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BP Initial Decision Adopts FERC Staff's Positions

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Seven years after the Federal Energy Regulatory Commission ("FERC"� or the "Commission"�) first opened an investigation into the trading practices of BP America Inc. and certain of its affiliates (collectively "BP"�), on August, 13, 2015, Administrative Law Judge Carmen Cintron ("ALJ Cintron"�) issued her Initial Decision in the case of *BP America Inc.*, finding that "BP engaged in market manipulation"� by "intentionally [selling] large volumes of next-day physical gas at HSC in a way designed to benefit their corresponding short financial positions."� ***[1]*** ALJ Cintron agreed with FERC Staff on all the material issues in the case, disagreeing with BP that FERC did not have jurisdiction over the case and finding BP's defenses unpersuasive. FERC Enforcement initiated its investigation into BP based on a recorded phone conversation between trading trainee Clayton Luskie ("Luskie"�) and his colleague/mentor Gradyn Comfort ("Comfort"�). During the recorded conversation, Luskie, who was attending an internal BP trader certification course, stated to Comfort that he may have given the false impression to a senior official that they were engaging in market manipulation. Over the course of the conversation, as Luskie explained the Texas team's trading activities, including whether their trading and transportation was economic, Comfort repeatedly cut Luskie's questions off, giving the listener the impression that he wanted to cut short the conversation. Further evidence showed that after ending the conversation on the recorded line, Luskie and Comfort soon thereafter spoke on an unrecorded line. After completing its investigation, FERC Enforcement alleged that traders on BP's Texas trading desk engaged in a scheme to defraud by engaging in uneconomic trading in the physical markets at the Houston Ship Channel ("HSC"�) designed to suppress the HSC *Gas Daily* index, in order to benefit the team's pre-existing HSC-Henry Hub financial spread position.***[2]*** ALJ Cintron found in her Initial Decision that Enforcement Staff had met its burden of proof in establishing that BP had intentionally engaged in market manipulation. Specifically, ALJ Cintron noted that "[o]ne indicia of manipulation is the existence of benefiting financial positions that are "˜directionally opposite' to physical positions ["¦] especially if the respondent does not attempt to, or cannot, explain or justify the increases in positions."� ***[3]*** ALJ Cintron's decision stressed the fact that BP had "not adequately explained the changes in their trading"� during the relevant time period and had provided "no economic or other justification for their ["¦] unprofitable trading patterns."[4] Further, ALJ Cintron also agreed with Enforcement Staff that BP had acted with the intent to manipulate, citing *Barclays* and *Brian Hunter* for the proposition that "open market transactions undertaken with manipulative intent are sufficient to establish scienter."[5] ALJ Cintron found that BP's team engaged in "hundreds of affirmative acts" to further its manipulative scheme, including "680 fixed-price sales at HSC, 101 bid-initiated sales at HSC when they could have hit a more economic bid at Katy, and 129 offer-initiated sales when they could have sold more economically by adjusting their offer price at Katy."[6] A threshold issue in the case is whether FERC has jurisdiction over BP's conduct. Enforcement Staff asserted that FERC has jurisdiction when "a manipulative scheme's conduct is intended to affect jurisdictional transactions."[7] BP argued that because it had not engaged in any jurisdictional natural gas sales at HSC, FERC lacked jurisdiction.[8] Further, BP asserted that purely intrastate transactions affecting an index do not and should not fall under the Commission's jurisdiction. [9] Ultimately, ALJ Cintron agreed with the more expansive view of jurisdiction argued by Enforcement Staff, finding that Staff had "proved Commission jurisdiction ["¦] through [jurisdictional] third party transactions priced off of the HSC *Gas Daily* index, [jurisdictional] cash-out transactions priced off the HSC *Gas Daily* index, and BP's own [jurisdictional] next-day, fixed-price sales of gas at HSC made to suppress the HSC *Gas Daily* index."[10] ALJ Cintron quoted Order No. 670 for the proposition that the Commission has jurisdiction when an entity engaging in fraud or manipulation "intended to affect, or acted recklessly to affect, a jurisdictional transaction."[11] ALJ Cintron rejected outright BP's arguments that accepting jurisdiction over sales affecting an index would be at odds with the Natural Gas Act, because it would "necessarily include intrastate transactions," and that doing so would subject all parties reporting transactions to Commission jurisdiction, a "case of the exception swallowing the rule."[12] ALJ Cintron responded that jurisdiction will still be limited to cases where a showing is made as to a "nexus ["¦] between manipulation and Commission jurisdictional transactions in order for the Commission to properly have jurisdiction. Therefore, not every transaction reported would be subject to Commission jurisdiction; only those transactions where there exists a connection between manipulative behavior and jurisdictional transactions."[13] Because jurisdictional sales were priced off of an index found to have been manipulated by BP's actions, ALJ Cintron held that the Commission had jurisdiction over the case.[14] The August 13, 2015 Initial Decision serves as the first substantive ruling in the case. Going forward, , BP will have the opportunity to raise its defenses again before the Commission, which will issue a Final Decision on the merits of the case. Depending on the outcome of the Final Decision, BP may challenge the decision in federal appellate court.[15] [1] *BP America Inc.*, 152 FERC ¶ 63,016 at P 276 (2015) (Initial Decision). [2] *Id.* at P 6. [3] *Id.* at P 33. [4] *Id.* at PP 77, 276. [5] *Id.* at 99. [6] *Id.* at P 187. [7] *Id.* at P 129 (internal quotations and citations omitted). [8] *Id.* at P 137. [9] *Id.* at P 139. [10] *Id.* at P 146. [11] *Id.* at P 145 (internal quotations omitted). [12] *Id.* at PP 149-150 (internal quotations omitted). [13] *Id.* at P 150. [14] *Id.* at P 152. [15] *Barclays Bank*

PLC, another major manipulation action brought by FERC Enforcement, is currently on review in federal court. *See* Lias et al., *Federal District Court Denies Barclays Motion to Dismiss FERC Petition Which Alleges Manipulation and Assesses Significant Penalties,* Energy Legal Blog (May 21, 2015), *available at* http://www.energylegalblog.com/archives/2015/05/21/6239?utm_source=feedburner&utm_medium=email& In ruling on a motion to dismiss, the Eastern District of California in the *Barclays* case held that FERC had jurisdiction over alleged manipulation of financial swaps, when the alleged manipulation occurred in physical products to benefit a financial position. The District Court also found that FERC was not barred from bringing manipulation actions against individual traders.