sup> The Commission’s enforcement mandate also extends to novel schemes and manipulative devices that affect prices in, or otherwise interfere with, well-functioning markets,<sup>99</sup> and not just the tried-

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<sup>96</sup> Cf. *ATSI Communications, Inc. v. The Shaar Fund, Ltd.*, 493 F.3d 87, 100 (2d Cir. 2007) (citing *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976) (Manipulation in the securities markets “connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.”)).

<sup>97</sup> Cf. *Kourouma*, 723 F.3d at 279 (rejecting claim of inadequate notice of Commission’s broad reading of Market Behavior Rule 3, 18 C.F.R. § 35.41(b), and deferring to agency’s interpretation of its own regulations).

<sup>98</sup> The Exchange Act’s prohibition of manipulative and deceptive devices is codified at 15 U.S.C. § 78j(b).

<sup>99</sup> See *United States v. Arcadipane*, 41 F.3d 1, 5 (1st Cir. 1994) (“Fair warning, however, does not mean that the first bite is free, nor does the doctrine demand an explicit or personalized warning.”); see also *Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 10 n.7 (1971) (“[We do not] think it sound to dismiss a complaint merely because the alleged scheme does not involve the type of fraud that is ‘usually associated with the sale or purchase of securities.’ We believe that § 10b and Rule 10b-5 prohibit all fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws.”) (quoting *A.T. Brod & Co. v. Perlow*, 375 F.2d 393, 397 (2d Cir.1967)); *Kourouma*, 723 F.3d at 279 (citing *Star Wireless, LLC v. FCC*, 522 F.3d 469, 473 (D.C. Cir. 2008) (holding that adequate notice means “‘a regulated party acting in good faith’” must “be able ‘to identify, with ascertainable certainty, the standards with which the agency expects parties to conform.’”)).

and-true schemes and devices that have already been the subject of securities fraud actions.<sup>100</sup>

**b. Open-Market Transactions**

38. BP's argument that open-market transactions cannot be the basis of a claim of manipulation is without merit. As the Commission has stated, open-market transactions undertaken with manipulative intent can send inaccurate price signals to, or otherwise impair, a well-functioning market, even in the absence of some other deceptive conduct.<sup>101</sup> Here, the Staff Report includes specific allegations of BP's use of Houston Pipeline transport to ship natural gas from Katy to Houston Ship Channel, not for the purpose of increasing supply to meet actual or perceived demand, but to engage in heavy selling of natural gas at the open of the Houston Ship Channel market, including by "hitting bids" in unprofitable transactions with the intent to suppress prices, motivated by

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<sup>100</sup> While stating an intent "on a case-by-case basis, to be guided by analogous securities law precedent that is appropriate under the specific facts, circumstances, and situations in the energy industry," in Order No. 670 the Commission also stated an intent "to recognize, on a case-by-case basis, that the roles of the Commission and the SEC are not identical in determining whether it is appropriate to adopt securities precedents to specific energy industry facts, circumstances, or situations." Order No. 670, FERC Stats. & Regs. ¶ 31,202 at PP 31, 42. The Commission "recognize[d] that the SEC does not have a duty to assure that the price of a security is just and reasonable, and that our duty is not to protect purchasers through a regime of disclosure." *Id.* P 32.

<sup>101</sup> *Barclays*, 144 FERC ¶ 61,041 at PP 50-58 (citing, *inter alia*, *Brian Hunter*, 135 FERC ¶ 61,054 at P 51 n.78 (citing *Amaranth*, 587 F. Supp. 2d at 534 (holding that "[A] legitimate transaction combined with an improper motive is commodities manipulation."))). The Commission's position is readily reconcilable with Rule 10b-5 securities precedent. *See Markowski v. SEC*, 274 F.3d 528, 529 (D.C. Cir. 2001) ("'manipulation' can be illegal solely because of the actor's purpose").

BP cites to the Second Circuit's decision in *ATSI*, for the proposition that "[s]hort selling—even in high volumes—is not, by itself, manipulative." BP Answer at 116 (internal quotations omitted) (citing *ATSI*, 493 F.3d at 101). However, the Second Circuit notably did not reject the concept of open-market manipulation and instead recognized that what may "be actionable as a manipulative act," is short selling "willfully combined with something more to create a false impression of how market participants value a security." *ATSI*, 493 F.3d at 101 (affirming dismissal of complaint on the limited ground that "[n]owhere does *ATSI* particularly allege what the defendants did – beyond simply mentioning common types of manipulative activity – or state how this activity affected the market in *ATSI*'s stock.").

a desire to benefit BP's physical and financial positions that settled based on a related Houston Ship Channel *Gas Daily* index.

39. A material issue of fact for consideration at the hearing is thus whether BP's transport and trading activities were undertaken with manipulative intent and, in particular, whether those activities were motivated by a desire to benefit physical and financial positions that settled off the Houston Ship Channel *Gas Daily* index. The ALJ may consider, but is not limited to considering, in this regard whether those activities sent false signals or affected prices in a way that was not reflective of the genuine interplay of supply and demand.

**c. Plausibility of OE Staff's Theory**

40. BP contends that OE Staff's theory of "marking the open" does not state a cognizable manipulation claim because it has never been adopted in the securities context.<sup>102</sup> BP is incorrect. As a threshold legal matter, it is not dispositive whether OE Staff's theory of "marking the open"—or related theory of "framing the market"—has been adopted in federal securities cases. We reiterate that fraud is fundamentally a question of fact, and so the proper inquiry is whether OE Staff's allegations of manipulative activity, including an alleged pattern of "early and heavy trading" in the Houston Ship Channel physical market and its potential effect on other market participants and impact on a related financial index, state a claim of market manipulation. A fundamental responsibility of the Commission is to ensure that prices are "just and reasonable," and consequently market-based pricing depends on the "accuracy, reliability and transparency" of the index prices used to settle trades.<sup>103</sup> OE Staff has sufficiently alleged, as a threshold matter, that BP's conduct—including its "marking the open"—violated the Anti-Manipulation Rule. BP's attempt to distinguish OE Staff's allegations from "marking the close" in futures contracts misses the mark. The pricing period of natural gas indices is the volume-weighted average price for the specified period. Thus, for a daily index such as Houston Ship Channel *Gas Daily*, the relevant pricing period might be the trading day (or certain hours during the day) when reported prices are

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<sup>102</sup> BP Answer at 114.

<sup>103</sup> *Price Discovery in Natural Gas and Elec. Mkts.*, 109 FERC ¶ 61,184, at P 1 (2004). See generally 18 C.F.R. § 284.288(a) (2013) (requiring accurate and factual reporting of transactions to publishers of natural gas indices and that such information not be knowingly false or misleading); *Price Discovery in Natural Gas and Elec. Mkts.*, 104 FERC ¶ 61,121, at PP 33-34 (2003) (market participants that report transaction data to price index developers must report prices that accurately reflect market activity and index developers must identify "activity that may reflect an attempt to manipulate energy price indices").

averaged by volume.<sup>104</sup> This period of time is analogous to the two-minute closing period in futures markets when qualifying trades are averaged.<sup>105</sup>

41. BP's contention that prices during the day often differ widely from the early trading prices does not necessarily undermine OE Staff's theory of early manipulative trading as a matter of law.<sup>106</sup> OE Staff argues that "marking the open" sets the tone early and could have a large impact on the development of the daily volume-weighted average price.<sup>107</sup> BP and OE Staff also dispute whether BP had sufficient negative exposure to the Houston Ship Channel *Gas Daily* index through its financial positions to benefit from lower (i.e., manipulated) Houston Ship Channel physical prices.<sup>108</sup> All of these disputes raise issues of material fact, not threshold legal issues, and so we will not address them here except to state that OE Staff's theories are not foreclosed as a matter of law.

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<sup>104</sup> See *Platts Gas Daily* (McGraw Hill Financial), available at <http://www.platts.com/products/gasdaily>; Platts, *Methodology and Specifications Guide, Northern American Natural Gas* at 4-5 (McGraw Hill Financial 2014) (describing use of a 11:30 CT "cutoff" for its daily gas survey and use of a volume-weighted average price), available at <http://platts.com/methodology-specifications/natural-gas>; see also 17 C.F.R. § 242.201(d)(7)(i) (2013) (describing short sale at the volume-weighted average price).

<sup>105</sup> For example, the CFTC's online glossary defines "marking the close" as "[a] manipulative or disruptive trading practice whereby a trader buys or sells a large number of futures contracts *during the closing period of a futures contract* (that is, *the period during which the futures settlement price is determined*) in order to benefit an even larger [financial] position . . . that is cash settled based on the futures settlement price that day." CFTC Glossary, <http://www.cftc.gov/consumerprotection/educationcenter/cftcglossary/index.htm> (emphasis added).

<sup>106</sup> For illustrative purposes, the volume-weighted average price might be viewed like a bag for picking an assortment of apples. It starts off empty in the morning, but gradually fills up during the day. An extra-heavy (or extra-light) apple added in the morning could have a large impact on the average weight of the bag at the moment, but less so when the bag is full at the close of the day. In both an upward and downward trending market, the volume-weighted average price lags market prices insofar as it is a weighted average that includes past transaction data.

<sup>107</sup> See OE Staff Reply at 20.

<sup>108</sup> BP Answer at 33-35; OE Staff Reply at 17-20.

**d. Legitimate Economic Purpose**

42. BP also contends that it cannot be liable for manipulation because it has shown that its trading activity is supported by legitimate economic rationales. Such an assertion, however, cannot be dispositive since the manipulative nature of the trading is a question of fact yet to be resolved. Trades undertaken solely for bona fide economic purposes are not violative of section 1c.1 of the Commission's regulations, but the very same trades, if intended to manipulate the market, are indeed prohibited. At the hearing, BP may present evidence as to its business purpose, which will be considered along with OE Staff's evidence of manipulation in determining whether a claim for manipulation has been established.<sup>109</sup>

**C. Scienter**

**1. BP's and OE Staff's Positions**

43. BP argues that OE Staff's allegations respecting scienter were insufficient as a matter of law. In making this argument, BP addresses in turn three ways to satisfy the scienter element as a legal matter: direct evidence, circumstantial evidence and recklessness.<sup>110</sup> BP contends that, by relying on circumstantial evidence, OE Staff implicitly conceded that there was no direct evidence of scienter. As to circumstantial evidence, BP states that OE Staff's proffered circumstantial evidence is not probative of scienter. Without direct evidence or probative circumstantial evidence, BP contends, OE Staff resorts to meeting the scienter element by relying on recklessness. As to recklessness, BP asserts that only "extreme" or "severe" recklessness can meet the scienter element and that the complex scheme alleged by OE Staff could not be achieved through recklessness, extreme, severe, or minimal.

44. In its Reply, OE Staff states that the Staff Report satisfies the scienter requirement as a threshold legal matter because it alleges both intent and recklessness. OE Staff points to the Staff Report as laying out "substantial corroborating evidence of the traders' intent to manipulate," including the November 5, 2008 recorded call, BP's trading and transport records, BP's financial position, another recorded call on November 3, 2008, and testimony regarding the trader's belief about making money at Houston Ship

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<sup>109</sup> *Barclays*, 144 FERC ¶ 61,041 at P 61 & n.197 (citing *Investigations of Terms and Conditions of Pub. Util. Mkt.-Based Rate Authorizations*, 114 FERC ¶ 61,165, at P 29 (2006)) ("[A]n entity's business purposes will be relevant to an inquiry into manipulative intent, but a 'legitimate business purpose' is not a dispositive, affirmative defense to manipulation.").

<sup>110</sup> BP Answer at 118-22.

Channel, and OE Staff's explanation about how BP's trading ran counter to economic incentives.<sup>111</sup> OE Staff notes that while the Commission could alternatively find that BP acted recklessly, nevertheless its case "is based on intentional conduct."<sup>112</sup>

## 2. Commission Determination

45. We deny BP's motion to dismiss due to the claimed insufficient pleading of scienter in the Staff Report. BP asserts that recklessness must be "extreme" or severe to meet the scienter element of a manipulation claim.<sup>113</sup> That is incorrect. In Order No. 670, the Commission did not adopt a more specific definition of recklessness necessary to establish a violation of the Anti-Manipulation Rule,<sup>114</sup> and, because it is not necessary to address this issue for our present consideration, we decline to do so today.

46. As for the remainder of BP's objections, we note that OE Staff alleged not only that BP acted with the requisite scienter, but OE Staff also provided evidence regarding the scienter of BP's traders, such as knowledge of the effect of BP's trading on the Houston Ship Channel *Gas Daily* index and their motivation to profit from that effect.<sup>115</sup> In so doing, OE Staff satisfied the threshold legal requirement of alleging, with supporting evidence, that BP acted with scienter. Much of BP's objection goes to the weight of and the inferences that should be drawn from the evidence. These are questions of material fact more appropriate for resolution at the hearing, and we will therefore not address them here.

## IV. Issues Set for Hearing

### A. The Anti-Manipulation Rule

47. Based on its review of the Staff Report and the pleadings filed in response to the Show Cause Order by BP and OE Staff, the Commission finds that there are genuine issues of fact material to the decision of this proceeding which require a hearing before

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<sup>111</sup> OE Staff Reply at 50.

<sup>112</sup> *Id.* at 52-53.

<sup>113</sup> BP Answer at 118-20.

<sup>114</sup> *See, e.g., Barclays*, 144 FERC ¶ 61,041 at PP 66-68; Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 53.

<sup>115</sup> *See, e.g., Staff Report*, apps. A (audio file of recorded call), B (transcript of recorded call); Staff Report at 69-71 (recorded calls, trading conduct, profit motivation).

an ALJ. The ALJ should determine whether BP violated section 4A of the NGA and the Commission's Anti-Manipulation Rule. In so doing, the ALJ should make findings respecting subject matter jurisdiction and each of the elements of a manipulation claim, as described in section 1c.1 of our regulations, namely:

(i) Conduct: whether BP “directly or indirectly, . . . (1) . . . use[d] or employ[ed] any device, scheme, or artifice to defraud; (2) . . . ma[d]e any untrue statement of a material fact or omit[ted] to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or (3) . . . engage[d] in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity;”

(ii) Scienter: whether BP acted with actual intent or recklessness; and

(iii) “In connection with” a jurisdictional transaction: whether BP's conduct was “directly or indirectly, in connection with the purchase or sale of natural gas or the purchase or sale of transportation services subject to the jurisdiction of the Commission.”<sup>116</sup>

## **B. Civil Penalty**

48. OE Staff proposes a penalty of \$28,000,000 based on the Commission's Penalty Guidelines.<sup>117</sup> We reserve for our later consideration: (a) whether civil penalties should be imposed for any BP violations, and the determination of the amount of penalties, per section 22(c) of the NGA;<sup>118</sup> (b) whether any other sanctions should be imposed; and (c) whether, and the method by which, BP should disgorge any unjust profits, and in what amount.

49. The Commission will make these determinations based on the record developed at the hearing. To assist us in determining these issues, we direct the ALJ to make factual findings on the statutory factors relevant to a civil penalty and to the factors set forth in the Penalty Guidelines regardless of the ultimate determination of the manipulation claim. In particular, the ALJ shall:

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<sup>116</sup> 18 C.F.R. § 1c.1(a) (2013); Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 49.

<sup>117</sup> *Enforcement of Statutes, Orders, Rules, and Regulations*, 132 FERC ¶ 61,216 (2010) (Penalty Guidelines).

<sup>118</sup> 15 U.S.C. § 717t-1(c) (2012).

- (i) determine the number of violations, if any, committed by BP and the number of days on which any such violations occurred;<sup>119</sup>
- (ii) make findings regarding loss, the amount of natural gas involved (separately calculating financial and physical natural gas positions), and duration;<sup>120</sup>
- (iii) make findings regarding whether BP “committed any part of the [alleged] instant violation less than 5 years after a prior Commission adjudication of any violation or less than 5 years after an adjudication of similar misconduct by any other enforcement agency”;<sup>121</sup>
- (iv) determine whether “the commission of the [alleged] instant violation violated a judicial or Commission order or injunction directed at [BP] by the Commission or other Federal and state enforcement agencies that adjudicate similar types of matters as the Commission”;<sup>122</sup>
- (v) make findings respecting BP’s compliance program on each of the factors specified in § 1B2.1 of the Penalty Guidelines; and
- (vi) make findings concerning the amount of profits obtained by BP for its alleged manipulative trading conduct, entertaining any reasonable method for calculating this amount,<sup>123</sup> and provide both a gross number of profits and a net amount that deducts BP’s losses from its physical trading.

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<sup>119</sup> See *id.* § 717t-1.

<sup>120</sup> Penalty Guidelines § 2B1.1. In making these findings, the ALJ shall “make a reasonable estimate of loss.” Penalty Guidelines § 2B1.1, commentary note 2(C).

<sup>121</sup> Penalty Guidelines § 1C2.3(c)(2). In its Staff Report and Reply, OE Staff refers to two settlements entered into in proceedings in the federal district court for the Northern District of Illinois and one settlement with the Commission. OE Staff Report at 73 (citing *CFTC v. BP Products North America, Inc.*, No. 1:06-cv-03503 (N.D. Ill. Oct. 25, 2007); *United States v. BP America Inc.*, No. 07-cr-683 (N.D. Ill. Oct. 25, 2007); see also OE Staff Reply at 66-69 (citing *In re BP Energy Co.*, 121 FERC ¶ 61,088 (2007)).

<sup>122</sup> See Penalty Guidelines § 1C2.3(d).

<sup>123</sup> See *Barclays*, 144 FERC ¶ 61,041 at P 149 (concluding in electric manipulation case that disgorgement amount was “reasonable approximation of profits causally connected to the violation. . .”).

The Commission orders:

(A) BP's motion to dismiss and motion to strike Public Citizen's protests are hereby denied.

(B) Public Citizen's protest is hereby placed in the public file associated with this proceeding.

(C) Pursuant to the Commission's authority under the Natural Gas Act, particularly sections 14, 15, 21, and 22, and the Commission's rules and regulations, a public hearing is to be held in Docket No. IN13-15-000 to make findings and a determination as to matters relevant to the issues set forth above in Section IV of this order.

(D) A Presiding Administrative Law Judge, to be designated by the Chief Administrative Law Judge for that purpose pursuant to 18 C.F.R. § 375.304, shall convene a prehearing conference in this proceeding within twenty (20) days after issuance of this order, in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426. The prehearing conference shall be held for the purpose of establishing a procedural schedule. The Presiding Administrative Law Judge is authorized to establish procedural dates and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

( S E A L )

Kimberly D. Bose,  
Secretary.

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