Beyond the Boardroom: Understanding the Energy Industry

“Federal Energy Regulatory Issues”

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Agenda

• Key Regulatory Issues Affecting Energy Industry
• Role of FERC
• Conclusions
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There are three paths to change regulatory policy and law: Congress, agencies, courts

**Key Regulatory Issues: How Policy Changes**

- **Congress:** energy legislation normally bipartisan
- **Agencies** do more than implement and administer law – they can also change law and policy
  - Reinterpreting existing law, exercising discretionary authority
  - Biggest changes in electric and gas regulatory policy in past 30 years were achieved by FERC reinterpreting decades old laws
    -- Congress played no role in these major changes
- **Courts** also change regulatory law/policy by changing settled interpretation of existing law
  - Court decisions as likely to expand as contract agency authority

Pace of regulatory policy changed has increased
Key Regulatory Issues: Change is a Constant

• Electric and gas markets heavily regulated – electricity industry never “deregulated”
• Regulatory burden on energy industry increasing
• Regulation (aka “policy”) lays down “rules of road” and rules are subject to change
• Multiple regulators – depending on business lines – FERC, EPA, NRC, CFTC, state PUC, other state agencies
  – Little or no coordination among regulatory bodies
  – Differing quality of regulation
• Regulatory change can occur much faster than new law

Companies can initiate change in regulatory policy … but hardly ever try
Differences in electric/gas regulatory construct driven by differences in industry structure

Key Regulatory Issues: Industry Structure

- **Gas industry – regulatory jurisdiction**
  - Production – highly competitive, deregulated, no market power
  - Transportation – large networks, exclusive FERC regulation
  - Distribution – exclusive state regulation

- **Electric industry – regulatory jurisdiction**
  - Generation – no deregulation – shared jurisdiction – FERC regulates wholesale power sales, states regulate retail sales
  - Transmission – shared jurisdiction*, disaggregation
  - Distribution – regulated exclusively by states

Gas regulation – regulatory jurisdiction better aligns with industry structure, much smaller role of government utilities
FERC has many electric regulatory policy initiatives

Key Regulatory Issues: Electric

- Reliability regulation
- Grid policy reform – cost allocation, siting, planning, incentives
- Wind/solar integration
- Energy efficiency/demand response
- Wholesale competition – RTO market rules
- Enforcement

Electric regulatory policy in flux in number of areas
Fewer federal regulatory issues on gas side – because FERC sees gas policy is sound and reform is not needed

**Key Regulatory Issues: Gas**

- Shale gas production
- Pipeline rate cases
- Infrastructure development
- Electric-gas coordination
- Enforcement
- Possible LNG exports
- Pipeline safety (DOT/PHMSA)

Fewer changes expected on gas regulatory policy
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FERC does more than set rates – it sets policy – not judges in black robes

FERC: Overview

- Old agency – established in 1920
- Independent: not subject to President/Congress control
- Multi-member Commission: 5 members, 1 Chairman
- Highly qualified staff – dedicated to Chairman’s agenda
- Heavy workload – 1,200+ orders per year – 3-5 per day
- 66% electric, 30% gas, remainder-hydropower/oil pipelines
- Quality of FERC regulation praised by analysts
- Much less partisan other multi-member commissions

FERC is principal energy agency of federal government – not DOE
FERC has 5 missions – 2 of which are relatively new:
1. Energy infrastructure – established in 1920
2. Economic regulation – established in 1935, 1938
4. Enforcement – modern program established in 2005
5. Electric reliability – established in 2005

FERC missions have steadily expanded over time

Enforcement and electric reliability missions still being implemented
Oldest mission – started in 1920 with hydro, expanded to gas pipelines and storage, electric transmission

**Energy Infrastructure**

- **Gas**
  - Pipeline siting – exclusive and preemptive
  - Storage projects
  - LNG terminals
- **Electric**
  - Limited transmission siting authority
- **Hydropower**
  - Licensing – exclusive and preemptive – 1,700 projects

Infrastructure mission focused on gas pipelines and hydro projects
Core mission: established in 1930s – expanded since

Economic Regulation

- **Electric**
  - Mergers – federal and state approval
  - Rate – cost based-rates and market-based rates
  - Market rules – RTOs/ISOs
  - Transmission open access, planning, cost allocation

- **Gas**
  - Pipeline rates and terms of service
  - Transportation open access
  - Storage

Economic regulation mission focused primarily on electric markets, secondary focus on gas markets
Safety mission evolved from hydropower regulation

Safety

- **Hydropower**
  - Dam safety is focus of FERC
- **Gas**
  - LNG projects – shared safety role with Coast Guard/DOT

Safety mission not widely recognized – quiet success
Prospect of large civil penalties, reputational harm, loss of privileges, such as market-based rate authority

**Enforcement**

- Civil penalty authority ($1 million/day/violation)
  - Penalty guidelines
  - Flexibility in determining continuing violations
- Anti-manipulation rule
- Market and tariff rules, hydropower licenses
- Electric reliability standards
  - Role of NERC and Regional Entities
  - Very large and diverse regulated community
- Corporate compliance programs

Enforcement mission – new mission – work in progress
Reliability is new mission – many challenges exist

Electric Reliability

• FERC establishes mandatory reliability standards
  – FERC can’t modify proposed standards – can direct changes

• Self regulatory organization – Electric Reliability Organization (ERO) – NERC – partnership
  – ERO develops draft reliability standards
  – Delegated enforcement authority from FERC – constitutional?
  – Regional Entities also enforce reliability standards

• Major challenges – ambiguous standards, inconsistent interpretation, enforcement, FERC/NERC relationship

FERC reliability regulation has become very contentious
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• Regulatory policy will continue to change, especially electricity policy – and pace of change may increase
• “Regulatory certainty” – relative certainty, not absolute
• Regulated companies must be as smart about regulation as they are about financing, engineering, operations
• Possible Congress acts on energy legislation – deadlock between President and Congress does not preserve policy status quo – shifts initiative to agencies
• Possible to change regulatory policy from the outside
• Judicial review – should challenge agency decisions
• Enforcement – hard to successfully litigate agency that comprehensively regulates your business
• Policy change/technology can change industry structure

“The future ain’t what it used to be” – Yogi Berra