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**THE IMPLICATIONS OF ENRON ON THE
INTERPLAY BETWEEN THE JURISDICTIONS
OF THE CFTC AND THE FERC**

Paul J. Pantano, Jr.
Kari S. Larsen*
McDermott, Will & Emery
600 13th St., N.W.
Washington, DC 20005

* © 2002. All rights reserved. Paul J. Pantano, Jr. is a partner, and Kari S. Larsen is an associate, in McDermott, Will & Emery's Energy and Derivatives Markets Group.

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I. INTRODUCTION

The Federal Energy Regulatory Commission (the "FERC") and the Commodity Futures Trading Commission (the "CFTC") have jurisdiction over different types of power and natural gas transactions. In some areas, their jurisdictions overlap, while in others they are separate and distinct. Recent developments in the energy markets, including the demise of Enron Corporation and its numerous affiliates, have focused the attention of policy makers and market participants on the interplay between the jurisdictions of these two agencies. These developments have also led to investigations by the FERC and the CFTC into potential manipulation of the wholesale power market, prompting additional discussion of jurisdictional overlap. A number of these emerging developments have the potential of subjecting various power and natural gas transactions to conflicting or inconsistent standards of review.

A. Scope of the FERC's Jurisdiction

The FERC is an independent federal regulatory agency under the Department of Energy. The Federal Power Act (the "FPA") grants the FERC jurisdiction over the interstate "transmission of electric energy" and the "sale of electric energy at wholesale."¹ In general, the FERC's jurisdiction extends to physical, wholesale power and transmission transactions. The FERC also regulates various types of transmission rights, both physical and financial, that wholesale market participants use to hedge their exposure to congestion on interstate transmission lines.

Wholesale electricity sellers include generators and power marketers that have obtained approval from the FERC to sell wholesale power at market-based rates. Sellers seeking market-based rate authority, as compared to monopoly utilities that sell power at cost-based rates, must demonstrate that they lack market power. Once the FERC authorizes a power marketer to sell power at market-based rates, the power marketer's rates presumably are "just and reasonable" because, absent a change in circumstances, the seller lacks the market power needed to manipulate prices.²

¹ Federal Power Act ("FPA") § 201, 16 U.S.C. § 824 (2001). See generally 42 U.S.C. § 7171 (2001).

² See, e.g., GWF Energy LLC, Southern Company Services, Inc., 98 F.E.R.C. ¶ 61,330 (Mar. 27, 2002).

Under the FPA, any rate that is "unjust and unreasonable" is unlawful.³ If the FERC finds that the market is not functioning properly or that an individual market participant has market power, the FERC can take steps to ensure that rates are just and reasonable. For example, the FERC can alter the structure of the market, implement reporting requirements, impose price caps, institute mandatory sale requirements, revoke market-based rate authorization from market participants to buy and sell on energy markets, or order refunds.⁴ The FERC can initiate a refund proceeding on its own or based upon a complaint by a private party requesting that the FERC find that wholesale power rates, charges or classifications are unjust and unreasonable.⁵

B. Scope of the CFTC's Jurisdiction

Under the Commodity Exchange Act, as amended (the "CEA"), the CFTC has exclusive jurisdiction over "accounts, agreements [including any transaction which is of the character of or commonly known as an option] and transactions involving contracts of sale of a commodity for future delivery."⁶ The CEA provides that the term future delivery "does not include any sale of any cash commodity for deferred shipment or delivery."⁷ Thus, spot power transactions for immediate delivery and forward power transactions for deferred delivery generally are not subject to the CFTC's jurisdiction.

The CEA does not explicitly define what constitutes a futures contract within the CFTC's jurisdiction or a forward contract excluded from the CFTC's jurisdiction. As a result, the elements of futures and forward contracts have been developed through case law, and various interpretations and policy statements issued by the CFTC.⁸ Anyone who practices commodities and derivatives law is well-aware of the machinations that the courts, the CFTC and commercial parties have gone through trying to distinguish between contracts within and outside of the CFTC's jurisdiction. The dividing lines between contracts on a continuum from spot to forward to swaps and options to futures have become less clear as market participants and transactions become more innovative and sophisticated.

³ FPA § 205(a), 16 U.S.C. 824d (2001).

⁴ See, e.g., FPA § 206, 16 U.S.C. 824e (2001).

⁵ *Id.*

⁶ 7 U.S.C. § 2(a)(1)(A) (2001).

⁷ 7 U.S.C. § 1(19) (2001).

⁸ See Statutory Interpretation Concerning Forward Transactions, (1990-1992 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 24,925 (Sept. 25, 1990); Exemption for Certain Contracts Involving Energy Products, (1992-1994 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 25,633 (Apr. 20, 1993).

Rather than attempt to draw bright-line distinctions between different types of contracts, in late 2000, the U.S. Congress decided to increase the legal certainty and enforceability of commodity contracts by excluding or exempting certain contracts from CFTC regulation. The Commodity Futures Modernization Act of 2000 (the "CFMA")⁹ created, among other things, broad safe harbors for transactions in exempt commodities, including electricity and natural gas, provided that the contract is entered into solely between eligible contract participants ("ECPs") and not on a "trading facility" or between eligible commercial entities ("ECEs") on a trading facility.¹⁰ The CFMA also added a section to the CEA which precludes private parties from claiming that contracts entered into between ECPs "or persons reasonably believed to be [ECPs]" are void, voidable or unenforceable solely because they fail to satisfy the terms or conditions of, or any exemption or exclusion from, any provision of the CEA or the CFTC regulations.¹¹

II. JURISDICTIONAL INTERPLAY BETWEEN THE FERC AND THE CFTC

During the past year, the interplay between the respective jurisdictions of the FERC and the CFTC has raised a number of odd and interesting issues. Here are a few examples starting with the odd:

A. Can a Spot Transaction Last as Long as a Year?

Unlike the CFTC, which generally does not have jurisdiction over spot commodity transactions, the FERC has jurisdiction over physically-settled spot power contracts. In a number of FERC administrative proceedings, parties have raised questions about how to define a spot power transaction. It is not yet clear whether the views of these agencies concerning the definition of a spot transaction will be consistent.

The CFTC has explained that "cash" or "spot" transactions outside of its jurisdiction are "transactions for the immediate sale and delivery of a commodity."¹² Industry practice determines what constitutes the immediate sale

⁹ See Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 (Dec. 21, 2000).

¹⁰ See 7 U.S.C. § 2(h) (2001).

¹¹ 7 U.S.C. § 25(a)(4) (2001).

¹² See, e.g., *Salomon Forex, Inc. v. Tauber*, 8 F.3d 966, 970 (4th Cir. 1993), cert. denied, 511 U.S. 1031 (1994). See also *Dunn v. CFTC*, 519 U.S. 465, 472 (1997) ("spot transactions" [are] agreements for purchase and sale of commodities that anticipate near-term delivery").

and delivery of a cash commodity.¹³ Generally, the commodities industry considers cash or spot transactions as trades in which the commodity is delivered against payment on or within two days of the trade date.¹⁴

In 2001, the FERC issued an order regarding the California wholesale markets in which it defined a spot transaction in the Western Systems Coordinating Council ("WSCC") as a sale that is "24 hours or less and that [is] entered into the day of or day prior to delivery."¹⁵ In a 1998 report on the causes of wholesale electric pricing abnormalities in the Midwestern U.S., the FERC staff similarly described the spot market as "a market where goods are traded for immediate delivery."¹⁶

In a recent administrative proceeding, the FERC ordered one of its administrative law judges to determine whether spot transactions during a particular time period were unjust and unreasonable and, therefore, subject to refunds. The parties seeking a refund tried to broaden the universe of "spot" transactions eligible for refunds to transactions in which the period between the trade date and the delivery date was as long as one year. The parties opposed to a refund argued that there was no rational basis for defining a spot transaction in one geographic area differently from the exact same type of transaction in a smaller portion of the same market. They also pointed out that because the Bankruptcy Code defines forward contracts as transactions involving a maturity

¹³ See, e.g., Bank Brussels Lambert, S.A. v. Intermetals Corp., 779 F. Supp. 741, 748 (S.D.N.Y. 1991) (referring to "the conventions of foreign currency trading" to determine what constitutes the "current market"); Regulation of Noncompetitive Transactions Executed on or Subject to the Rules of a Contract Market, 63 Fed. Reg. 3708, 3712 (Jan. 26, 1998) (noting importance of "prevailing cash market practice" in determining the delivery parameters of a cash market transaction); CFTC, Division of Trading and Markets, Report on Exchanges of Futures for Physicals, 51, 65 (1987) ("CFTC Report") (declaring duration of spot transaction is determined by market practice); see also CFTC Interpretative Letter 98-73, (1998-1999 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 27,449 at 47,155 (Oct. 1998) ("In a spot transaction, immediate delivery of the product and immediate payment for the products are expected on or within a few days of the trade date").

¹⁴ 1 NATIONAL LEGAL RESEARCH GROUP, REGULATION OF THE COMMODITIES FUTURES AND OPTIONS MARKETS § 9.01 (2d ed. 1995).

¹⁵ San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, 95 F.E.R.C. ¶ 61,418 at 62,545, n.3 (June 19, 2001).

¹⁶ Staff Report to the Federal Energy Regulatory Commission on the Causes of Wholesale Electric Pricing Abnormalities in the Midwest During June 1998, Offices of the Chief Accountant, Economic Policy, Electric Power Regulation, and General Counsel G-3 (FERC Sept. 22, 1998).

(delivery) date more than two days after the trade date, it is appropriate to limit spot transactions to those involving delivery within two days of the trade date.¹⁷

The ALJ concluded that, for purposes of this proceeding, spot power transactions are comprised of all sales for up to one month in length, which are entered into one day in advance, or before weekends or holidays, up to 48 hours in advance.¹⁸ This definition of a spot transaction is inconsistent with industry practice and broader than comparable transactions in other commodity markets. It will be interesting to see whether the FERC accepts or modifies the ALJ's recommendation.

B. Are Cash-Settled Power Transactions Subject to the FERC's Jurisdiction?

As is often the case in other commodity markets, many power forward contracts are financially-settled between the parties without actual delivery of the underlying power. In other words, they are "booked-out."¹⁹ A book-out is an agreement between two parties, typically in a chain or string of forward contracts, to settle their respective delivery obligations with a cash payment of the difference between the contract and reference (market) prices, as opposed to making and taking physical delivery.²⁰

The CFTC repeatedly has affirmed that the forward contract exclusion to CFTC jurisdiction remains available even if transactions ultimately are cash-settled provided that delivery "routinely" occurs.²¹ While not addressing

¹⁷ See 11 U.S.C. § 101 (25) (2000) ("forward contract means a contract (other than a [futures] contract) for the purchase, sale, or transfer of a commodity, . . . with a maturity date more than two days after the date the contract is entered in to . . .") (emphasis added); and NY General Obligation Law § 5-701(b) (2001) ("a 'qualified financial contract' [which is enforceable even if not in writing] means . . . a contract . . . for the purchase, sale or transfer of any commodity . . . with a maturity date more than two days after the date the contract is entered into") (emphasis added).

¹⁸ Puget Sound Energy, Inc. v. All Jurisdictional Sellers of Energy and/or Capacity at Wholesale Into Electric Energy and/or Capacity Markets in the Pacific Northwest, 96 F.E.R.C. ¶ 63,044 at 65,386 (September 24, 2001).

¹⁹ Exemption for Certain Contracts Involving Energy Products, (1992-1994 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 25,633 (Apr. 20, 1993).

²⁰ See PAUL HORSNELL & ROBERT MABRO, OIL MARKETS AND PRICES - THE BRENT MARKET AND THE FORMATION OF WORLD OIL PRICES 41 (1993).

²¹ See Statutory Interpretation Concerning Forward Transactions, (1990-1992 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 24,925 (Sept. 25, 1990); Exemption for Certain Contracts Involving Energy Products, (1992-1994 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 25,633 (Apr. 20, 1993).

electricity markets directly, the CFTC has explained that cash settlement does not change a forward contract into a futures contract if the original contracts are entered into between commercial participants in connection with their businesses and create specific delivery obligations that impose substantial commercial risks on the parties and the book-out transactions are separately agreed to in individually (or multilaterally, in the case of delivery chains or loops) negotiated, new agreements.

Because the FERC historically has taken the position that it does not have jurisdiction over financially-settled contracts, whether they are spot, forward or futures contracts, it previously did not require power marketers to report booked-out power transactions.²² Rather, it only required power marketers to report those contracts that resulted in delivery.²³

The FERC recently amended its quarterly reporting rules to require power marketers to disclose financially-settled power transactions.²⁴ Power marketers are now required to report counterparty names, products offered, contract date and duration, and price terms, including book-outs, for each energy transaction. The FERC claimed that it was not deciding whether it had jurisdiction over book-outs. However, it argued that book-outs consist of sales for resale of electric energy in interstate commerce by a public utility and “affect” or “relate to” transactions and prices paid for power sales that go to delivery – thereby fitting the definition of a jurisdictional transaction and supporting the FERC’s finding that market participants must report book-outs in their Electric Quarterly Reports. The FERC reasoned that the disaggregated transactions underlying a book-out are physical power sales that obligate the parties to deliver power at a specified price and that the book-out does not arise until the public utility enters into later agreements that allow deliveries to be offset – in the absence of the offsetting power sales, power transmission would occur. The FERC asserted that a majority of market-based

²² New York Mercantile Exchange, 74 F.E.R.C. ¶ 61,311 at 61,987 (Mar. 27, 1996). Before trading electricity futures contracts, NYMEX requested the CFTC's approval to offer the contracts and an order from FERC establishing that such contracts were not securities as defined by the FPA. FERC found that a "plain reading" of the security definition under the FPA would not include an electricity futures contract. However, FERC noted that, in order to avoid future misunderstandings, it would have jurisdiction "pursuant to Sections 205 and 206 of the FPA if the electricity futures contract goes to delivery, the electric energy sold under the contract will be resold in interstate commerce, and the seller is a public utility." *Id.* at 61,985, 61,987. In addition, FERC stated that it was not addressing whether it has jurisdiction over other risk management instruments. *Id.* at 61,984.

²³ Annual Charges Under the Omnibus Budget Reconciliation Act of 1986, CNG Power Services, et al., 87 F.E.R.C. ¶ 61,074 at 61,302 (1999).

²⁴ Revised Pub. Utility Filing Requirements, 99 F.E.R.C. ¶ 61,107 (Apr. 25, 2002), 67 Fed. Reg. 31,044 (May 8, 2002) (to be codified at 18 C.F.R. pts. 2, 35).

transactions at issue are delivered without physical transmission, but there is physical delivery.²⁵

Although the FERC does not have jurisdiction over derivatives transactions, it is considering whether, and to what extent, it should require power marketers to report their energy derivatives transactions on an annual basis. It is not clear what the FERC plans to do with this information if it requires it to be reported. Comments from industry participants on this FERC Notice of Proposed Rulemaking were submitted by March 11, 2002.

C. How is Market Manipulation determined?

The most significant area of overlap between the jurisdictions of the CFTC and the FERC is price manipulation. The standards applied by the two agencies in analyzing whether prices have been manipulated are substantially different.

The CFTC generally does not have jurisdiction over cash market transactions. However, it has jurisdiction to investigate and prosecute alleged manipulation of the cash price of a commodity.²⁶ In addition, the CFTC can compel persons to produce information about cash market transactions in connection with an investigation or prosecution of an alleged manipulation of the price of a cash commodity or futures contract.²⁷

The CFTC determines if there has been a violation of the CEA's anti-manipulation provisions by evaluating whether: (1) a party has the ability to influence market prices; (2) the party specifically intended to do so; (3) there was an artificial price; and (4) the party's conduct caused the artificial price. The CFTC also considers the dissemination of false reports and rumors to constitute market manipulation, including offering investment advice to favorably affect prices in markets in which the advisor has a position and issuing false press releases.²⁸ The potential sanctions the CFTC can seek or impose include civil penalties, restitution, injunctions/cease and desist orders, and trading prohibitions. Unlike the FERC, the CFTC does not have the authority to set or to retroactively adjust market prices.

²⁵ *Id.*

²⁶ *See* 7 U.S.C. §§ 9, 15 (2001); 17 C.F.R. 11.2 (2001).

²⁷ *See* 7 U.S.C. §§ 9, 15 (2001).

²⁸ *See, e.g.,* Rueben Earl McGuigan, 9 Agric. Dec. 1299 (1950); Ralph W. Moore, 9 Agric. Dec. 1151 (1971).

On August 21, 2001, for example, the CFTC accepted an offer of settlement by Avista Energy and issued an order in which it found that, between April and August 1998, Avista's traders engaged in a scheme to manipulate the settlement price of electricity futures on the NYMEX to increase the value of Avista's over-the-counter ("OTC") positions.²⁹ The CFTC concluded that Avista had the financial ability to place, and placed large, market-moving orders during the close on options expiration days in an illiquid market. According to the CFTC, the evidence overwhelmingly showed that Avista intended to, and did, influence electricity market prices.³⁰ The CFTC ordered Avista to cease and desist from further violations of the CEA, pay a penalty of \$2,100,000, and comply with certain undertakings specified in the settlement order.³¹ The NYMEX recently stopped trading electricity futures because market participants were not using electricity futures contracts.³²

Unlike the CFTC, which focuses on whether a price is artificial, the FERC evaluates whether energy or transmission rates are just and reasonable.³³ This is a much more subjective standard than the one utilized by the CFTC. Neither the FPA nor its legislative history provides any guidance regarding the parameters of the just and reasonable standard or how it should be applied by the FERC.³⁴ The original goal of the standard was to ensure that regulated utilities, which charge for power at cost-based rates, earn a reasonable rate of return for their shareholders.

Much of the caselaw interpreting the just and reasonable standard pre-dates FERC's decision to authorize marketers to sell power at market-based rates. The courts have explained that the FERC is not required to use any single method or formula in determining whether a rate is just and reasonable.³⁵ To satisfy the standard, a rate simply must fall within a "zone of reasonableness."³⁶

²⁹ In the Matter of Avista Energy, Inc. and Griswald, (2000-2002 Transfer Binder) Comm. Fut. L. Rep. (CCH) ¶ 28,623 (Aug. 21, 2001).

³⁰ Id. at 52,359.

³¹ Id.

³² See NYMEX, Notice Of Delisting Of NYMEX Electricity Futures Contracts, Notice 02- 57 (Feb. 14, 2002), available at <http://www.nymex.com>.

³³ 16 U.S.C. § 824d (2001).

³⁴ See Duguesne Light Co. v. Barasch, 488 U.S. 299, 310 (1989); see generally McCormick and Cunningham, The Requirements of the "Just and Reasonable" Standard: Legal Bases for Reform of Electric Transmission Rates, 21 Energy 389 (2000).

³⁵ See, e.g., Wisconsin v. FPC, 373 U.S. 294, 309 (1963).

³⁶ Jersey Cent. Power & Light Co. v. FERC, 810 F. 2d 1168, 1177 (D.C. Cir. 1987).

The FERC repeatedly has emphasized that there is "no precise legal formulation for setting a just and reasonable rate and no precise bright-line for when a rate becomes unjust and unreasonable."³⁷ In the context of a competitive market, the FERC can "rely on market-based rates in lieu of cost-of-service regulation to ensure that rates satisfy [the just and reasonable] requirement."³⁸ On the other hand, "if over time rates do not behave as expected in a competitive market, the [FERC] [will] step in to correct the situation."³⁹ The FERC's reliance on a competitive market to ensure that wholesale power rates are just and reasonable suggests that the FERC should use an objective standard, like the artificial price test, when trying to determine whether market-based rates have been manipulated.

If the FERC determines that a rate is unjust and unreasonable, it will set what it considers a just and reasonable rate, and will issue an order imposing that rate on the parties to the affected transaction.⁴⁰ It also can require the seller to refund to the buyer the difference between the original and revised rates.⁴¹

III. THE FERC'S WESTERN MARKETS MANIPULATION INVESTIGATION

On February 13, 2002, the FERC issued an order directing its staff to investigate whether any entity, including Enron Corporation (through any of its affiliates or subsidiaries), manipulated or otherwise exercised undue influence over wholesale prices for electric energy or natural gas in the West, resulting in potentially unjust and unreasonable rates in long-term power sales contracts.⁴² The order initiates a broad investigation and allows the FERC's staff to "obtain information on any and all matters relevant to potential market manipulation in the West, including comparative information from other markets in the country."⁴³

FERC officials have stated that since the FERC's "responsibility and jurisdiction" lie primarily in the physical assets market, rather than in the financial

³⁷ San Diego Gas & Electric v. Sellers of Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, 93 F.E.R.C ¶ 61,294 at 61,998 (Dec. 15, 2000) ("December 15 Order").

³⁸ Louisiana Energy and Power Authority v. FERC, 141 F. 3d 364, 365 (D.C. Cir. 1998).

³⁹ December 15 Order at 61,998.

⁴⁰ FPA § 206, 16 U.S.C. 824e (2001).

⁴¹ Id.

⁴² Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices, 98 F.E.R.C. ¶ 61,165 (Feb. 13, 2002).

⁴³ Id. at 61,614.

assets markets where many of Enron's activities occurred, it intends to consult with the CFTC, the Securities Exchange Commission, the Department of Justice, and the Federal Trade Commission to gain their assistance in understanding and analyzing financial markets.⁴⁴ In this regard, in a letter to Congress, dated March 7, 2002, CFTC Chairman Newsome noted that the CFTC, as well as other federal agencies, "are conducting independent inquiries" into the events leading to the collapse of Enron.⁴⁵

Pursuant to the February 13, 2002 Order, the FERC Staff issued Data Requests on May 8 and May 21, 2002, requesting admissions and documents from market participants in the Western Systems Coordinating Council relating to market activities during the years 2000-2001.⁴⁶ The May 8, 2002 Data Request sought all admissions and documents concerning, generally, types of trading described as "inc-ing load" and "relieving congestion." FERC Staff described "inc-ing load" as artificially increasing load (demand) on the schedule the company submits to the California Independent System Operator (Cal ISO) with a corresponding amount of generation (supply). The company sends the scheduled generation but does not take the load as scheduled, resulting in the Cal ISO paying the company for its excess generation. "Relieving congestion" involves a company creating congestion in the California Power Exchange's (Cal PX) market and then relieving such congestion in the real-time market in order to receive a congestion premium.

The May 8, 2002 Data Request sought admissions and documents concerning the following types of trading strategies or any variants thereof:

- (1) "Export of California Power," in which a company buys energy at the Cal PX to export outside of California to get the price spread between the capped California markets and other uncapped markets;
- (2) "Non-Firm Export," where a company schedules non-firm energy from a point in California to a point outside California to obtain a

⁴⁴ Summary of Testimony of Pat Wood, III Chairman, Federal Energy Regulatory Commission Before the Subcommittee on Energy and Air Quality of the Committee on Energy and Commerce United States House of Representatives, (Feb. 13, 2002), [available at www.ferc.gov/news/congressionaltestimony/wood-02-13-02.pdf](http://www.ferc.gov/news/congressionaltestimony/wood-02-13-02.pdf).

⁴⁵ Letter to Senators Crapo and Miller from CFTC Chairman James E. Newsome, Mar. 7, 2002.

⁴⁶ Letter to Sellers of Wholesale Electricity and/or Ancillary Services in the United States Portion of the Western Systems Coordinating Council During the Years 2000-2001, Docket No. PA 02-2-000 (FERC Staff May 21, 2002); Letter to Sellers of Wholesale Electricity and/or Ancillary Services in the United States Portion of the Western Systems Coordinating Council During the Years 2000-2001, Docket No. PA 02-2-000 (FERC Staff May 8, 2002).

counterflow congestion payment from the Cal ISO and then cuts the energy flow;

(3) "Death Star," in which the company schedules energy in counterflow to appear to relieve congestion, with no actual power put on or taken off the grid;

(4) "Load Shift," where the company submits artificial schedules giving the appearance of relieving congestion in one zone and shifting it to a lesser congested zone in order to receive inter-zonal congestion payments;

(5) "Get Shorty" or "paper trading," in which a company sells ancillary services in the Day-ahead market and then cancels the commitment to sell and buying ancillary serves in the real time market to cover its position;

(6) "Wheel Out," where a company schedules a flow over a completely constrained facility, knowing the schedule will be cut and it will receive a congestion payment without actually sending any energy out;

(7) "Fat Boy," in which the company artificially increases load on the schedule it submits to the Cal ISO with a corresponding amount of generation. The company then dispatches the generation it scheduled, which is in excess of its actual load. This results in the Cal ISO paying the company for the excess generation;

(8) "Ricochet" or "megawatt laundering," in which the company: (i) buys energy from the Cal PX and exports to another entity, which charges a small fee; and (ii) the first company buys it back and resells the energy back to the Cal ISO in the real-time market;

(9) "Selling Non-Firm energy as Firm," in which the company sells or resells non-firm energy to the Cal PX, but claims that it is firm energy, allowing the company to receive payment from the Cal ISO for ancillary services that it claims to be providing, but does not in fact provide; and

(10) "Scheduling Energy to Collect Congestion Charge II," where a company (i) schedules a counterflow even though it does not have any available generation; (ii) in real time, the Cal ISO charges the company for

each MW that it was short; and (iii) the company collects a congestion payment associated with the counterflow scheduled.⁴⁷

The May 21, 2002 Data Request sought admissions and documents concerning any sales of electricity products to another company together with a simultaneous purchase of the same product at the same price, commonly referred to as "wash," "round trip" or "sell/buyback" trading. If a company admitted engaging in the foregoing activities, the Data Request asked the company to describe all policies and procedures implemented to prevent future transactions of this type.

As to the majority of the above strategies, there does not appear to be any express prohibitions under the FPA, the FERC tariffs and decisions, or Cal ISO rules against such trading practices unless they result in a price that is unjust and unreasonable. Wash sales, for example, are not specifically prohibited by FPA, although they can create regulatory issues in a variety of other contexts, including for publicly traded companies that report revenues on a gross basis in their financial statements.

By contrast, the CEA expressly prohibits wash sales.⁴⁸ To prove a wash sale violation, the CFTC must demonstrate that the trader did not intend to make a bona-fide transaction.⁴⁹ Proving the existence of trading that is suspicious due to matching aspects of various sales and purchases is insufficient. The CFTC must also show "a specific intent . . . to avoid the open market and its inherent risks."⁵⁰ The CFTC and federal courts have acknowledged that legitimate trading may produce an outcome identical to a wash sale.⁵¹ In its Data Requests, the FERC Staff has not explicitly indicated whether intent will be a factor in its review of any alleged power wash trades.

⁴⁷ Id. The descriptions of these trading strategies are based upon the FERC's interpretation of such strategies and memoranda drafted by Enron council, dated December 6, 2000, and December 8, 2000, which describe in detail certain trading strategies engaged in by Enron traders during the years 2000 and 2001.

⁴⁸ See 7 U.S.C. § 6c(a).

⁴⁹ See In re Bear Stearns & Co., [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,994 (CFTC Jan 25, 1991).

⁵⁰ See In re Gorski, [1998-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,742 (CFTC Aug. 23, 1999).

⁵¹ See, e.g., In re Glass, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27.337 (CFTC Apr. 27, 1998); In re Gilchrist, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,993 (CFTC Jan. 25, 1991).

IV. LOOKING FORWARD

The power and natural gas markets are interesting examples of the spectrum of wholesale commodity transactions. Historically, the regulation of those transactions has been largely separated between the FERC, which primarily regulates physical transactions, and the CFTC, which primarily regulates financial transactions.

It is increasingly apparent that the distinctions between purely physical and purely financial transactions and how those transactions should be regulated are not always readily discernable. It is also increasingly apparent that there are a number of areas in which the jurisdictions of, and legal precedents set by, the FERC and the CFTC may overlap, intersect or conflict. The concurrent inquiries by the FERC and the CFTC into the activities of Enron, its affiliates and other wholesale power and natural gas sellers may provide an indication about whether these agencies will apply similar standards to alleged manipulative conduct in the physical and financial power markets.