

INSIGHTS

Court Rejects FERC's Attempt to Limit Defendant's Rights

July 27, 2016

By: [Michael W. Brooks](#)

On July 21, 2016, the U.S. District Court for the District of Massachusetts issued an order finding that Maxim Power Corp. and several affiliates and an employee (collectively, the “Maxim Respondents”) were entitled to a full trial on the merits and discovery rights. The ruling came in an action by the Federal Energy Regulatory Commission (“FERC”) seeking an order affirming FERC’s assessment of significant civil penalties against Maxim for alleged violations of the Federal Power Act’s (“FPA”) prohibition on market manipulation and related FERC rules. The court’s order is significant both for its determination that an action seeking enforcement of a FERC penalty assessment under the FPA should proceed as an ordinary civil action and the dim view that it takes of the fairness of the existing FERC enforcement process. Noting that a process in which FERC acts as both investigator and judge is inherently biased, the court found that due process requires that the FPA’s reference to *de novo* review of a FERC penalty assessment be interpreted in a manner that ensures that respondents in FERC enforcement actions be afforded an opportunity to a full hearing and discovery rights at the district court stage. While the court recognized that the discovery process should be tailored in a manner that avoids duplication of any discovery efforts or information exchange that occurred in the underlying FERC proceeding, the court stressed that respondents must have an opportunity to depose FERC witnesses or other third parties. Not only does the order recognize that respondents in FERC enforcement actions should be afforded an opportunity to obtain the evidence necessary to present a full defense, but the court’s reasoning raises the question of whether FERC enforcement staff—who already will have had the opportunity to conduct a full investigation in the underlying proceeding—should be permitted to conduct any additional discovery at the district court stage.

The FPA sets out two procedural avenues for respondents in actions where FERC has proposed to assess a civil penalty for violations of FERC’s rules and regulations:

- **Administrative Law Judge (“ALJ”) hearing:** A respondent may elect to adjudicate the allegations before a FERC ALJ, including a full trial and discovery rights.
- **Immediate penalty assessment and “*de novo*” review:** Alternatively, a respondent may elect an immediate penalty assessment, followed by “*de novo* review” of any FERC order assessing civil penalties against the respondent in a U.S. District Court.

The issue presented to the court was whether the reference to *de novo* review entitled the Maxim Respondents to a full trial-type hearing. Generally, defendants assumed that the FPA's reference to *de novo* review meant that respondents electing an immediate penalty assessment were entitled to a full trial on the merits when FERC sought to enforce its penalty in a U.S. District Court. In recent years, however, FERC has taken the position that a full trial and discovery rights is not required. Instead, FERC Enforcement Staff has argued that a U.S. District Court is only required to review FERC's penalty assessment to determine whether FERC's order is supported by credible evidence and that the respondent had failed to rebut the claims against it in the underlying FERC action. While FERC Enforcement Staff has recognized that a court may order supplemental fact finding to the extent that it deems appropriate, FERC Enforcement Staff has taken the position that FERC's enforcement process affords respondents with ample opportunities to present a defense such that additional fact-finding and discovery is unnecessary. FERC Enforcement Staff also has argued that respondents must elect an ALJ hearing to the extent that they believe that a full trial is necessary to mount a defense.

The July 21 Order rejects this limited interpretation of *de novo* review. Specifically, in the July 21 Order, the court held that the FPA's reference to *de novo* review requires the court, upon reviewing a civil penalty assessment issued by FERC, to treat the matter as an "ordinary civil action" such that it is "governed entirely by the Federal Rules of Civil Procedure and culminates in a jury trial." The district court of Massachusetts decided that "it [was] clear... that *de novo* means 'a fresh, independent determination' that gives 'no deference' to FERC's decision." The court also noted that the language of the FPA was strikingly similar to the language of the Natural Gas Policy Act, which FERC administers and has recognized as conferring a right to a full trial for review of agency actions.

The court found that the interpretation advocated by FERC would not be fair to respondents, who would not have any ability to determine what due process rights would be afforded to them at the district court level—something which Congress could not have intended. The court also noted that the fact that FERC performs both an investigatory and adjudicatory function under its existing enforcement processes creates "an inherent bias in the decision making process, even if that bias is entirely unintentional and even if the combination of functions does not alone violate due process." The court found that while FERC had taken the position that the underlying proceeding had been "adversarial" and that the Maxim Respondents had been free to submit evidence and arguments to support its defense, the court noted that they were "unable to seek discovery, depose witnesses interviewed by FERC, gain any insight into the presentation of the case made by FERC's enforcement staff to the commissioners during the investigative phase, or present their own witnesses." For these reasons, the court stated that the "fundamental requirement of due process . . . [that a person] have the opportunity to be heard at a meaningful time and in a meaningful manner" required that the Maxim Respondents be afforded an opportunity for fact finding at the district court level.

While the court found that FERC's action must proceed as an ordinary civil action, the court added that discovery should be tailored in a manner that avoids needless duplication and production of evidence that had been considered in the underlying FERC proceeding. Recognizing that extensive evidence had been reviewed and exchanged by the parties in the underlying FERC proceeding, the court directed FERC and the Maxim Respondents to craft a discovery plan that avoids "replicating these efforts or targeting anything that has already been submitted or reviewed." Nevertheless, the court emphasized that it "would not be fair or

conducive to *de novo* review to limit the factual record to the materials FERC wants the court to see” and that the Maxim Respondents should be permitted to “seek discovery from witnesses interviewed by FERC or present their own witnesses.”

The July 21 Order represents a significant victory for those that believe that targets of FERC enforcement actions should have the right to have the allegations against them tested in a civil action and be afforded the due process rights typically afforded to litigants in such actions. If adopted by other courts with pending FERC penalty assessment actions, the interpretation set out in the July 21 Order would ensure that respondents in FERC enforcement actions have the ability to seek testimony and evidence from third parties, including regional transmission organizations and independent system operators, relevant to the claims against them. At the same time, the court’s reasoning that discovery should be circumscribed to avoid duplicating any efforts that occurred in the underlying FERC investigation and related proceeding raises the question of whether FERC Enforcement, which had the ability to conduct discovery in the underlying FERC proceeding and investigation, should have the opportunity to conduct any additional discovery at the district court level.