UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

FEDERAL ENERGY REGULATORY COMMISSION,

Petitioner,

v.

MAXIM POWER CORP., MAXIM POWER (USA), INC., MAXIM POWER (USA) HOLDING COMPANY INC., PAWTUCKET POWER HOLDING COMPANY, LLC, PITTSFIELD GENERATING COMPANY, LP, and KYLE MITTON,

Respondents.

Case No. 3:15-cv-30113-MGM

FEDERAL ENERGY REGULATORY COMMISSION'S
OPPOSITION TO RESPONDENTS' MOTION TO DISMISS

September 25, 2015

INTRODUCTION

After an adversarial proceeding in which its Enforcement staff and Respondents were opposing parties, the Federal Energy Regulatory Commission ("Commission") issued a 65-page Order on May 1, 2015, finding that Maxim Power Corp. and its subsidiaries,[1] along with Maxim employee Kyle Mitton (collectively "Maxim" or "Respondents"), executed a scheme in 2010 to extract nearly $3 million in inflated payments from the New England energy marketplace, and ultimately from consumers and businesses throughout this region. The Commission brings this action to affirm its Order and to enforce the civil penalties it there assessed against Respondents.

The key facts are straightforward: on a string of hot days in July and August 2010, when Maxim knew its power plant in Pittsfield was needed to ensure the reliability of the New England grid, and was subject to rules limiting it to 110% of its costs, Maxim sought to charge the regional energy marketplace at high oil prices when its plant actually burned much less expensive natural gas. As part of this scheme, Maxim sent a series of artfully-crafted emails designed—through implied misrepresentations and material omissions—to try to ensure that the New England market's watchdog (the "Market Monitor") would not discover that Maxim had burned natural gas, not fuel oil, and that on many days Maxim had actually purchased natural gas *before* offering Pittsfield on high oil prices.

Although the Market Monitor later uncovered and reversed Maxim's scheme, the Commission's Enforcement staff investigated to evaluate whether Maxim had violated energy laws and regulations. Throughout the investigative process, Maxim submitted voluminous filings to Enforcement defending its conduct. Pet. ¶¶ 56, 57.

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[1] Per the footnote on the cover page of Respondents' brief, the first named Respondent is now identified as "Maxim Power Corp." (vs. "Corporation") and the fourth named Respondent is now identified as "Pawtucket Power Company, LLC" (*i.e.*, "Company" vs. "Co.").

Enforcement concluded that Maxim had broken the law and prepared a Staff Report setting forth its findings. The Commission initiated an adversarial proceeding, with Enforcement and Maxim as opposing parties, to determine whether to impose a civil penalty on the Maxim companies and Mitton. In responding to the Staff Report, Maxim had the opportunity, without page limits, to present any evidence or arguments it chose, including declarations from Mitton or other Maxim employees to supplement their sworn testimony.

On March 4, 2015, Maxim submitted a 57-page Response and Mitton filed a separate 28-page Response, each attaching more than 280 pages of exhibits. Enforcement filed a Reply on March 23, 2015. On April 6, 2015, Maxim made an additional 39-page submission, followed by still another filing on April 14, 2015.[2]

The Commission's Order Assessing Civil Penalties ("Order" or "Penalty Assessment Order"), issued May 1, 2015, carefully examined the record evidence,[3] assessed the arguments made by Maxim in its voluminous submissions, and determined that (a) Maxim and Mitton violated the Commission's Anti-Manipulation Rule, 18 C.F.R. § 1c.2 (2014), and that (b) Maxim violated a separate rule requiring firms granted certain market privileges by the Commission to be candid, and not omit material information, in communications with Market Monitors, 18

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2 The public version of the filings by both Enforcement and Maxim in the adversarial proceeding before the agency, along with the Commission's Orders, are available on the Commission's web site at http://elibrary.ferc.gov/idmws/docket_search.asp (under Docket No. IN15-4). For the Court's convenience, the portions of the Response of Maxim Power Corp. to Order to Show Cause (March 4, 2015) ("Maxim Show Cause Response") discussed in this brief are reproduced in Appendix A.

3 As the docket sheet for the FERC proceeding shows, the Commission had not only the opposing parties' lengthy filings but also the underlying factual materials, which Enforcement filed at the outset of the proceeding. Although most of these materials came from Maxim, Enforcement provided Maxim with the same materials it filed with the Commission.

C.F.R. § 35.41(b) (2014).[4] Consistent with its guidelines for civil penalties, the Commission ordered the corporate Respondents to pay $5 million in civil penalties and Mitton to pay $50,000. The Commission stated that it would have imposed the same penalties even if Respondents had violated only section 35.41(b), rather than both provisions. Order at P 121.

On July 1, 2015, pursuant to the procedures set forth in the Federal Power Act ("FPA"), Pet. ¶¶ 11-12, 20-21, the Commission filed a Petition in this Court to affirm the agency's Penalty Assessment Order. On September 4, 2015, Maxim filed a motion to dismiss.

Respondents' principal argument in their Memorandum of Law ("Mem.") is that the Commission has not properly alleged that they made misrepresentations or material omissions in their communications with the Market Monitor. That argument fails: it is based on (i) an incorrect description of the law of misrepresentations and (ii) a straw-man mischaracterization of the Commission's claims about material omissions.

As to misrepresentations, Respondents contend they can escape liability because, they claim, they did not make a literally false statement (such as "we are burning oil, not gas, today"). But even if that factual claim were true (and it is not), Respondents are wrong about the law: in a series of controlling decisions that Maxim does not mention, the First Circuit (and this Court in a June 2015 decision) have held that "*literally accurate [statements], can become, through their context and manner of presentation, devices which mislead* . . . ."[5]

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[4] Chairman Bay did not participate in the Order. Among the Commissioners participating, the vote was 3-1 in support of the Order.

[5] *Massachusetts Mut. Life Ins. Co. v. DB Structured Products, Inc.*, Civ. No. 11-30039-MGM, 2015 WL 3964560, at *10 (D. Mass. June 19, 2015) (emphasis added) (quoting *Lucia v. Prospect Street Income Portfolio, Inc.*, 36 F.3d 170, 175 (1st Cir. 1994) (quoting *McMahan v. Wherehouse Entertainment, Inc.*, 900 F.2d 576, 579 (2d Cir. 1990))).

As to omissions, Respondents purport to rebut a contention that the Commission has not made: that independent of any other communication, Maxim had a free-standing obligation to alert the Market Monitor that it was burning gas while offering on high oil prices. But the Commission's point, as made clear in the Petition and the Commission's Order, is different: when Maxim *did* communicate about oil-gas issues, it had a duty not to omit material information needed to make Maxim's statements not misleading. Under the Commission's Anti-Manipulation Rule,[6] and under settled law,[7] material omissions of this type are actionable.

The Commission's Order also found that Maxim violated a separate Commission rule, 18 C.F.R. § 35.41(b), requiring firms granted certain market privileges, such as Maxim's Pittsfield Generating Company, LP ("Pittsfield Generating Co."), to be truthful, and not to omit material information, in their communications with Market Monitors. Because of the critical importance of candor in communications with Market Monitors, this provision has no scienter requirement. *Kourouma v. FERC*, 723 F.3d 274, 278 (D.C. Cir. 2013) ("even negligent misrepresentations may be actionable" under section 35.41(b)). For the same reasons discussed above, the Petition's allegations about misrepresentations and omissions fully comply with pleading standards in this context as well.

Maxim also advances a "materiality" defense (Mem. at 3 & 23-24), arguing, in effect, that its deceptive July 2010 communications with the Market Monitor are excused because the

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6 The Commission's Anti-Manipulation Rule makes it unlawful "to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 18 C.F.R. § 1c.2(a)(2). Maxim acknowledges that the Commission has asserted a claim under this provision. Mem. at 21.

7 *E.g.*, *V.S.H. Realty, Inc. v. Texaco, Inc.*, 757 F.2d 411, 414-15 (1st Cir. 1985) ("'[f]ragmentary information may be as misleading . . . as active misrepresentation, and half-truths may be as actionable as whole lies . . . .'"), quoting *Kannavos v. Annino*, 356 Mass. 42, 48, 247 N.E.2d 708 (1969). *See* pp. 14-15 *infr*a.

deception was later exposed ("the allegedly concealed information was [later] disclosed to ISO-NE") and the public ultimately was not harmed. For many reasons, that contention is incorrect. *First*, unlike in the private securities cases that Maxim cites, neither reliance nor damages is an element of either of the Commission's claims. *See infra* at pp. 23-24. *Second*, attempted market manipulation is as actionable as successful manipulation; that a scheme was ultimately foiled is no defense. *See infra* at p. 24. *Third*, although in the end its efforts were unsuccessful, Maxim's intent in sending its carefully-crafted emails was to *prevent* the Market Monitor from discovering the facts. And for many weeks, Maxim believed its plan had succeeded. In a call with the Market Monitor on August 18, 2010, for example, Mitton said he had expected that, because he had mentioned "'potent[i]al' gas procurement" issues in his emails, "*no further review would be done by [the Market Monitor]*." Pet. ¶ 46 (emphasis added).

Finally, giving market participants a free pass if their deception is later exposed would defeat the purpose of both the Anti-Manipulation Rule and section 35.41(b): market participants could mislead Market Monitors with impunity, knowing they (a) would profit if the deception was not caught and (b) at worst, would give up their unjust profits, but suffer no penalty, if their deception was exposed. *See* Order at P 122, pp. 24-25 *infra*.[8]

As demonstrated below, Maxim's other defenses are equally without merit.

[8] Because this Opposition concerns Maxim's motion to dismiss, we do not here address the question of what procedures this Court should follow in this case under the applicable provisions of the Federal Power Act (quoted in PP 11 & 22 of the Petition) following resolution of the present motion. As stated in the Petition, however, the Commission submits that "this Court can and should affirm the penalty assessments without modification following a review of the Commission's Order Assessing Civil Penalties and the materials presented to the Commission during the penalty assessment process." Pet. ¶ 76. The Commission will be happy to brief this procedural issue at the appropriate time.

STANDARD OF REVIEW

In evaluating a motion to dismiss under Rule 12(b)(6), "[t]he sole inquiry . . . is whether, construing the well-pleaded facts of the complaint in the light most favorable to the plaintiffs, the complaint states a claim for which relief can be granted." *Ocasio–Hernández v. Luis Fortuño–Burset,* 640 F.3d 1, 7 (1st Cir. 2011). While legal conclusions and factual allegations that simply parrot legal standards are not entitled to a presumption of correctness, *id.* at 10, 12, the reviewing court is required to "accept the remaining factual allegations of the complaint as true and evaluate whether, taken as a whole, they state a facially plausible legal claim." *Id.* at 10-11. In doing so, the court must "draw[] all reasonable inferences in the plaintiff's favor." *Maloy v. Ballori-Lage*, 744 F.3d 250, 252 (1st Cir. 2014) (citations omitted).

Critically, a motion to dismiss is not evaluated based on the *moving party's* (here, Maxim's) version of the facts. Nevertheless, Respondents ask the Court to accept as true not the factual allegations of the Petition, as the law requires, but Respondents' own version of the facts. For example, Respondents repeatedly invite the Court to accept as true – and as the whole truth – statements in their carefully-worded emails to the Market Monitor about supposed "legitimate economic reasons" for offering on high oil prices.[9] While these claims about Maxim's motivations would not help Maxim even if true – because they would not

[9] Mem. at 1 ("offer[ing] conservatively on oil because of gas pipeline restrictions"); *id.* at 2 ("offers [were] based on the price of oil to minimize its financial exposure"); *id.* at 22 (same); *see id.* at 2 (oil offers "based on legitimate economic concerns"); *id.* at 8 ("These restriction notices informed Maxim's ongoing concerns about its ability to secure . . . natural gas . . . . To minimize the risk of suffering significant financial losses . . . Maxim made day-ahead offers based on the price of oil"); *id.* at 23 (oil offers "based on legitimate economic concerns").

As discussed below, none of Maxim's emails to the Market Monitor mentions that Maxim was burning nearly 100% gas and virtually no oil; that it expected to enjoy profits of more than $100,000 per day if it could charge for oil while burning gas; or that Maxim often bought substantial quantities of gas before offering on costly oil. *See* pp. 17-23 *infra*.

excuse Maxim's misrepresentations and omissions to conceal (among other things) that Maxim was burning gas and not oil – the Court should not accept them for purposes of this motion.[10]

Fed. R. Civ. P. 9(b) provides that "[a] party must state with particularity the circumstances constituting fraud or mistake." Because this is a petition to affirm an agency Order following an adversarial proceeding, rather than a civil fraud complaint, Rule 9(b) does not apply. But even if it did, the Petition far exceeds the specificity requirements of Rule 9(b).

THE COMMISSION'S ANTI-MANIPULATION RULE

In the wake of abusive market conduct by Enron in wholesale energy markets in the early 2000's, in 2005 Congress gave the Commission explicit anti-manipulation authority. Pet. ¶ 23. Reflecting the importance of deterring and penalizing improper market conduct, Congress authorized the Commission to assess penalties of up to $1 million per day, per violation, against entities that engage in market manipulation or violate other Commission rules. *Id.* ¶ 25.

The Commission implemented this statute in 2006 by promulgating section 1c.2 of its regulations, 18 C.F.R. § 1c.2. Though patterned on SEC Rule 10b-5, the Commission "adapt[s] analogous securities precedents as appropriate to specific facts, circumstances, and situations that arise in the energy industry." *Prohibition of Energy Market Manipulation*, Order No. 670, 114 FERC ¶ 61,047, at P 30, *reh'g denied*, 114 FERC ¶ 61,300 (2006) ("Order No. 670").

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[10] Maxim also claims (at 1) that "FERC . . . admits that [Pittsfield's gas burns] were disclosed to [the Market Monitor] before any purported windfall payment was made to Maxim" (citing Petition, Penalty Assessment Order, and Show Cause Order); *see id.* at 3 ("FERC concedes that Maxim provided the fuel burn data to [the Market Monitor] *before* ISO-NE made any purported windfall payment to Maxim") (emphasis in original). That claim is untrue: the materials cited by Maxim simply say that excess payments to the Pittsfield plant were later mitigated. *E.g.*, Penalty Assessment Order at P 33 (Market Monitor notified Maxim in the fall of 2010 that it would be mitigated for July and August, and as a result Maxim's payments "were reduced by $2.99 million through this mitigation process").

As the Commission explained in its Order in this case, "a finding of manipulation does not require a violation of a tariff . . . ." Order at P 64. Consistent with settled law, the Commission noted that "fraud is a very fact-specific violation, the permutations of which are limited only by the imagination of the perpetrator. Therefore, no list of prohibited activities could be all-inclusive." *Id.* P 64 n.141 (citing authorities).

FACTUAL BACKGROUND

In Massachusetts, and throughout New England, households, businesses, and government agencies buy their electricity from utilities like National Grid. Utilities, in turn, buy electricity in the wholesale market, and pass their costs along to their retail customers. Because electricity bills affect everyone, and because a reliable supply of electricity is vital to the entire economy, Congress has, through the Federal Power Act, directed the Commission to ensure both that wholesale electricity rates are "just and reasonable" and that the wholesale grid operates reliably. Pet. ¶ 2; Order at P 67; 16 U.S.C. §§ 824d(a), 824o.

In this region, both the wholesale electricity market and the wholesale grid itself are operated by a Commission-regulated entity called ISO-New England, Inc. ("ISO-NE" or "the ISO"), based in Holyoke, Massachusetts. Each day, ISO-NE conducts auctions in which the price of electricity is set by market forces: the interaction of supply (from coal- or gas-fired power plants, wind and solar facilities, hydroelectric dams, and nuclear plants) and demand (principally utilities). These auctions include both "Day-Ahead" (one day before delivery) and "Real-Time" (day of delivery) markets for energy. Pet. ¶¶ 2-3, 33-34.

Most wholesale electricity bought and sold in New England is settled at market prices set through these daily auctions. But because of the paramount importance of ensuring that power stays on without interruption, ISO-NE sometimes – for engineering reasons – needs to procure

electricity outside its auctions. In particular, the ISO sometimes needs a specific generator to operate to ensure the reliable operation of the regional grid, even if the generator's offer prices are above – even far above – market rates. Pet. ¶¶ 3-4, 33.

A generator needed for reliable grid operation has what economists call "market power"; that is, because of lack of competition, the plant could extract extremely high prices from the ISO if not constrained. Consistent with the FPA's policy of ensuring that electricity prices are just and reasonable, ISO-NE has a rule limiting generators needed for reliability to just above (*i.e.*, 110% of) their estimated fuel and other variable costs. Pet. ¶¶ 5, 33, 35.[11]

The facts giving rise to this case are simple: during a string of days of very hot weather in New England in July and August 2010, a power plant in Pittsfield, Massachusetts, owned and operated by respondent Maxim Power Corp. (through various subsidiaries), was needed by ISO-NE to operate to ensure the reliability of the New England wholesale grid. The Pittsfield plant can burn either natural gas or fuel oil, although fuel oil is virtually always much more costly. Across many days during this hot spell, Maxim submitted Day Ahead offers to the ISO at high oil prices (averaging around $175/MWh) but then burned natural gas (at prices averaging around $75/MWh)).[12] On many days, Maxim bought substantial quantities of natural gas before submitting Day Ahead offers at costly fuel oil prices. Pet. ¶¶ 8, 37-39. Maxim's advance gas purchases reflected its confidence that it would be called on for reliability on hot days, Pet. ¶ 37,

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[11] Through a separate process, not at issue here, the ISO compensates generators for being available to provide energy, separate from payments for actually producing energy on particular days. ISO-NE, *Introduction to New England's Forward Capacity Market* (2014), available at http://www.iso-ne.com/static-assets/documents/2014/08/iso101-t4-mkt-fcm.pdf.

[12] In wholesale electricity transactions, the applicable unit is megawatt-hours (MWh's), as opposed to the kilowatt-hours (KWh's) that consumers see on their electric bills.

since buying gas in advance was contrary to Maxim's normal practice of waiting to buy gas until after getting Day Ahead awards. Order at P 86.[13]

In mid-July 2010, ISO-NE's Market Monitor watchdog unit, which is responsible (among other things) for preventing overpayments to units needed for reliability, saw that Maxim was offering Pittsfield at very high prices, and contacted Maxim to learn why. Through its employee Kyle Mitton, Maxim sent a series of hide-the-ball emails saying that it was offering on oil because of "pipeline restrictions," which Mitton claimed were causing "bottlenecks" that were a "serious issue." By stressing these supposed pipeline problems, Maxim falsely implied that these problems were affecting *its own* ability to acquire gas to operate Pittsfield – which is the only reason these alleged problems would be relevant in this context. Pet. ¶¶ 40-45.

In writing these misleading emails, Maxim and Mitton knew that if the Market Monitor did not discover that Maxim was actually burning gas at Pittsfield, Maxim would enjoy windfall profits – averaging more than $100,000 per day[14] – by being paid for costly oil while actually burning gas during times it was being dispatched for reliability. To maximize its chances of keeping that windfall, Maxim omitted numerous facts needed to make its affirmative statements not misleading. While repeatedly telling the Market Monitor about a supposed pipeline crisis, for example, Maxim did not disclose that claimed pipeline problems were having no (or virtually no) effect on Maxim itself. Maxim did not disclose that while expecting to be paid based on high oil prices on previous days, it had burned no (or virtually no) oil. And most strikingly, Maxim did not mention that before submitting offers at high oil prices, supposedly because of

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[13] By waiting to acquire gas until it was sure it would need it, Maxim avoided the risk of "incur[ring] a potentially significant loss" if Pittsfield was not dispatched and had to sell unneeded gas, potentially at a loss. Order at P 86.

[14] Across 22 days, Maxim's unjust gains of $2.99 million amount to an average overpayment of about $136,000 per day.

gas pipeline problems, it often had already bought large quantities of natural gas to use if (as Maxim expected on hot days) it was dispatched for reliability. Pet. ¶¶ 40, 48.

Maxim believed that by managing what it said in its emails, it could deter the Market Monitor from looking into what fuel Pittsfield had burned (and thus from taking away Maxim's windfall). In a call with the Market Monitor on August 18, 2010, for example, Mitton admitted that because he had mentioned "'potent[i]al' gas procurement [problems]" in his emails, he expected that "no further review would be done by [the Market Monitor]." Pet. ¶ 46.

ARGUMENT

I. RULE 9(b) DOES NOT APPLY HERE, BUT IN ANY EVENT, THE PETITION FAR EXCEEDS THE SPECIFICITY REQUIREMENTS OF THAT RULE

Rule 9(b) does not apply here, because rather than filing a civil fraud complaint, the Commission's Petition seeks judicial affirmance of an administrative penalty order resulting from an adversarial proceeding. But if the Rule were applicable, it is difficult to imagine a case in which a party accused of fraud has been more fully informed of the details of the case against them. The Petition identifies (and quotes) each of Respondents' misleading communications and material omissions; explains why the statements and omissions were misleading; and provides detailed factual allegations showing that Respondents knew all of the relevant facts (*e.g.*, about gas purchases and burns) and sought to mislead the Market Monitor about them to make windfall profits. Pet. ¶¶ 7-9, 37, 39-51, 63. And the Petition is based on and seeks to enforce a Commission Order (filed with the Petition as Exhibit 1) that sets forth in even greater detail the facts about Respondent's misleading statements, material omissions, and scienter. Order at PP 25-33, 49-62, 83-97. The Commission has fully informed Respondents about the legal and factual bases for the agency's determination that Maxim and Mitton violated the Anti-Manipulation Rule and that Maxim violated section 35.41(b).

II. THE PETITION PROPERLY PLEADS THAT MAXIM AND MITTON VIOLATED THE COMMISSION'S ANTI-MANIPULATION RULE

The Commission's Anti-Manipulation Rule reads in relevant part as follows:

1c.2 Prohibition of electric energy market manipulation.

(a) It shall be unlawful for any entity, directly or indirectly, in connection with the purchase or sale of electric energy or the purchase or sale of transmission services subject to the jurisdiction of the Commission,

(1) To use or employ any device, scheme, or artifice to defraud,

(2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) To engage in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity.

As elaborated by the Commission in its Order promulgating the Rule, section 1c.2 prohibits an entity from (1) (a) using a fraudulent device, scheme, or artifice, or (b) making a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule, or regulation, or (c) engaging in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite scienter; (3) in connection with the purchase or sale of electricity subject to the jurisdiction of the Commission. Order No. 670 at P 49.

Respondents do not dispute the third element of a Rule 1c.2 violation – jurisdiction – but contend that they (a) did not engage in any of the three types of wrongdoing listed in section 1c.2, and (b) lacked scienter. These contentions lack merit: the Petition properly pleads that Respondents violated each of the three subsections of Rule 1c and had the requisite scienter.

A. <u>The Petition Properly Pleads that Maxim and Mitton Made Material Misrepresentations and Omissions in Their Communications with the Market Monitor</u>

Maxim focuses most of its Memorandum on the second category of wrongdoing under the Anti-Manipulation Rule, concerning misrepresentations and material omissions, 18 C.F.R. § 1c.2(a)(2). As the Commission explained in Order No. 670, this prong of the Rule makes it unlawful to "mak[e] a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule, or regulation, . . ." Order No. 670at P 49. Here, Maxim had a "duty to speak" because it was required by a separate rule, 18 C.F.R. § 35.41(b), not to omit material information in communications with Market Monitors. Pet. ¶ 73; Order at P 43 n.91, P 52 n.111; *see* pp. 16-17 *infra*.

Respondents contend (at 17) they cannot be held liable under this prong of Rule 1c because, they claim, the Petition does not allege that they "expressly misrepresented any facts." Respondents also contend (at 17-20) they cannot be held liable for omitting the facts identified in the Petition, *e.g.*, that (a) their plant was burning gas, not oil, even while offering on oil, and (b) Maxim often purchased large quantities of gas before submitting oil offers. Pet. ¶¶ 40, 48.

Respondents are mistaken on both counts.

1. <u>Under Settled Law, Even Literally Accurate Statements Can Qualify As Misrepresentations</u>

Based on a few words in a single case, *Baron v. Smith*, 285 F. Supp. 2d 96, 101 (D. Mass. 2003), *aff'd*, 380 F.3d 49 (1st Cir. 2004), Respondents contend (at 17) the Commission cannot make out a claim for misrepresentation because the Petition does not allege that they "expressly misrepresent[ed] any facts," *i.e.*, that they made literally false statements. But both *Baron* and controlling First Circuit authority show that a misrepresentation claim can be based on statements that are literally accurate but that mislead through context.

As this Court observed (in a June 2015 decision not mentioned by Respondents), "[s]ome statements, *although literally accurate, can become, through their context and manner of presentation, devices which mislead . . . .*"[15] For that reason, "the misrepresentation requirement 'is measured not by literal truth, but by the ability of the material to accurately inform rather than mislead prospective buyers.'"[16] In its decision, this Court quoted the leading case in this Circuit, *Lucia v. Prospect Street Income Portfolio*, *Inc.*, 36 F.3d 170, 175 (1st Cir. 1994). Strikingly, the lone case that Respondents cite in support of their position (*Baron v. Smith*), in a passage not mentioned by Respondents (285 F. Supp. 2d at 102), cites *Lucia* for the same point. Other courts in this District routinely apply this same principle.[17]

2. Under Settled Law, Omissions Are Actionable If The Omitted Facts Were Necessary To Make Other Statements Not Misleading

In its attack on the Commission's finding that they omitted material information, Respondents argue that they did not have a free-standing obligation to disclose they were burning gas when they offered on oil prices during reliability dispatches. Mem. at 1, 3, 12, 18, 25, 27-28.

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15 *Massachusetts Mut. Life Ins. Co. v. DB Structured Products, Inc.*, Civ. No. 11-30039-MGM, 2015 WL 3964560, at *10 (D. Mass. June 19, 2015) (emphasis added) (quoting *Lucia v. Prospect Street Income Portfolio, Inc.*, 36 F.3d 170, 175 (1st Cir. 1994) (quoting *McMahan v. Wherehouse Entertainment, Inc.*, 900 F.2d 576, 579 (2d Cir.1990))). As the First Circuit explained, "'emphasis and gloss can, in the right circumstances, create liability.'" *Lucia*, 36 F.3d at 175-76 (citations omitted). *Cf.* Restatement (Second) of Contracts § 159, Ch. 7, Comment a. (1981) ("A misrepresentation, being a false assertion of fact, commonly takes the form of spoken or written words. *Whether a statement is false depends on the meaning of the words in all the circumstances, including what may fairly be inferred from them*.") (emphasis added).

16 *DB Structured Products*, *supra*, at *10 (quoting *Lucia*, 36 F.3d at 175 (quoting *McMahan*, 900 F.2d at 579)).

17 *E.g.*, *Brumbaugh v. Wave Sys. Corp.*, 416 F. Supp. 2d 239, 249 n.10 (D. Mass. 2006) (citing *Lucia*); *see In re Sepracor, Inc. Securities Litigation*, 308 F. Supp. 2d 20, 34 (D. Mass. 2004) (liability under the securities laws can be based on "implicit factual assertions").

Respondents' argument misses the point. One way in which a communication can be deceptive – and the type of wrongful communication at issue here – is if it omits facts necessary to prevent the statements made from communicating an untrue message.[18] The Commission's Anti-Manipulation Rule specifically recognizes this form of deception: the second prong of that Rule makes it unlawful "[t]o make any untrue statement of a material fact *or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading*." 18 C.F.R. § 1c.2(a)(2) (emphasis added). Similar language is commonplace in many statutes and rules.[19]

This form of deceptive communication is sometimes called a "half-truth." Courts have long held that a half-truth can be misleading and amount to a misrepresentation. *E.g.*, *Equitable Life Ins. Co. of Iowa v. Halsey, Stuart & Co.*, 312 U.S. 410, 426 (1941) (under common law of fraud, "a statement of a half truth is as much a misrepresentation as if the facts stated were untrue"); *V.S.H. Realty, Inc. v. Texaco, Inc.*, 757 F.2d 411, 414-15 (1st Cir. 1985) (under common law of misrepresentation, "'[f]ragmentary information may be as misleading . . . as active misrepresentation, and half-truths may be as actionable as whole lies . . . .'") (citations omitted).[20] The Petition properly alleges that Respondents engaged in this form of deception.

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[18] That the ISO later (in 2012) adopted a free-standing requirement for generators to disclose what fuel they were burning (Mem. at 18) is likewise irrelevant.

[19] SEC Rule 10b-5, for example, forbids, among other things, the omission of any material fact "necessary in order to make the statements made ... not misleading." 17 C.F.R. § 240.10b–5 (2015). The Massachusetts Uniform Securities Act ("MUSA") has a similar provision. Mass. Gen. Laws ch. 110A, § 410(a)(2) (1991).

[20] Other authorities to the same effect include *United States v. Carpenter*, No. 04-10029-GAO, 2014 WL 691659, at *5 (D. Mass. Feb. 21, 2014) (under mail and wire fraud statutes, "[t]he affirmative representations that the funds were deposited in accounts maintained at Merrill Lynch and later Paine Webber were true as far as they went, but *what they omitted made them misleading*") (emphasis added), *aff'd*, 781 F.3d 599 (1st Cir. 2015); *AT&T Corp. v. Stockard*, No. 03-cv-11377-RCL, 2006 WL 6491253, at *12 (D. Mass. June 28, 2006) ("Irrespective of

3. Maxim Was Barred Not Only From Making Affirmative Misrepresentations But Also From Omitting Material Information In Its Communications With The Market Monitor

Under Commission rules, if an entity wishes to conduct wholesale energy transactions at market rates, rather than at rates set by a tariff, it must obtain market-based rate authority from the Commission. Firms granted that privilege (called "Sellers") are required to comply with special Market Behavior Rules, codified at 18 C.F.R. § 35.41. One of these Rules requires Sellers not only to "provide accurate and factual information and not submit false or misleading information,'but also to refrain from "*omit[ting] material information*, in any communication with . . . Commission-approved market monitors . . . unless Seller exercises due diligence to prevent such occurrences." 18 C.F.R. § 35.41(b) (emphasis added).

During the summer of 2010, one of the Maxim entities, Respondent Pittsfield Generating Co., had market-based rate authority from the Commission, Pet. ¶ 73, and was therefore a "Seller" subject to the Market Behavior Rules. Maxim was thus barred from omitting material information in any communication with the Market Monitor, unless the omission occurred despite exercise of due diligence. 18 C.F.R. § 35.41(b).

Maxim does not dispute that its Pittsfield Generating Co. unit was a "Seller" required to comply with this rule, and was therefore obliged not to omit material information in communications with the Market Monitor. Mem. at 16 ("FERC Regulation 35.41(b) proscribes misstatements and omissions of material fact by a seller of electricity to market monitors.").

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whether Defendants had any initial duty to disclose this information, once Defendants opted to discuss these subjects, they had a duty to do so truthfully . . . [and] to make sure that their statements on these topics were not 'half-truths,' *i.e.* 'misleading by a significant omission.'"); *SEC v. Druffner*, 353 F. Supp. 2d 141, 148 (D. Mass. 2005) ("the securities laws give rise to a duty to disclose any information necessary to make an individual's voluntary statements not misleading") (citing Rule 10b–5(b)).

Under the Commission's Anti-Manipulation Rule, as interpreted by the Commission in Order No. 670, omissions of material fact are actionable if the omission is one "as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule or regulation."[21] Because its Pittsfield unit was required (by section 35.41(b)) not to omit material information in communication with the Market Monitor, for purposes of section 1c.2, Maxim had a "duty to speak under a . . . Commission rule" when it communicated with the Market Monitor. Pet. ¶ 73; Order at P 43 n.91, P 52 n.111.

4. **The Petition Properly Pleads That, In The Context Of Their Communications With The Market Monitor, Respondents Made Both Misrepresentations And Material Omissions**

As just discussed, under settled law, both literally accurate statements and material omissions can provide a basis for liability under the Commission's Anti-Manipulation Rule. Both the Petition and the Order quote Maxim's and Mitton's relevant statements and explain why they are misleading and omit material information. Pet. ¶¶ 9, 40-50.

Citing several cases, Respondents claim their statements to the Market Monitor (from July 16 through July 21) were appropriate based on "the question asked" by the Market Monitor in an initial voicemail on July 15, which (according to Mitton's email the next day) was about Maxim's offer prices.[22] But as the First Circuit's decision in *Lucia* makes clear, what is relevant in evaluating whether Maxim's statements were deceptive is not any single circumstance in isolation, but the *entire* "context and manner of presentation" of Maxim's back-and-forth with

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[21] Order No. 670 at P 49.

[22] Mem. at 18-19 (citing *Boston Sci. Corp. Sec. Litig*., 686 F.3d 21, 28 (1st Cir. 2012); *In re Ubiquiti Networks, Inc. Sec. Litig*., 33 F. Supp. 3d 1107, 1132-33 (N.D. Cal. 2014); *City of Omaha Police & Fire Ret. Sys. v. Timberland Co*., No. 11-cv-277- SM, 2013 WL 1314426, at *16-17 (D.N.H. Mar. 28, 2013); *Foley v. Transocean Ltd*., 861 F. Supp. 2d 197, 218-19 (S.D.N.Y. 2012)).

the Market Monitor. *Lucia*, 36 F.3d at 175. Similarly, in evaluating whether information omitted by Respondent was material, it is the overall context of Respondent's interactions with the Market Monitor over several days, and not simply the words used in an initial voicemail, that matters. The remainder of this section describes the most significant aspects of the context that made Maxim's communications deceptive.

Because of the very large ($100/MWh) price difference between oil and gas, Maxim knew it would enjoy large profits if it offered Pittsfield on oil prices and burned gas, so long as the Market Monitor did not realize that Pittsfield had burned gas. Pet. ¶¶ 38-39. But Maxim also knew that if the Market Monitor learned that Maxim was actually burning gas, it would reduce Maxim's payments to the much lower price of that fuel. *Id.* ¶ 40. This knowledge shaped Maxim's communications with the Market Monitor during this period. *Id.*

On July 15, 2010, the Market Monitor left a voicemail for Mitton asking about Maxim's offer prices for Pittsfield. Mitton emailed the next day, saying: "We have been offering the unit in conservatively on fuel oil due to the daily gas restrictions on Tennessee Gas Pipeline. I can provide you the restriction notices for your records if you like . . . ." By claiming that "gas restrictions" were the reason for Maxim's oil offers, Mitton falsely implied that the restrictions had affected *Pittsfield's* ability to obtain gas. In fact, as Mitton knew, Maxim had successfully acquired all of the gas it needed to meet the previous nine days of reliability dispatches, and had burned no oil whatsoever. And for every operating day from July 7 to July 16, Maxim bought gas hours before it learned whether it had received a Day Ahead award, and on several days did so before offering on oil prices. Mitton's July 16 email omitted these material facts. Pet. ¶ 41.

Over the next week, Mitton exchanged a series of additional emails with the Market Monitor. On July 19, for example, Mitton sent the Market Monitor a document showing recent

pipeline restriction notices, saying "there have been restrictions [on the Tennessee Gas Pipeline] every day of the month so far in July." Mitton told the Market Monitor official that the pipeline was facing "*bottlenecks*" that were "*reducing the amount of [natural] gas that can flow*," and that "[d]uring normal heat this wouldn't be an issue however with the prolonged heat wave in the Northeast restrictions have been *a serious issue*." Pet. ¶ 42 (emphasis added).

Since Mitton was providing this information about pipeline problems in connection with *Maxim's own behavior*, his email about "serious" pipeline "bottlenecks" that were "reducing the amount of gas that can flow" implied that these alleged "serious issues" were having a significant impact *on Maxim*. Pet. ¶ 43. That implied representation was untrue. For every operating day between July 7 and July 22, Maxim not only obtained natural gas to satisfy nearly all of Pittsfield's Day Ahead awards, but purchased natural gas hours before the ISO announced generator selections, and often before Maxim submitted Day Ahead offers at noon. In his July 19 email, Mitton again did not disclose any of these material facts. *Id.*

On July 20, 2010, the Market Monitor sent an email to Mitton asking to be advised when Pittsfield "ha[s] a fuel issue . . . so we [the Market Monitor] *can model the unit on the correct fuel*." Pet. ¶ 43 (emphasis added). As Maxim admits, for a generator needed for reliability, like Pittsfield, the correct fuel for purposes of determining how much the unit should be paid was the "fuel actually burned." Mem. at 8 ("Under the public and FERC-approved ISO-NE Tariff, Maxim's compensation would be reduced or 'mitigated' based on the mix of fuel actually burned.").

That same day (July 20), Mitton responded, "we are in on fuel oil again tomorrow [i.e., July 21, 2010]," *id.*, misleadingly implying (again) that Maxim was having problems acquiring natural gas, would therefore be burning fuel oil, and should be modeled (and paid) at fuel oil

prices. Pet. ¶ 43. In fact, before submitting its Day-Ahead offer based on burning fuel oil, Maxim had already purchased nearly 11 hours' worth of natural gas for Pittsfield for the next day, July 21, 2010.[23] Again, Maxim did not disclose either that it had been burning nearly 100% gas or that it bought gas in advance for July 21 itself. *Id.* As with every day when Maxim bought gas before offering on oil, Maxim was assured of windfall profits for the next day as a whole if, as expected, the ISO dispatched Pittsfield for reliability.[24]

Mitton sent another misleading email on July 21, 2010. In that email, Mitton stated that "Altresco [i.e., Pittsfield] is on fuel oil pricing again for 7/22 due to gas restrictions again," and attached a summary of pipeline restrictions. Through his statements, Mitton (for Maxim) again falsely implied that Pittsfield itself was having problems obtaining natural gas and was therefore burning fuel oil. Pet. ¶ 44. In fact, Maxim had already purchased natural gas for operating date July 22 before submitting its Day Ahead offer. *Id.*[25]

As the email exchange on July 20 shows, Mitton knew that the Market Monitor was using his statements about oil to "model" Pittsfield on oil. And other documents show that Maxim hoped and expected that the Market Monitor would never check on what fuel Maxim had burned.

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[23] Maxim Show Cause Response at 30 (reproduced in Appendix A hereto).

[24] For dispatches up to 11 hours on July 21, for example, Maxim would enjoy profits of $100/MWh (the difference between oil and gas prices). If dispatched for longer, Maxim would, at worst (in the unlikely event it could not acquire more gas) be paid 110% of its estimated costs for oil. For the day as a whole, therefore, Maxim knew it would recover far more than its costs if, as expected, Pittsfield was dispatched for reliability.

[25] Again improperly inviting the Court to rely on its factual contentions, and not on the Petition (and Order), Maxim tries to explain away its advance gas purchases as supposedly "dictated" by the daily schedule for purchasing gas and submitting offers to the ISO. Mem. at 19 n.8. But in fact, Maxim "generally did not purchase gas prior to receiving a dispatch award because of the risk it would not be dispatched and would incur a potentially significant loss." Penalty Assessment Order at P 86. That is, the daily timetable for oil and gas transactions did *not* "dictate" that Maxim purchase gas in advance. *See id.* ("Maxim does not deny that in 2010 it also followed this practice of waiting to purchase gas until it had a dispatch award.").

An internal Maxim email to Mitton on July 20, 2010, for example, said that Maxim could deter the Market Monitor from doing further inquiry into what fuel Maxim burned "[i]f we can provide the [Market Monitor] with the rationalization behind our pricing." Pet. ¶ 46. And Mitton told the Market Monitor on August 18, 2010 that he "was under the impression . . . that the mere notification of 'potent[i]al' gas procurement [problems] and the offer of oil was sufficient and that no further review would be done by [the Market Monitor]." *Id.* That is, Maxim believed that if it worded its emails in just the right way, the Market Monitor would never discover that Pittsfield had burned nearly 100% gas while collecting at high prices ($175/MWh) for oil it did not burn.

B. **The Petition Properly Pleads A Fraudulent Device, Scheme, or Artifice Under Rule 1c.2(a)(1) and an "Act, Practice, or Course of Business That Operates or Would Operate as a Fraud or Deceit Upon Any Entity" Under Rule 1c.2(a)(3)**

Maxim contends that the Commission cannot make out a claim for a "fraudulent device, scheme, or artifice" (under Rule 1c.2(a)(1)) or for "engaging in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity" (under Rule 1c.2(a)(3)) because those claims would be "duplicative of a claim for alleged misrepresentations or omissions under Rule 10b-5(b), the analogue of FERC Rule 1c.2(2)." Mem. at 21. That contention is incorrect.

First, while the Commission considers precedents about the SEC's Rule 10b-5 to be helpful, the Commission is not bound by those precedents in applying its own Rule. *See* Order No. 670 at P 30. *Second*, Maxim cites no authority from the First Circuit or this District holding that claims under Rule 10b-5(a) and Rule 10b-5(c) are precluded by claims under Rule 10b-5(b). *Third*, and most important, the facts supporting liability under Rule 1c.2(a)(1) and 1c.2(a)(2) here are *not* limited to the false and misleading statements that Maxim and Mitton made to the Market Monitor. Rather, as the

Petition makes clear, "Maxim's fraudulent scheme consisted of its entire pattern of conduct, including its energy offers on fuel prices (when it in fact expected to and did acquire virtually all of the natural gas it needed, often doing so hours before the ISO announced Day Ahead dispatches)." Pet. ¶ 50.[26]

Maxim contends (at 22) that offering on oil while burning gas did not violate any tariff provision, and therefore cannot be part of a manipulative scheme. But as discussed above, market manipulation is not limited to tariff violations. In any event, Maxim not merely offered on oil and burned gas, but *expected and planned* to do so, and often bought gas in advance of submitting offers on high oil prices, Pet. ¶ 50, as part of a plan to defeat the ISO's rules aimed at preventing reliability units from exploiting their market power. *Id.* ¶¶ 30-40, 50, 51.

Finally, as discussed above, Maxim contends (at 23) that its conduct was based on "legitimate economic concerns" that led it to offer on high oil prices, and that the Court should dismiss the Petition on that basis. Maxim's contention is contrary to the factual allegations of the Petition (*e.g.*, ¶ 50), which the Court must accept as true in considering a motion to dismiss. But even if Maxim's explanations for its offers were accurate (and they are not),[27] it did not have the right to try to mislead the Market Monitor.

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[26] *See also id*. ¶ 7 ("Maxim and its employee in charge of making bids for the Pittsfield plant, Kyle Mitton, knew that the Pittsfield plant would make large amounts of money if Maxim could burn inexpensive natural gas at the Pittsfield plant but nevertheless be paid by the ISO based on the much higher price of fuel oil."); *id*. ¶ 8 ("During hot days in July and August 2010, Maxim and Mitton repeatedly submitted offers to ISO-NE for Pittsfield at high oil prices when they expected and planned to burn much cheaper natural gas. On many days, Maxim procured natural gas before it learned whether it had been dispatched by the ISO, and on at least 11 days it did so before submitting offers priced on oil.").

[27] While Maxim claims it offered at oil prices when the pipeline posted restriction notices, Maxim offered on gas prices on several days during the summer of 2010 even though the pipeline had posted restriction notices. Order at P 92. And in at least one case, Maxim changed an oil offer to a gas offer even though the pipeline had posted a restriction notice. *Id.* P 93.

As documented above, the factual allegations of the Petition far exceed the "plausibility" standard applicable to a motion to dismiss: those allegations show that Maxim sought, by offering oil and burning gas and then misleading the Market Monitor about what it had done, to defraud utilities and other purchasers of wholesale energy in New England of nearly $3 million.

C. The Petition Properly Pleads Materiality

Maxim does not dispute that the representations and omissions quoted and discussed in the Petition related to a plainly material issue: whether Maxim could collect (and ultimately force utilities and other purchasers to pay) more than $3 million for the costs of fuel oil that Maxim did not actually burn. Rather, Maxim argues, in effect, that it does not matter if it tried to mislead the Market Monitor in July 2010, because the truth came out later.[28]

Neither the FPA nor the Commission's Anti-Manipulation Rule give immunity to deceptive conduct because the deception is later uncovered. Nor do the private securities class action cases that Maxim cites (at 24) help their case. Those cases are about how to prove (or to rebut proof of) reliance by individual investors.[29] But as is true in SEC enforcement actions,

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[28] Based on a statement in the dissent (which did not cite any record evidence), Maxim claims (at 24) that the Market Monitor reversed the $2.99 million in inflated payments "prior to settlement." That contention would be irrelevant even if that were true, because the Anti-Manipulation Rule does not require reliance or damages. *See* p. 24 & n.30, *infra*. But in any event, the contention is wrong. The ISO's mitigation of the overpayments to Maxim occurred months later (in October and November 2010). Order at P 33. As Maxim conceded in the adversarial proceeding before the Commission, it had to "return" (*i.e.*, pay back) money that the ISO had already paid it. Specifically, Maxim told the Commission that it "*returned* all of this money [*i.e.*, the $2.99 million in inflated payments] under ISO-NE's standard process," and described the $2.99 million as "amounts *returned* through mitigation." Maxim Show Cause Response at 53, 54 (emphasis added) (reproduced in Appendix A hereto).

[29] *In re Boston Scientific Corp. Sec. Litig.*, 708 F. Supp. 2d 110, 128 (D. Mass. 2010) ("The 'truth on the market' defense "is intended to rebut the plaintiff's presumption of reliance on the market . . . "), *aff'd sub nom. Mississippi Pub. Employees' Ret. Sys. v. Boston Scientific Corp.*, 649 F.3d 5 (1st Cir. 2011); *In re Sec. Litig. BMC Software, Inc.*, 183 F. Supp. 2d 860, 905 n.46

neither reliance nor damages is an element in a case under the Commission's Anti-Manipulation Rule.[30] And under the Anti-Manipulation Rule, like under Rule 10b-5, attempts to defraud create the same liability as successful schemes.[31]

That the Market Monitor eventually discovered the truth (that Maxim was burning gas while charging for oil) is therefore no defense, particularly when Maxim's express goal in its communications with the Market Monitor was to *prevent* the Market Monitor from learning the relevant facts. *See* Pet. ¶ 46 (Mitton believed that because he had mentioned pipeline problems in his emails, "*no further review would be done by [the Market Monitor]*") (emphasis added).[32]

In its Penalty Assessment Order, the Commission considered and correctly rejected Respondents' argument that they should be exonerated (or pay no penalty) because their conduct was caught before it ultimately harmed consumers. Order at P 7 n.5, P 53 n.112, P 122, P 144 n.290. As the Commission explained, "manipulation, fraud, and misrepresentations to market

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(S.D. Tex. 2001) ("The defendants can then rebut [the] presumption of reliance by demonstrating . . . that the nondisclosures did not affect the market price . . . .").

[30] Order No. 670 at P 48 n.102 ("reliance, loss causation and damages are not necessary for a violation of [FERC's] Final Rule"). *See also, SEC v. Tambone*, 597 F.3d 436, 447 n.9 (1st Cir. 2010) ("the SEC need not establish [reliance] in a Rule 10b–5 case").

[31] The phrase "would operate as a fraud" in Rule 1c.2(a)(3) (like the same phrase in Rule 10b-5) covers schemes that are unsuccessful or later reversed. Order at 7 n.5; *see SEC v. Todt*, No. 98 Civ. 3980, 2000 WL 223836 (JGK), at **9-10 (S.D.N.Y. Feb. 27, 2000), *aff'd mem.*, 7 Fed. App'x 98 (2d Cir. 2001); *Grumet v. Shearson/American Express, Inc.*, 564 F. Supp. 336, 340-41 (D.N.J. 1983).

[32] Nothing in the ISO's statements about post hoc reviews (*e.g.*, "The market monitor uses pipeline public postings and other documentation to verify Market Participant statements") (Mem. at 8-9) says that the Market Monitor always did a manual review of pipeline records, particularly when (as here) a generator sought to discourage the Market Monitor from checking on what fuel it burned. In any event, even if the Market Monitor had a foolproof system for later detecting false statements by market participants, that would not provide Maxim with a defense to violation of either the Anti-Manipulation Rule or section 35.41(b), because achievement of Maxim's ultimate goal is not an element of either provision. *See United States v. Dixon*, 449 F.3d 194, 202 (1st Cir. 2006) ("Since the elements of those offenses do not require that the unlawful goal be achieved, factual impossibility is irrelevant.") (citations omitted).

monitors are unacceptable in Commission-regulated markets even where such behavior is caught before it causes harm to consumers. Courts have long recognized that attempted manipulation and fraud are worthy of punishment in the same manner as successful schemes." Order at P 7 n.5 (citing cases); *id.* P 122 ("The fact that a violation is discovered by a market monitor does not excuse the violation. If the elimination of an unjust gain upon discovery of misconduct excused the misconduct, then a civil penalty would have no deterrent effect: if its manipulative conduct is undiscovered, a market participant keeps the unjust gains, but if its manipulative conduct is discovered, it only pays back the unjust gains. Under those circumstances, a manipulator that is caught is no worse off than the honest market participant.").

D. <u>The Petition Properly Pleads Scienter</u>

Based on detailed allegations about Respondents' conduct (Pet. ¶¶ 7-10, 29-32, 37-50), the Petition properly alleges scienter, *id*. ¶ 63, and incorporates by reference the Commission's lengthy and detailed findings on that topic (Order at PP 83-97). As the Petition explains, "[t]he Commission determined that Maxim and Mitton intentionally engaged in a scheme to offer on fuel oil prices while actually burning natural gas and to mislead [the Market Monitor] about what they had done." Pet. ¶ 63. (Although Respondents' conduct was intentional, recklessness is sufficient to satisfy the scienter standard of the Anti-Manipulation Rule. Order at P 83.)

Maxim's arguments to the contrary fail. *First*, Maxim contends (at 25) that it had "no reason to conceal" that Pittsfield burned natural gas while submitting offers at high oil prices. But Maxim had a strong motive to do so: it could collect nearly $3 million in inflated payments if the Market Monitor did not discover the facts. *See* Pet. ¶¶ 1, 9-10, 39-40, 48, 51, 62-63.

Second, Maxim contends (at 25) it did not have a free-standing duty to report that it was burning natural gas. But as discussed above, that contention, even if true, misses the point: in

the context of specific communications with the Market Monitor about oil-gas issues, and to protect its windfall, Maxim made misrepresentations and omitted material facts needed to make its affirmative statements not misleading.

Third, Maxim argues (at 25-27) that because the Market Monitor's initial voicemail mentioned offer prices, Maxim's communications were not misleading. But as discussed above, what matters is not merely the wording of a single voicemail, but the entire context of a series of communications. In that context, Maxim's communications were deceptive. *See* pp 13-14, 17-23 *supra*.[33]

III. THE PETITION PROPERLY PLEADS A VIOLATION OF A SEPARATE COMMISSION RULE REQUIRING MAXIM TO BE ACCURATE AND NOT OMIT MATERIAL INFORMATION IN COMMUNICATIONS WITH MARKET MONITORS

Maxim's Pittsfield Generating Co. unit was required to comply with the Commission's Market Behavior Rules, which require entities with market-based rate authority (called "Sellers") to "provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with . . . Commission-approved market monitors . . . unless Seller exercises due diligence to prevent such occurrences." 18 C.F.R. § 35.41(b) (2015). Unlike with the Anti-Manipulation Rule, "intent to deceive is not an element of [section 35.41(b)]. The Rule's plain text lacks any reference to intent and forgives false or misleading submissions only if they are made inadvertently despite the filer's due diligence to avoid such errors." *Kourouma v. FERC*, 723 F.3d 274, 278 (D.C. Cir. 2013).

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[33] Maxim also argues (at 27 n.9) that its subsidiaries named as Respondents were not on notice of what each entity did. But as the Commission noted, Maxim's subsidiaries have no employees; Maxim runs all of the units as a "single unified business enterprise"; and parent company employees act on behalf of, and are named as representatives of, the subsidiaries. Order at PP 8, 19, 136. All of the Respondents were fully on notice of the relevant facts.

The Petition properly alleges, and the Commission found at the conclusion of an adversarial proceeding, that Maxim made false and misleading statements and material omissions. Pet. ¶¶ 40-48, 74; Order at PP 49-63. (Maxim did not assert a due diligence defense. Order at P 102 n.235.) For the reasons discussed above, the Petition's allegations about misrepresentations and omissions far exceed pleading requirements, and the Court should deny Respondents' motion to dismiss the section 35.41(b) claims.

IV. <u>FERC'S CLAIMS ARE NOT BARRED BY THE FAIR NOTICE DOCTRINE</u>

Maxim contends (at 27-28) that it did not have fair notice that its July-August 2010 conduct could be considered unlawful. In particular, Maxim claims it was not told that "FERC interpreted its tariffs, rules, and regulations in 2010 to prohibit a dual-fuel unit from offering on one fuel but burning another fuel or to require a dual-fuel unit to provide [the Market Monitor] with fuel burn data before it is asked." But those are not the allegations on which this case is based. The Order finds, and the Petition charges, that Maxim engaged in a scheme not merely to offer on one fuel but burn another, but to plan to do exactly that (*e.g.*, through advance gas purchases), and to defeat the ISO's mitigation rules and collect a windfall by, among other things, deceiving the Market Monitor. Likewise, the Petition does not allege a free-standing obligation to disclose gas burns, but an obligation to do so to ensure that other statements are not misleading.

The Commission correctly rejected Respondents' claims that "they were not on notice that misleading statements or omissions of material fact to a market monitor could constitute manipulation." Order at ¶ 63. As the Commission explained, "[i]n the order promulgating this rule, the Commission . . . made explicit this prohibition on intentionally misleading statements and omissions of material fact." *Id.*

Similarly, Maxim was at all times on notice of its obligation under § 35.41(b) to be candid and not to omit material information. 18 C.F.R. § 35.41(b). Maxim can scarcely claim to be surprised that the Commission expects it to comply with this long-standing regulation.

V. FERC HAS STATUTORY AUTHORITY TO ASSERT A CLAIM AGAINST MITTON FOR VIOLATION OF SECTION 222(a) OF THE FPA

Mitton contends (at 28-30) that when Congress amended the FPA to give the Commission express anti-manipulation authority, it intended to insulate individuals from liability. As the Commission concluded in Order No. 670, and as the U.S. District Court for the Eastern District of California recently confirmed,[34] that contention is incorrect.

Section 222 of the FPA bars "any entity" from engaging in "manipulative behavior . . . in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of electric ratepayers." Based on the plain meaning of the word "entity," the logical reading of the text in the context of Congress' goals, and the deference due the agency under *Chevron*, section 222 authorizes the Commission to impose liability on individuals for market manipulation.

Mitton argues (at 28) that "'[e]ntity' does not and cannot mean an individual." In fact, numerous sources interpret the broad term "entity" to include individuals. *E.g.*, *City of Abilene v. FCC*, 164 F.3d 49, 52 (D.C. Cir. 1999) (entity "may include a natural person, a corporation, a partnership, a limited liability company, a limited liability partnership . . . ."); Black's Law Dictionary (6th ed. 1990) ("an organization or being that possesses separate existence for tax purposes); West's Encyclopedia of American Law (2nd ed. 2008) ("Entity" is "[a] real being; existence. . . . Entity includes person, estate, trust, governmental unit."); American Heritage

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[34] *FERC v. Barclays Bank PLC*, No. 2:13–cv–2093–TLN–DAD, 2015 WL 2448686, at *20-21 (E.D. Cal. May 20, 2015), as amended (May 22, 2015) (attached as Appendix B).

Dictionary (5th ed. 2011) ("Something that exists as a particular and discrete unit: *persons and corporations are equivalent entities under the law*") (emphasis in original).

Reading "entity" in section 222 to include natural persons is logical given Congress' goal of providing the Commission with strong tools to combat market manipulation in the wake of the Enron scandal. As the *Barclays* court explained:

> Overall, a meaning of "entity" that includes natural persons appears more consistent with the goals of FPA § 222 and the surrounding statutory scheme. *See Roberts v. Sea–Land Services, Inc.*, ––– U.S. ––––, 132 S. Ct. 1350, 1357, 182 L.Ed.2d 341 (2012) ("[T]he words of a statute must be read in their context and with a view to their place in the overall statutory scheme.") Other relevant enforcement provisions in the FPA include natural persons. For example, FPA § 221, 16 U.S.C. § 824u, which was enacted concurrently with FPA § 222, provides that "No entity shall willfully and knowingly report any information relating to the price of electricity sold at wholesale or the availability of transmission capacity, which information *the person* or any other entity knew to be false . . ." (emphasis added). . . . FPA § 316, 16 U.S.C. § 825o(a) provides for criminal liability by "[a]ny person" who knowingly violates any provision of the FPA, which would include FPA § 222.

FERC v. Barclays Bank, 2015 WL 2448686, at *20.[35]

The Commission's interpretation of "any entity" to include individuals rests on the common-sense proposition that while they may act on behalf of corporations, it is *individuals* who plan and execute fraudulent schemes. Reading section 222 to exempt the individuals who actually engage in wrongful conduct would be inconsistent with Congress' intent to provide strong and effective remedies against manipulation of wholesale electricity markets.

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[35] Even if Mitton were correct in his critique of the *Barclays* court's conclusions based on another provision of the FPA (Section 316A) (Mem. at 30), it would not matter, in light of the many other grounds for concluding that "entity" includes individuals.

In addition, section 18 of Energy Policy Act of 2005, 15 U.S.C. § 717s (2012), prohibits trading by "individuals" who have violated the NGA's anti-manipulation provision (15 U.S.C. § 717c-1), which, like FPA § 222, applies to "any entity." Because the NGA's anti-manipulation provision treats individuals as "entities," it is logical to read the FPA anti-manipulation provision (enacted the same day) identically. In addition, it would be strange indeed for Congress to impose criminal (16 U.S.C.§ 825o(a)), but not civil, penalties on individual market manipulators.

Mitton argues that differences in the language of the Securities Exchange Act and of the FPA mean that Congress must have intended to exclude individuals under section 222 of the FPA. But as the *Barclays* court explained, the relevant point is the opposite:

> FPA § 222 makes unlawful the use of "any manipulative or deceptive device or contrivance (as those terms are used in section 78j(b) of title 15)," i.e. Section 10(b) of the Securities Exchange Act ("SEA") and its corresponding Rule 10b–5. Actions under Section 10(b) and Rule 10b–5 are routinely brought against individuals. . . . *Defendants do not provide adequate reason to conclude that Congress would enact an anti-manipulation statute modeled after the SEA, but preclude enforcement against persons who engaged in manipulative trading*.

FERC v. Barclays Bank PLC, 2015 WL 2448686, at *20-21 (emphasis added).

In addition, the Commission's determination is entitled to *Chevron* deference: even if the term "entity" is ambiguous, the Commission is permitted to adopt a reasonable interpretation consistent with its long experience and expertise administering the FPA. *See Chevron U.S.A., Inc. v. Natural Resources Def. Council*, 467 U.S. 837, 843 (1984); *Rolland v. Romney*, 318 F.3d 42, 48 (1st Cir. 2003) ("'[a]n inquiring court – even a court empowered to conduct *de novo* review – must examine the [agency's] interpretation of the statute, as expressed in the regulation, through a deferential glass.'") (citations omitted). And as the Supreme Court recently emphasized in *City of Arlington v. FCC*, 133 S. Ct. 1863 (2013), *Chevron* deference extends to all ambiguities in a statute, even those that an enforcement subject might try to characterize as "jurisdictional" (like the meaning of "any entity" in FPA § 222). *Id.* at 1874-75.

The Court should therefore conclude that the Federal Power Act authorizes the Commission to assess a penalty against Mitton for market manipulation.

CONCLUSION

For the reasons discussed above, the Court should deny Respondents' motion to dismiss.

Respectfully submitted,

FEDERAL ENERGY REGULATORY COMMISSION

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Dated: September 25, 2015

Certificate of Service

I hereby certify that a true copy of the above document will be served on September 25, 2015 by filing this document using the CM/ECF system. I also certify that I have arranged for a copy of the document to be emailed today to counsel at Gibson, Dunn & Crutcher LLP.

/s/ Thomas P. Olson
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