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FERC Regulations: Managing Compliance Through ETRM Technology

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Abstract

With increasing government regulations and the subsequent pressure to comply, energy companies are dealing with many challenges, including time-consuming, manual, and error-prone business processes in order to meet these requirements. This paper will explore the ever-changing environment energy companies operate within and focus on utilizing technology to manage Federal Energy Regulatory (FERC) regulations for U.S. energy companies who buy and sell natural gas, electricity and crude oil. More and more, these companies are turning to technology to provide transparency into every transaction, manage their risk and avoid penalties. Specifically, Energy Trading and Risk Management (ETRM) solutions can deliver vast benefits to these market participants with accurate, real-time automated reporting capabilities and tools to ensure adequate controls needed to comply with current and future FERC regulations.

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We live in a period of increasing governmental regulation. It is no surprise, really, that the aftermath of a series of financial mishaps, record oil and gas volatility, rising carbon dioxide emissions and large institutional failures would usher in a more proactive and, in many respects, punitive approach to regulation. It is a response aimed at restoring confidence in American business and in the regulators who watch over them.

The energy industry, like others, is moving to ensure that its compliance programs are aligned with the interests of its constituents. The Energy Policy Act of 2005 provided the foundation for a number of new regulations, including regulations to ensure price transparency in energy markets. Federal Energy Regulatory Commission (FERC) Order 704, which was issued in 2007, specifically requires wholesale market participants to report summary information about their sales and purchases on newly created FERC Form No. 552. Similarly, FERC Order 2001 established and clarified requirements related to Electronic Quarterly Reports (EQR) for market participants. Beyond FERC requirements, energy market participants also are confronted with fair market value regulations promulgated in Financial Accounting Standards Board (FASB) 133 and FASB 157, as well as compliance requirements inherent to Sarbanes-Oxley. By any measure, the compliance requirements are rigorous.

While directed toward “reporting” requirements, these new regulations, by their very nature, have intrinsic “process” requirements. Compliance is achieved not only through reporting. The accuracy of the reports, of course, is dependent upon the accuracy of the data, which is dependent upon the processes and systems used to perform that work and capture the information related to it. The final report, while critical to ensure the compliance, is an output function from various inputs. The outputs captured in the reports will be as accurate as the inputs throughout the work processes.

Energy Trading and Risk Management (ETRM) software solutions are being utilized by market participants to help ensure compliance with FERC regulation. Among other things, ETRM solutions help participants ensure adequate controls, process discipline and transparency regarding relevant transactions. Companies that endeavor to ensure compliance with the reporting requirements, as well the spirit of the applicable regulations, find comfort in the proficiency and economy provided by ETRM solutions.

Energy companies operate in a complex, dynamic and ever-changing environment. These complexities are the result of market volatility, changing market participants, dynamic financial markets and, of course, the complexities and volume of the transactions themselves. Data and information regarding individual market transactions are originated from multiple sources with great frequency throughout the course of each day. Capturing that information in a timely manner that is conducive to regulatory reporting can be difficult and overwhelming for market participants, especially for those without the proper tools.

The complexity of this environment, when viewed alongside the expanding regulations associated with it, has left many companies exploring ways to have a real-time, comprehensive and transparent view of all energy transactions. Because FERC Order 704, and resulting Form 552, require that information be captured related to all transactions that contribute to the price index, utilize the price index or could contribute to the price index, it is little surprise that ETRM solutions are gaining in popularity. Without them, the resource commitment and risks associated with erroneous reporting become too great. The regulations also carry a mandate for public utilities to “file Electronic Quarterly Reports (EQR) summarizing the contractual terms and conditions of their agreements for all jurisdictional services...and transaction information for short-term and long-term market-based power sales and cost-based power sales during the most recent calendar quarter.” (FERC Order 2001). In short, the compliance requirement is not insignificant, nor is it easy.

Consider, for example, the time and resource requirements necessary to consolidate data and information from several, and possibly different, systems, across multiple divisions and perhaps even across multiple departments within a division. This concern may be further complicated by the use of spreadsheets as “systems” that currently hold much of this transactional information. On top of the tactical concerns with simply consolidating the data, companies are compelled to take every step possible to ensure that all transactions are captured in a timely and accurate manner that ensures integrity of the data. No easy task, even for the most experienced professionals, especially if existing systems are not up to the task.

FERC has been clear that it is serious about compliance requirements:

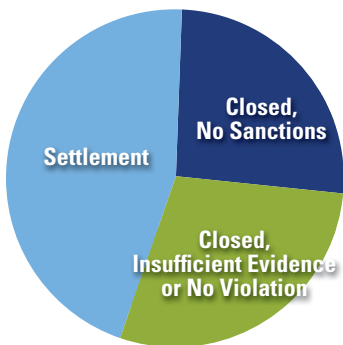
“The central object of the FERC enforcement program is achieving compliance with our regulatory requirements, and it is in the public interest to promote strong compliance programs by regulated companies and others.”

Former FERC Chairman Kelliher
October 16, 2008

Indeed, over the past few years, FERC has been much more visible on the enforcement front than in prior years. On October 31, 2008, the Office of Enforcement provided FERC with its “Report on Enforcement”. Among other things, the Office of Enforcement provided this comparative view of enforcement activity between 2007 and 2008, which demonstrates that in each year more than one-third of all investigations resulted in some settlement activity in each year. *(see graphic on left)*

To date, those settlements have ranged from non-monetary settlements to the whopping \$1.5 billion settlement for the Enron case. More commonly, though, settlements range from several hundred thousand dollars to several million. Those closely aligned with the industry believe that FERC will continue to be active on the regulatory front and that current regulation will be reviewed and adapted as necessary to ensure transparency and fairness related to energy transactions. The enforcement, of course, also will adapt as the regulations and participant compliance requires.

Disposition of Investigations, FY 2007



Disposition of Investigations, FY 2008



Organizations seeking to address these regulatory requirements and overcome the complexities of the processes which underlie them must seek solutions that adequately address:

- Timely gathering and consolidation of data/information
- Data/information integrity and congruity
- Timely and complete promulgation of data/information
- Transparency of processes
- An audit trail that survives close scrutiny

By addressing these items, and the organizational challenges inherent to them, market participants will be able to achieve greater confidence that they are meeting the compliance requirements.

This is no small order. Energy companies have evolved through time and current organizational structures and processes were not designed or implemented with the current regulations in mind. This means that market participants need to adapt their organizations to meet these needs. Doing this manually, or with existing systems, will require them to increase the demands on their employees, adapt their organizational structures and possibly even add a layer of management.

Manually consolidating information from disparate sources is time-consuming, burdensome for employees and expensive. It is also subject to normal human error and innocent mistakes. Compliance requirements, of course, make no formal exceptions for errors inherent to manual processes. Even innocent mistakes can cost a company a significant amount of time and money during the investigative process, even if no fines or penalties are assessed.

Market participants wishing to overcome these challenges and meet the compliance goals of its executives, regulators, employees and investors/owners will be well served to seek solutions that overcome these organizational challenges and the risks associated with manual processes.

Energy Trading Risk Management (ETRM) Solutions

Energy Trading Risk Management (ETRM) software solutions provide an integrated approach to capturing information that exists within a market participant's disparate systems and connect those systems directly to real-time data sources. With this functionality, they are a natural solution for those companies endeavoring to minimize the risks associated with manual processes.

As the regulatory environment continues to evolve, it will be important for market participants to implement an ETRM solution. The solution must not only meet today's needs, but also offer the architecture, design and support to meet future compliance needs.



Enter Allegro's FERC Connect 8.1

Allegro Development Corporation's FERC Connect 8.1 is such a product. It offers market participants an integrated solution to assist with compliance needs resulting from FERC Form 552 and EQR requirements. FERC Connect 8.1 streamlines the extraction and compilation of transactional natural gas and electricity data needed to meet FERC Form 552 and FERC EQR requirements. Once extracted and compiled, the information can be validated and automatically formatted and submitted to FERC. In combination with the Allegro 8 ETRM platform, the solution assists companies in achieving FERC, Sarbanes-Oxley, FASB 133, FASB 157 and IAS 39 compliance with the flexibility to enable market participants to respond to future regulatory requirements.

FERC Connect 8.1 presents an effective solution for energy market participants seeking to streamline regulatory reporting, lower administrative costs associated with compliance efforts and reduce the inherent risks associated with less automated compliance efforts.



About the Author

Energy industry veteran and former utility CIO Bart Thielbar has joined Sierra Energy Group (SEG), a division of Energy Central. SEG provides IT and Smart Grid research, analysis and consulting services to leading electric and natural gas utilities and vendors to the industry.

Thielbar serves as President of Iility Solutions, LLC, which he founded in early 2009. Iility provides executive advisory and consultative services regarding business process optimization and technology investments, including those related to the Smart Grid. Prior to forming Iility Solutions, LLC Thielbar held various executive level positions, including serving as the Sr. Vice-President and CIO of NorthWestern Energy.

Thielbar also is a former chair of the Edison Electric Institute's (EEI) and American Gas Association's (AGA) Technology Advisory Council (TAC). He holds his certified Information Systems Auditor (CISA) designation from the Information Systems Audit and Control Association (ISACA).

About Sierra Energy Group

Sierra Energy Group (SEG) is the research and analysis division of Energy Central, the leading resource connecting professionals in the global power industry to news, events, databases, insight and analysis. SEG provides a variety of off-the-shelf reports, advisory programs and proprietary research solutions to clients who are active along the business and technology interface of the utility industry. The groups practice encompasses three main business areas: Enterprise Solutions, Transmission & Distribution Automation and Business & Workforce Issues.

About Energy Central

Energy Central, headquartered in Aurora, Colorado, and established in 1996, is the leading resource connecting professionals in the global power industry to news, events, databases, insight and analysis. Using web sites, e-newsletters, direct marketing channels, events and print publications, and employment services the company delivers critical business information to top executives, managers, leaders and industry influencers. Energy Central currently publishes EnergyBiz and Intelligent Utility magazines.

About Allegro

Allegro is the global leader in energy trading and risk management (ETRM) solutions for producers, refiners, power and gas utilities, commodity traders and commodity consumers. With more than 24 years of steady growth and deep industry knowledge, our enterprise-wide trading and risk management platform drives transparency and efficiency across front, middle, and back offices, while also managing complex logistics associated with physical commodities. Allegro's proven solutions provide traders, risk managers and management with flexible solutions - across all currencies and commodity types - that allow decision makers to hedge and execute with confidence. Allegro is headquartered in Dallas, Texas, and serves customers worldwide with offices in Calgary, Houston, London, Rotterdam, Singapore and Zurich along with a global network of partners.

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