

CANARIES IN THE COAL MINE: FACTS FROM SECURITIES FRAUD PRIVATE CIVIL ACTIONS CAN IDENTIFY INTENT TO MANIPULATE ENERGY MARKETS

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Synopsis: Congress modeled its Energy Policy Act of 2005 market manipulation provisions on longstanding federal securities law. The EAct 2005 specifically declared unlawful, for energy markets, any manipulative or deceptive device or contrivance, as those terms are used in federal securities law for securities markets. The FERC and energy industry participants thus can use analogous securities industry precedents as a guide in energy industry litigations. But, in the words of an anonymous FERC practitioner: “What is [manipulation]? How do we know it?” Approaching that pre-eminent question from one angle, market manipulation cannot be proved without evidence of intent, or *scienter*. Besides the Securities and Exchange Commission’s own cases on intent, many additional private party, civil class action federal court cases also analyze securities fraud intent. The U.S. Supreme Court views those private civil actions as an indispensable tool to deter fraud. Analogous facts from those federal court decisions work as do canaries in coal mines,¹ helping to identify *scienter* or its absence in energy industry market manipulation prosecutions, for which the FERC has substantial new penalty powers.

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1. “[T]raditionally used by miners to warn those who labor mightily in a difficult area when ‘danger’ is imminent.” *United States v. Simmons*, 31 M.J. 884, 886 (A.F.C.M.R. 1990).

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I. SUMMARY AND INTRODUCTION

The Energy Policy Act of 2005 (EPAAct 2005)² requires the Federal Energy Regulatory Commission (FERC) to prevent energy industry market manipulation and fraud through such enforcement rules and regulations as that agency prescribes. The FERC has concluded that its energy industry enforcement actions must show a person's or an entity's intent, or *scienter*, to manipulate or defraud.³ The FERC, its Office of Enforcement (OE), and other energy industry participants therefore should be able to identify *scienter*.⁴

Congress expressly patterned EPAAct 2005 prohibitions of manipulation and fraud in U.S. energy markets on securities law prohibitions of manipulation and fraud in U.S. securities markets. The FERC declares that its civil prosecutions of energy market manipulation will be guided by U.S. Securities and Exchange Commission (SEC) civil enforcement decisions, including the law of alleged manipulator intent or *scienter*. *Scienter* is to apply to FERC enforcement just as *scienter* applies to SEC enforcement.⁵

Besides the SEC's own cases, to help identify *scienter* or its absence FERC practitioners should employ the many federal court securities law cases with facts showing or failing to show *scienter*. Federal courts recognize and adjudicate civil class actions by private parties complaining of violations of federal, antifraud securities law, and treat such suits as essential, necessary

2. Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594 (2005).

3. Order No. 670, *Prohibition of Energy Market Manipulation*, F.E.R.C. STATS. & REGS. ¶ 31,202 (2006), 71 Fed. Reg. 4,244 (2006), 114 F.E.R.C. ¶ 61,047 at [text paras.] PP 49, 52-53, *reh'g denied*, 114 F.E.R.C. ¶ 61,300 (2006) [hereinafter Order No. 670].

4. Dictionary definition can be too abstract to be useful (i.e., *scienter* as the degree of knowledge making one "legally responsible for the consequences" of an act or omission, "[especially] as a ground for civil damages or criminal punishment." BLACK'S LAW DICTIONARY 1373 (8th ed. 2004). *Scienter* and intent are used interchangeably here.

5. Order No. 670, *supra* note 4, at PP 30-31 & n.56, 52-53 (at P 31 the FERC states that while "a wholesale overlay of the securities laws onto energy markets is overly simplistic, we also believe it would be illogical to simply ignore decades of useful guidance that securities law precedent can offer, especially considering that Congress deliberately modeled EPAAct 2005 sections 315 and 1283 on Section 10(b) of the Exchange Act").

supplements to SEC civil enforcement and U.S. Department of Justice (DOJ) criminal prosecution.⁶ Private securities litigation functions as an indispensable tool to deter fraud.⁷ In fact, the U.S. Supreme Court first applied the *scienter* requirement to securities law enforcement in a private civil action, not an enforcement by the SEC itself.⁸

Using a heightened pleading standard to promote meritorious private party actions enforcing securities law, the Private Securities Litigation Reform Act of 1995 (PSLRA) amended the Exchange Act to require complainants to show with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.⁹ The PSLRA, however, does not change the ultimate standard of proof to be met or the kind of evidence to be adduced for *scienter* under Exchange Act § 10(b) and SEC Rule 10b-5.¹⁰ PSLRA federal court decisions thus apply the same *scienter* standard of proof, and require the same kind of *scienter* evidence to be adduced under Exchange Act § 10(b) and SEC Rule 10b-5, as SEC decisions do.¹¹

Like canaries in coal mines, facts from securities law cases, including the very large body of PSLRA cases, can indicate the presence or absence of intent for energy industry prosecutions. PSLRA decisions set out in section IV below teach, among other things, that *scienter* is not alleged adequately without facts either of motive and opportunity to manipulate markets, or of reckless behavior. Generalized motives common to all business corporations and persons are insufficient to plead intent. Specific instances must be given and described with particularity. Culpable behavior should link individuals to the manipulation or fraud alleged. Factual background must be explained. Neither negligent mistakes, nor even grossly negligent behavior, amount to *scienter* to defraud. As a final, practical matter, fraudulent filing of documents, reports, or forms readily can show the intent by signatory corporate officers required to prosecute market manipulation.

The EPAct 2005 creates no private rights of action to prove market manipulation. Vesting enforcement solely with the FERC, however, does not prevent the use of PSLRA case facts to argue for or against *scienter*. The FERC and its OE appropriately need to identify and define intent to manipulate in U.S.

6. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S.Ct. 2499, 2504 (2007).

7. *Id.* at 2508 n.4.

8. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193-94, 201 (1976). The Court later ruled that *scienter* also must be established as an element for SEC civil actions to enjoin violations of Securities Exchange Act of 1934 (Exchange Act) § 10(b) (15 U.S.C. § 78j(b)) and SEC Rule 10b(5) (17 C.F.R. § 240.10b-5). *Aaron v. SEC*, 446 U.S. 680, 682-84, 701-02 (1980).

9. 15 U.S.C. § 78 u-4(b)(2) (2000). Facts must be pleaded "rendering an inference of *scienter* at least as likely as any plausible opposing inference." *Tellabs*, 127 S.Ct. at 2513.

10. Congress prescribed in the PSLRA what private parties are to plead to state a claim. Congress did not re-determine what must be proved to prevail on the merits. *Tellabs*, 127 S.Ct. at 2508, 2512-13.

11. Recent SEC *scienter* rulings include: *In re Amanat*, 2007 SEC LEXIS 2558, at *1, 35, & n.44 (Nov. 3, 2007) ("[A chief technology officer executing wash trades and matched orders] . . . knew or was, at a minimum, reckless in not knowing that the thousands of ETF trades he was executing . . . matched against each other at least seventy-five percent of the time on each of the trading days in question."); *In re OM Group, Inc.*, 2007 SEC LEXIS 1558, at *20-23 & n.7 (July 18, 2007) ("The level of *scienter* was high. The CFO and Controller concealed from the company's auditor the fact that many of their top-side adjustments lacked support and were done with the intent to manage earnings. The CFO's and the Controller's *scienter* is imputed to OM Group.").

wholesale natural gas and electricity markets to refrain from making insufficient, vague, or conclusory allegations in prosecutions. PSLRA decision facts will help them do that. Better identification and understanding of *scienter* by energy industry participants also will work to deter fraud by reducing regulatory uncertainty and promoting greater compliance with the energy laws and the FERC's rules and regulations, especially given the high stakes under new, substantial, EAct 2005 FERC penalty powers.

II. FERC ENFORCEMENT PENALTY AND POLICY LANDSCAPE

Patterned deliberately on the Exchange Act, the EAct 2005 declares unlawful any direct or indirect use or employment of manipulative or deceptive devices or contrivances in energy industries regulated under the Natural Gas Act (NGA), the Natural Gas Policy Act of 1978 (NGPA), and the Federal Power Act (FPA).¹²

A. Increased Civil and Criminal Penalties

The EAct 2005 increases civil and criminal penalties applicable to all NGA, NGPA, and FPA violations, including market manipulation.¹³ Defined penalties now are available for the FERC to match with violations of different energy laws and different FERC actions under those laws. For civil violation of the NGA, or of a rule, regulation, restriction, condition, or order under the NGA, a penalty up to \$1,000,000 per day per violation may be imposed, after notice and opportunity for public hearing.¹⁴ The FERC Chairman has declared: "The enforcement and civil penalty provisions of the Energy Policy Act of 2005 were inspired in large part by the market manipulation that occurred during 2000-01 [I]t may be appropriate, depending on the facts, to impose maximum or near-maximum penalties for market manipulation . . . even in the absence of serious harm."¹⁵ For NGA, NGPA, and FPA criminal violations, limits on fines are raised to \$1,000,000, and prison term limits to five years.¹⁶ As does the SEC, the FERC refers alleged criminal violations to the DOJ for prosecution.

12. Such EAct 2005 provisions prohibiting market manipulation forbid such devices or contrivances in connection, in a statutory mouthful, either with the purchase or sale of gas or FERC-jurisdictional gas transportation services, or with the purchase or sale of electric energy or FERC-jurisdictional electricity transmission services, if the use or employment of the devices or contrivances contravenes FERC rules and regulations prescribed in the public interest or to protect gas or electric ratepayers. EAct 2005 §§ 315 and 1283, which are new NGA § 4A, and FPA § 222. 15 U.S.C. § 717c-1 (2000); 16 U.S.C. § 824v (2000). See generally J. Michel Marcoux, *Day of Decision for FERC*, 143 PUB. UTIL. FORT., No. 12, 55-62 (Dec. 2005); see also *Tellabs*, 127 S.Ct. at 2507.

13. *Day of Decision*, *supra* note 13, at 57-58; accord OFFICE OF ENFORCEMENT, FERC, REPORT ON ENFORCEMENT 5-6, Docket No. AD07-13-000 (2007).

14. A civil violation of the NGPA, or of a rule or order under the NGPA, allows the FERC (or in a gas supply emergency, the President) to assess up to a \$1,000,000 penalty per violation. For a civil violation of the FPA Part II, or of a rule or order thereunder, the FERC may assess up to a \$1,000,000 penalty for each day the violation continues.

15. Joseph T. Kelliher, Chairman, FERC, Statement at Conference on Enforcement Policy, Docket No. AD07-13-000 (Nov. 16, 2007), at 5.

16. Criminal violation of a rule, regulation, restriction, condition, or order under the NGA, or a NGPA rule or order, can result in a fine up to \$50,000 each day the offense occurs. For criminal violations of a rule, regulation, restriction, condition, or order under the FPA, the limit is \$25,000 each day the offense occurs.

B. 2005 Enforcement Policy Statement

To provide guidance and regulatory certainty, the FERC listed factors in its 2005 Policy Statement on Enforcement, such as the extent of senior management involvement, that it considers in determining whether to apply increased penalties for energy law violations, including market manipulation.¹⁷

C. Negotiated Settlements

In 2007, the FERC's first dozen civil penalty orders approved negotiated settlements with the OE in five natural gas industry cases and seven electric industry cases.¹⁸ While demonstrating the FERC's increased penalty authority, none of the settlements dealt with market manipulation.¹⁹

D. Civil Penalty Assessments Absent Settlement

With its 2006 administrative policy statement, the FERC set out specific procedures to assess civil penalties when there is no settlement.²⁰ Nothing in that policy statement changes current practice to negotiate resolution of violations, including civil penalties, wherever possible. The agency reserves "the right to modify [policy statement] procedures . . . while still providing [a legal] process that meets . . . applicable statutory criteria."²¹ In 2007, the FERC began its first two proceedings, outlined in section III.B below, dealing with asserted market manipulations under that policy statement.²²

17. *Enforcement of Statutes, Orders, Rules, and Regulations*, 70 Fed. Reg. 66,378 (2005), 113 F.E.R.C. ¶ 61,068 (2005). The FERC looks to the nature of the harm caused; the presence or absence of manipulation, deceit, artifice, or willful action; whether offenses were repeated or not; the extent of senior management involvement; how the wrongdoing came to light; and the effect of penalties on a violator's financial viability. Mitigation can occur if violators demonstrate internal compliance measures, engage in self-reporting, or cooperate with the OE Staff.

18. OFFICE OF ENFORCEMENT REPORT, *supra* note 14, at App. A.

19. Five gas orders approved \$0.3 million to \$7 million in penalties. *In re Bangor Gas Co.*, 118 F.E.R.C. ¶ 61,186 (2007); *In re Calpine Energy Servs., L.P.*, 119 F.E.R.C. ¶ 61,125 (2007); *In re Columbia Gulf Transmission Co.*, 119 F.E.R.C. ¶ 61,174 (2007); *In re MGTC, Inc.*, 121 F.E.R.C. ¶ 61,087 (2007); *In re BP Energy Co.*, 121 F.E.R.C. ¶ 61,088 (2007). Seven electric orders approved \$0.5 million to \$10 million in penalties. *In re NRG Energy, Inc., PacificCorp, Entergy Servs., Inc., SCANA Corp., NorthWestern Corp.*, 118 F.E.R.C. ¶¶ 61,025-29 (2007); *In re Cleco Power*, 119 F.E.R.C. ¶ 61,271 (2007); *In re Gexa Energy*, 120 F.E.R.C. ¶ 61,174 (2007).

20. *Process for Assessing Civil Penalties*, 117 F.E.R.C. ¶ 61,317 (2006). Under the NGA, for example, the FERC can notice a proposed civil penalty, state material facts, and give the entity thirty days to respond. Following response, the FERC can issue a final decision assessing a penalty, or order further filings in a paper hearing process, or order a hearing before a FERC administrative law judge. Final decisions may be appealed to a U.S. Court of Appeals. Under the NGPA, following response, the FERC can assess a penalty immediately and the entity either can pay up or seek U.S. District Court review, with either course's outcome subject to appeal. Under the FPA Part I, depending on the presence or absence of a FERC compliance order to the alleged violator, different procedures allow for immediate penalty, or a hearing before an administrative law judge, or District Court review, subject to appeal (those procedures apply under FPA Part II, but with no compliance order).

21. *Id.* at P 2.

22. The FERC denied a challenge to the administrative policy statement (i.e., that issues of liability for civil penalties and other remedies sought by the FERC, and their proper amount, must be resolved by *de novo* U.S. District Court trial, not by the FERC itself). *Energy Transfer Partners, L.P.*, 121 F.E.R.C. ¶ 61,282, at PP 20-66 (2007). Effective December 20, 2007, the FERC also addressed future agency civil penalty adjudication procedures, including making non-decisional all OE investigative staff assigned to participate in the remainder

III. MARKET MANIPULATION

FERC enforcement rules and regulations implement EAct 2005's mandate to prevent wholesale gas and electricity market manipulations and frauds.

A. 2006 FERC Order No. 670 Prohibition of Energy Market Manipulation and Required Element of Intent (*Scienter*) to Manipulate

Aside from its general Enforcement Policy Statement, specific FERC regulations §§ 1c.1 and 1c.2 prohibit natural gas market and electric energy market manipulation.²³ FERC Order No. 670 promulgated those regulations.²⁴ The FERC acknowledged that its allegations must show *scienter*.²⁵ Not every common law fraud is reached, but only those frauds intended to affect, or where an entity intentionally acted recklessly to affect, the price of a FERC-jurisdictional transaction.²⁶ The *scienter* requirement helps avoid insufficient, vague, or conclusory allegations, ultimately enabling predictable and effective energy law enforcement. No *scienter*, no violation.²⁷

B. Orders to Show Cause in Market Manipulation Prosecutions: “[T]here is no evidence here of any intent to manipulate the markets.”²⁸

On July 26, 2007, the FERC issued orders in two cases requiring entities to show cause why they had not violated FERC regulations prohibiting natural gas market manipulation. Those enforcement cases, regardless of their outcomes, inaugurated FERC EAct 2005 prosecution of energy industry market manipulation and fraud. In *Amaranth Advisors L.L.C.*, the FERC alleged that a hedge fund and its traders had manipulated FERC-jurisdictional prices in wholesale interstate gas markets in 2006 by manipulating the New York Mercantile Exchange Natural Gas Futures Contract.²⁹ Warning that manipulations will be punished severely, the FERC compared *Amaranth* facts to 2000-01, western U.S., energy market manipulation facts, stating that such past Enron trader conduct

bespoke an attitude that markets served as their private laboratories where they were free to tinker with prices and supply in order to test responses and to make

of the *Energy Transfer* proceeding, and other future proceedings, in the belief that additional due process will be provided and perceptions of unfairness or prejudice will be eliminated in NGA, NGPA, and FPA civil penalty cases. *Id.* at PP 88-90.

23. 18 C.F.R. §§ 1c.1, 1c.2 (2007).

24. Order No. 670, *supra* note 4, at PP 5, 16-17 & n.30, 24.

25. *Id.* at PP 49, 52-53; accord Order No. 673, *Amendments to Codes of Conduct for Unbundled Sales Service and for Persons Holding Blanket Marketing Certificates*, F.E.R.C. STATS. & REGS. ¶ 31,207, at P 18 & n.30, 71 Fed. Reg. 9,709 (2006) (“Congress prohibited market manipulation by any entity and defined manipulation to include the requirement of *scienter*,” giving those terms the same meaning as used in Exchange Act § 10(b)).

26. Order No. 670, *supra* note 4, at PP 16, 20, 22 & n.39, 25, 52-53. An entity includes any person or form of organization. *Id.* at P 18.

27. *Id.* at PP 45, 52.

28. Alan Zibel, *Amaranth Charged in Control of Prices*, WASH. POST, July 26, 2007, at D3 (quoting Geoffrey F. Aronow, attorney for Amaranth Advisors L.L.C.’s former chief executive). See also *Amaranth Advisors L.L.C.*, Order to Show Cause and Notice of Proposed Penalties, 120 F.E.R.C. ¶ 61,085 (2007), *reh’g denied*, 121 F.E.R.C. ¶ 61,224 (2007).

29. 120 F.E.R.C. ¶ 61,085, at PP 2, 5.

extraordinary profits. Their “experiments” gave little care to the harmful impact of such behaviors on the functioning of the markets or harm to other market participants and the public at large. Congress passed the salient provisions of EPAct 2005 in direct response to those behaviors and charged us with the obligation to detect, investigate, punish, and deter such manipulations. As [Amaranth head energy trader] Hunter’s “bit of an experiment” illustrates, even after the legal aftermath of Enron, the enactment of EPAct 2005, and the promulgation of Commission rules, there are still those who need to recognize that manipulation, even in complex markets, can be detected and, when proven, will be punished severely.³⁰

The FERC declared that *Amaranth* facts indicated strong intent through reckless conduct to manipulate the settlement price (which sets the price of any futures contracts that go to delivery) of certain 2006 contracts.³¹ Respondents were directed to answer why they should not be assessed civil penalties for, and required to disgorge unjust profits plus interest from, market manipulation violations, totaling almost \$300,000,000.³²

Also, in *Energy Transfer Partners, L.P.*,³³ the FERC ordered a large master limited partnership to show cause that it had not manipulated Texas gas markets in violation of FERC anti-manipulation Market Behavior Rule 2 effective in 2003-05, that it should not pay \$82,000,000 in civil penalties and disgorge \$69,866,966 in unjust profits plus interest, and that it should not have its blanket certificate to sell gas subject to FERC jurisdiction revoked. Additionally, an affiliated intrastate pipeline was ordered to show cause it had not discriminated illegally against non-affiliated shippers and preferred unduly one or more affiliated shippers, not charged rates above NGPA Section 311 maximum lawful rates, not failed to file an amended statement of operating conditions, and should not pay civil penalties of \$15,500,000 and disgorge \$267,122 in unjust profits plus interest. The FERC commented in part that, while the timing of trades to sell gas and buy it back indicated an intent to manipulate the market, it was unclear whether senior management was involved.³⁴

C. Securities Law Pattern for Energy Market Manipulation Prohibition

The EPAct 2005 deliberately uses the phrase “manipulative or deceptive devices or contrivances” in the public interest and to protect gas and electric ratepayers, just as the same phrase in Exchange Act § 10(b) is used in the public interest, but to protect investors. The FERC declared that its Order No. 670 rule

30. *Id.* at P 140.

31. *Id.* at PP 111-12 (“intentional manipulation of the price for that jurisdictional gas. . . even if the object of the manipulation was simply to benefit swap or other derivative positions”) (relying on a pre-PSLRA, private securities litigation *scienter* precedent: *Sunstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977)).

32. Responses to the *Amaranth* show cause order cited PSLRA federal court *scienter* precedents. *See, e.g.*, Brian Hunter’s Mem. in Response to the FERC’s Order to Show Cause & Notice of Proposed Penalties at 87-88, *Amaranth Advisors L.L.C.*, 120 F.E.R.C. ¶ 61,085, (F.E.R.C. 2007) (No. IN07-26-000), and also Response of Matthew Donohoe to FERC’s Order to Show Cause & Notice of Proposed Penalties at 10, 19, 22 *Amaranth Advisors L.L.C.*, 120 F.E.R.C. ¶ 61,085, (F.E.R.C. 2007) (No. IN07-26-000).

33. *Energy Transfer Partners, L.P.*, 120 F.E.R.C. ¶ 61,086, at PP 1-2, 17, 34-37 (2007), *reh’g denied*, 121 F.E.R.C. ¶ 61,282 (2007).

34. *Id.* at P 146; *see also id.* at PP 41, 63, 73, 119.

is modeled on SEC Rule 10b-5.³⁵ The FERC intends to be guided, case-by-case, by analogous securities industry precedents that are appropriate under the facts, circumstances, and situations presented in energy industries.³⁶ Pointing to decades of useful guidance that securities law precedent can offer, the FERC insists that the *scienter* element of a market manipulation violation will apply to its Order No. 670 civil enforcements of EAct 2005 prohibitions against manipulation, fraud, and deceptive conduct just as it applies to SEC Rule 10b-5 enforcements.³⁷ In securities law, protecting investors refers to preventing practices intended to mislead by artificially affecting market activity.³⁸ The FERC and its OE focus on preventing manipulations that intentionally affect markets of FERC-regulated energy industries.

IV. EXAMPLES OF PSLRA FACTS IDENTIFYING *SCIENTER* FOR ENERGY LAW ENFORCEMENT

To succeed under the PSLRA, private parties must plead “with particularity facts [that] giv[e] rise to a strong inference that [a] defendant acted with the required state of mind.”³⁹ That heightened pleading standard, however, did not change the substantive standard of proof to be met, or the kind of evidence to be adduced to demonstrate *scienter* at trial in a securities fraud case.⁴⁰ PSLRA decisions can help identify, by analogy, facts for a showing of *scienter* under

35. OFFICE OF ENFORCEMENT REPORT, *supra* note 14, at 9 (“The [FERC] modeled its anti-manipulation rule after SEC Rule 10b-5 . . . to utilize the decades of precedent in securities litigation and adapt those precedents to the prohibition of market manipulation in wholesale natural gas and electricity markets, assisting market participants in understanding what is expected of them in their market dealings.”).

36. Order No. 670, *supra* note 4, at PP 2, 45.

37. *Id.* at PP 30-31 & n.56, 41-42, 52-53.

38. *Santa Fe Indus. v. Green*, 430 U.S. 462, 471-77 (1977); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197-215 (1976).

39. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S.Ct. 2499, 2504-05 (2007) (citing 15 U.S.C. § 78u-4b(2) (2000)). The PSLRA pleading standard applies to private party complaints, not administrative agencies. *SEC v. Collins & Aikman Corp.*, 524 F. Supp. 2d 477, 487 (S.D.N.Y. 2007) (“[T]he PSLRA does not apply to actions brought by the SEC”); accord Allan Horwich, *Warnings to the Unwary: Multi-Jurisdictional Federal Enforcement of Manipulation and Deception in the Energy Markets After the Energy Policy Act of 2005*, 27 ENERGY L.J. 363, 387-88 (2006); J. Michel Marcoux, *Proving Intent to Manipulate Markets*, 144 PUB. UTIL. FORT., No. 5, 19-23 (May 2006). Moreover, Order No. 670 explains that, while “cases arising in the context of private litigation may be instructive on certain points,” such as securities industry *scienter*, “elements needed for a private right of action are not the same as those required for [FERC] enforcement.” *Prohibition of Energy Market Manipulation*, F.E.R.C. STATS. & REGS. ¶ 31,202, 71 Fed. Reg. 4,244 at PP 48-49 & nn.100-01 (2006).

40. *Phillips v. LCI Int'l, Inc.*, 190 F.3d 609, 620 (4th Cir. 1999); *In re Comshare, Inc. Sec. Litig.*, 183 F.3d 542, 549-50 & n.5 (6th Cir. 1999). The PSLRA did not generally alter the substance of the *scienter* requirement for Exchange Act § 10(b) and SEC Rule 10b-5 claims. *Central Laborers' Pension Fund v. Integrated Elec. Serv.*, 497 F.3d 546, 551 (5th Cir. 2007). Substantive *scienter* analysis is the same in SEC as in PSLRA cases. See, e.g., *In re Disraeli*, 2007 SEC LEXIS 3015, at *16-20 (Dec. 21, 2007) (lending oneself securities offering proceeds “to pay for the release of a personal tax lien” and other personal expenses is a reckless, extreme departure from the standards of ordinary care when investors were informed the proceeds would be used for business purposes); *In re Doty, Jr.*, 2007 SEC LEXIS 2318, at *14-16 (Sept. 28, 2007) (“Respondent was one of Dynegey’s senior reporting officials Doty signed Dynegey’s 2001 Form 10-K, which misstated [a highly complex transaction’s] impact on Dynegey’s financial statements. Because of Respondent’s failure to ensure appropriate accounting treatment and failure to disclose the financing transactions . . . Dynegey’s financial performance was materially misstated.”).

energy laws.⁴¹ Because the EAct 2005 and the FERC's implementing regulations allow for no comparable private party right of action enforcing energy laws,⁴² PSLRA decisions are that much more serviceable to the practitioner.

PSLRA complaints brought pursuant to Exchange Act § 10(b) and SEC Rule 10b-5 must be considered in their entirety, while taking plausible opposing inferences into account.⁴³ Federal courts issue many PSLRA decisions each year. Such "actions continue to represent almost half of all class actions pending in federal court."⁴⁴ Securities industry law focuses on financial information disclosed to those whom Courts assume are largely less informed retail investors. That focus differs from energy industry commodity transactions, which are often bi-lateral, involving comparatively sophisticated wholesale customers. The securities markets also differ from largely cost-based, just-and-reasonable rate, regulated gas transportation and electricity transmission wholesale markets. The FERC intends to recognize such consequential differences by appropriately adapting securities precedents on a case-by-case basis to specific energy industry situations.⁴⁵ So will energy industry participants.⁴⁶

Application of PSLRA case facts to particular energy industry litigations would require focus not attempted here. These are recent, sample PSLRA precedents on whether or not a *scienter* claim is stated, answering anecdotally several related questions: Do motive and opportunity exist to affect markets? Are facts of either conscious misbehavior or recklessness present? Is only negligence or gross negligence involved? Are fraudulent reports, filings, or forms⁴⁷ implicated? There are very many other PSLRA intent decisions besides

41. Order No. 670, *supra* note 4, at PP 7, 31 & n.56, 49, 52. *Cf.*, Order Denying Rehearing, *Amaranth Advisors, L.L.C.*, 121 F.E.R.C. ¶ 61,224 at PP 17 n.39, 35 n.88 (The FERC was guided by PSLRA case, non-*scienter* precedents in *In re Lernout & Haupsie Sec. Litig.*, 236 F. Supp. 2d 161, 173 (D. Mass. 2003) and in *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472, 491, 505-06 (S.D.N.Y. 2005)).

42. 18 C.F.R. §§ 1c.1(b), 1c.2(b) (2007).

43. *Tellabs*, 127 S.Ct. at 2508-10.

44. Kathleen L. Casey, Comm'r, SEC, Address to the Inst. for Legal Reform's Annual Reform Summit (Oct. 24, 2007); accord John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 COLUM. L. REV. 1534, 1539-40 (2006).

45. Order No. 670, *supra* note 4, at P 31.

46. Commodity futures trading industry participants are doing likewise in their industry. Amaranth defendants argued that the *Tellabs* ruling on the PSLRA heightened *scienter* pleading standard in the securities industry supplies "direction" to and "logic" for pleading their alleged intent in their industry by the U.S. Commodity Futures Trading Commission in the U.S. Second Circuit. Mem. of Law in Support of Motion to Dismiss by Def.'s Amaranth Advisors L.L.C. & Amaranth Advisors (Calgary) ULC at 18, CFTC v. Amaranth Advisors, L.L.C., No. 1-07-cv-06682-DC (S.D.N.Y. Nov. 8, 2007), and also Def. Brian Hunter's Mem. of Law in Support of His Motion to Dismiss the Compl. at 18 & n.19, CFTC v. Amaranth Advisors, L.L.C., No. 1-07-cv-06682-DC (S.D.N.Y. Nov. 8, 2007).

47. See generally Order No. 704, *Transparency Provisions of Section 23 of the Natural Gas Act*, F.E.R.C. STATS. & REGS. ¶ 31,260 at PP 91, 114 (2007), 73 Fed. Reg. 1,014 (2008) (to be codified at 18 C.F.R. pts. 260, 284, 385) (wholesale natural gas market participant information is necessary to monitor for and police against market manipulation, and any FERC enforcement efforts will focus on instances of intentional submission of false, incomplete, or misleading information to the Commission, of failure to report in the first instance, or of failure to exercise due diligence in compiling and reporting data); Notice of Proposed Rulemaking, *Pipeline Posting Requirements Under Section 23 of the Natural Gas Act*, F.E.R.C. STATS. & REGS. ¶ 32,626 at P 63, 73 Fed. Reg. 1,116 (2008) (proposed daily electronic bulletin board postings by non-

these recent samples. The federal courts issue more regularly.⁴⁸ The purpose here is not at all to compile a comprehensive treatise, but to indicate a less than familiar source of authority to help practitioners identify *scienter* presence or absence. These decisions reveal the aptness of this kind of precedent. It must be considered, given the energy law market manipulation prohibition now patterned on securities law, the indispensable function of private securities litigation to deter fraud, and the FERC's substantial EAct 2005 penalty authority.

A. *Do motive and opportunity exist to affect markets?*

Securities law *scienter* allegations can be supported by facts showing motive, defined as concrete benefits to the violator, when combined with facts showing opportunity, defined as means or prospect to achieve such concrete benefits.⁴⁹

1. Facts supporting *scienter*

Motive can be pleaded with facts of fraudulent concealment of uncollectible receivables to drive up stock share demand, causing share distribution of proceeds to corporate officers and an audit committee.⁵⁰ Opportunity is alleged by facts of officers' involvement in preparing financial statements to hide a corporation's loans of money to itself through third parties.⁵¹ *Scienter* can be pleaded based on motive and opportunity of corporate defendants to make short-term profits at the expense of unsuspecting investors by systematically originating and quickly consummating large volumes of defective loans, despite signs of borrowers' lack of creditworthiness.⁵² A financing agreement's structure furnishes heightened motive and opportunity by putting an investment company in position to profit from selling short another company's stock in a declining market, due to the investment company's ability to obtain additional common stock shares of the other company cheaply.⁵³ A person's company position may be a circumstance combined with other facts to show intent to trade on inside information, when the information to be imputed to the person is of great importance to the company, such as Philadelphia Stock Exchange

interstate pipelines of capacity and volume of natural gas flows would allow the FERC and other market observers to identify and remedy potentially manipulative activity more actively).

48. These recent, sample PSLRA decisions were researched through Mar. 6, 2008. Stanford Law School and Cornerstone Research gather data on financial and economic characteristics of securities fraud class action litigation in their Securities Class Action Clearinghouse (<http://securities.stanford.edu>), indexing some 2,646 issuers named in federal class action securities fraud lawsuits post-PSLRA, and publishing annual reports. See, e.g., CORNERSTONE RESEARCH, SECURITIES CLASS ACTION CASE FILINGS 2007: A YEAR IN REVIEW (2008), http://securities.stanford.edu/clearinghouse_research/2007_YIR/20080103-01.pdf.

49. Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of America Sec., 446 F. Supp. 2d 163, 180-81 (S.D.N.Y. 2006); *In re Dynex Capital, Inc. Sec. Litig.*, 05 Civ. 1897 (HB), 2006 U.S. Dist. LEXIS 4988, *6-7, *25-29 (S.D.N.Y. Feb. 10, 2006); see also *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S.Ct. 2499, 2511 (2007) (holding that motive can be a relevant consideration).

50. *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 646-47, 654-55 (S.D.N.Y. 2007).

51. *Id.* at 647-48.

52. *Dynex*, 2006 U.S. Dist. LEXIS 4988, at *29-32.

53. *Pet Quarters, Inc. v. Badian*, No. 4:04-CV-697 (RSW), 2007 U.S. Dist. LEXIS 24611, at *21 (E.D. Ark. Mar. 30, 2007).

Governing Board membership when the information was the complete sale of the Exchange for a substantial price.⁵⁴

2. *Scienter* unsupported

Intent is not shown, however, by alleging only generalized motives common to all business corporations and persons,⁵⁵ such as motive to make a company appear stable and successful,⁵⁶ or to reduce costs,⁵⁷ or to arrange corporate financing,⁵⁸ or to appear profitable, including a desire to keep the stock price high to increase compensation to corporate officers.⁵⁹ As a precedent likely transferable to energy industries, establishing merely that a person holds a position in the corporate hierarchy does not plead intent.⁶⁰ Proximate resignations or replacements of high-ranking officers or directors do not alone support *scienter*.⁶¹ Nor do illogical motives do so, such as those defying economic reason and making little sense. For example, an alleged motive does not suffice for lenders, or their affiliates attempting to benefit them, to throw billions of good dollars after bad, hoping their investments profitably could be propped up by concealing a massive fraud *ad infinitum*.⁶² Intent is not pleaded adequately by failing to link the declarant of a challenged statement with facts that might contradict the statement.⁶³ Specific, underlying facts must be shown.⁶⁴

B. Are facts of either conscious misbehavior or recklessness present?

Scienter allegations can be supported, independently of motive and opportunity, by facts of conscious misbehavior or recklessness.⁶⁵

1. Supporting *scienter*

Conscious misbehavior or recklessness is alleged by failure to review information the violator had a duty to monitor, by ignoring obvious signs of fraud, by knowledge of facts or access to information contradicting public

54. *Feinberg v. Benton*, No. 05-4847, 2007 U.S. Dist. LEXIS 91561, at *18-20 (E.D. Pa. Dec. 13, 2007).

55. *In re Intelligroup Sec. Litig.*, 527 F. Supp. 2d 262, 340-42 (D.N.J. 2007).

56. *Andropolis v. Red Robin Gourmet Burgers*, 505 F. Supp. 2d 662, 678 (D. Colo. 2007).

57. *In re GeoPharma, Inc. Sec. Litig.*, 411 F. Supp. 2d 434, 443-44 (S.D.N.Y. 2006).

58. *Commc'ns Workers v. CSK Auto Corp.*, No. CV06-1503-PHX-DGC, 2007 U.S. Dist. LEXIS 22782, at *25-26 (D. Ariz. Mar. 28, 2007).

59. *In re Career Educ. Corp. Sec. Litig.*, 03 C 8884, 2007 U.S. Dist. LEXIS 23635, at *29-32 (N.D. Ill. Mar. 29, 2007); *Malin v. XL Capital Ltd.*, 499 F. Supp. 2d 117, 158-59 (D. Conn. 2007).

60. *Career Educ. Corp.*, 2007 U.S. Dist. LEXIS 23635, at *28; *Frank v. Dana Corp.*, 525 F. Supp. 2d 922, 930 (N.D. Ohio 2007).

61. *In re Impax Labs. Sec. Litig.*, No. C 04-04802 JW, 2007 U.S. Dist. LEXIS 52356, at *27 (N.D. Cal. July 18, 2007).

62. *In re Adelpia Commc'ns Corp. Sec. & Derivative Litig.*, 03 MD 1529(LMM), 2007 U.S. Dist. LEXIS 66911, at *11-12 (S.D.N.Y. Sept. 7, 2007).

63. *Winer Family Trust v. Queen*, 503 F.3d 319, 332 (3d Cir. 2007); *Intrepid Global Imaging 3D, Inc. v. Athayde*, No. 3:07-cv-1106-J-33HTS, 2007 U.S. Dist. LEXIS 94786, at *13-18 (M.D. Fla. Dec. 13, 2007).

64. *Nicholson v. N-Viro Int'l Corp.*, 3:06CV01669, 2007 U.S. Dist. LEXIS 76522, at *22-25 (N.D. Ohio Oct. 12, 2007).

65. Every U.S. Court of Appeals considering whether reckless behavior is sufficient for civil liability in the securities industry has held that plaintiffs may meet the *scienter* requirement by showing defendants acted intentionally or recklessly. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S.Ct. 2499, 2507 & n.3 (2007).

statements, or by purposeful failure to follow announced company policy.⁶⁶ Conscious misconduct is pleaded by circumstances of deliberate illegal behavior, while recklessness is alleged with facts of highly unreasonable conduct, departing extremely from standards of ordinary care, with the harm either known or so obvious that the violator must have been aware of it.⁶⁷

Recklessness allegations can suffice when based on facts of substantial transaction size, recurrent nature, and obvious lack of business purpose, together with dereliction in the responsibilities of the corporate secretary/controller, chief financial officer, and general counsel (but not the global marketing vice president, chief operating officer, or audit committee).⁶⁸ Alleged systematic disregard for borrowers' non-creditworthiness, in order to complete large loan volumes while ignoring signs of defective bond collateral, pleads recklessness.⁶⁹

Recklessness also is alleged by facts that analysts issued securities recommendations contrary to their true evaluations, or had conflicts of interest, and also when the corporation should have known its research reports misrepresented material facts.⁷⁰ Recklessness is pleaded by testimony that financial reporting systems were in such poor condition that unprocessed claims could not be tracked properly, and the person in charge of maintaining those systems in the U.S. had been dismissed in connection with those failures.⁷¹ The chairman, publisher, and executive vice president for circulation of *The Dallas Morning News* allegedly were severely reckless in not knowing circulation was overstated significantly, unearned revenue was being recognized, and overstated circulation figures were inflating financial reports to investors and the market.⁷²

2. *Scienter* unsupported

To the contrary, reliance only on circumstantial facts of defendants' fairly intimate knowledge of relevant transactions, without pleading any misleading statement or omission, shows no *scienter*.⁷³ Recklessness is not pleaded when plaintiffs do not show that outside auditor accounting practices were so deficient that the audit amounted to no audit at all, or that judgments made were ones that no reasonable accountant would have made if confronted with the same facts.⁷⁴ Nor is recklessness alleged for failure to correct errors in a tender offer evaluation, independently conducted by an investment bank whose assumptions and methodologies were not under defendants' direct control, and independently

66. *Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of America Sec.*, 446 F. Supp. 2d 163, 181-82 (S.D.N.Y. 2006); *In re Scottish Re Group Sec. Litig.*, 524 F. Supp. 2d 370, 393-94 (S.D.N.Y. 2007).

67. *Pension*, 446 F. Supp. 2d at 181-83.

68. *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 648-52 (S.D.N.Y. 2007).

69. *In re Dynex Capital, Inc. Sec. Litig.*, 05 Civ. 1897 (HB), 2006 U.S. Dist. LEXIS 4988, at *31-32 (S.D.N.Y. Feb. 10, 2006).

70. *Lapin v. Goldman Sachs Group*, 506 F. Supp. 2d 221, 241-42 (S.D.N.Y. 2007).

71. *Scottish Re Group Sec. Litig.*, 524 F. Supp. 2d at 394-95.

72. *Fener v. Belo Corp.*, 513 F. Supp. 2d 733, 736-37, 741-42 (N.D. Tex. 2007); *Fener v. Belo Corp.*, No. 3:04-CV-1836-D, 2007 U.S. Dist. LEXIS 86646, at *4-8 (N.D. Tex. Nov. 26, 2007).

73. *Teachers' Ret. Sys. of La. v. Hunter*, 477 F.3d 162, 184 (4th Cir. 2007).

74. *In re Williams Sec. Litig.*, 496 F. Supp. 2d 1195, 1288 (N.D. Okla. 2007).

supervised by a special committee.⁷⁵ Corporate officer Sarbanes-Oxley Act certification does not infer intent unless the certification is linked with “actual accounting and reporting problems,” i.e., that internal information controls were inadequate on the certification date.⁷⁶ Fraud by hindsight may not be pleaded when the violation is based only on what later occurred, such as “intent to break a promise already made.”⁷⁷ Facts must be pleaded to support a finding that a gas well developer in Texas knowingly misstated or omitted material facts at the time it made representations in connection with a promissory note to secure investment in the project.⁷⁸ Nor is there *scienter*, such “as knowing of or closing one’s eyes to a known ‘danger,’ or participating in [a] fraud,” when an investment advisor fails to conduct a promised, “uniquely comprehensive brand of due diligence” investigation before recommending an investment.⁷⁹ Without detailed descriptions of job particulars, individual responsibilities, and employment dates for confidential source witnesses, such witnesses’ statements are of no value as intent.⁸⁰ Absent allegations of personal enrichment from college bond sale proceeds, or of particular sophistication in securities transactions, non-profit educational institution officers, administrators, and trustees have different characteristics from corporate insiders standing to profit from sales of artificially inflated securities, making it more difficult to infer a high degree of recklessness or intent to defraud.⁸¹

C. Is only negligence or gross negligence involved?

Mistakes due to negligence or even gross negligence do not qualify as *scienter*.⁸²

1. Supporting *scienter*

Scienter is alleged that a financial services company made false assurances of its underwriting standards integrity because the company serviced the collateral, with responsibility to review delinquencies and know of day-to-day violations.⁸³ Facts of an affiliate’s functions to issue certificates, supposedly secured by sales contracts and mortgage loans that were of low quality, and to file SEC reports on such collateral, plead intent.⁸⁴ Corporate lack of disclosure of loan guarantee financing arrangements when associated risky financial

75. Stark Trading & Shepherd Inv. Int’l Ltd. v. Falconbridge, Ltd., No. 05-C-1167, 2008 U.S. Dist. LEXIS 2677, at *25-27 (E.D. Wis. Jan. 14, 2008).

76. Central Laborers’ Pension Fund v. Integrated Elec. Serv. Inc., 497 F.3d 546, 554-55 (5th Cir. 2007).

77. Rodriguez-Ortiz v. Margo Caribe, Inc., 490 F.3d 92, 97-98 (1st Cir. 2007); *In re Winn-Dixie Stores, Inc. Sec. Litig.*, 3:04-CV-71-J-33MCR, 2007 U.S. Dist. LEXIS 89266, at *44-45 (M.D. Fla. Dec. 4, 2007).

78. Galvin v. McCarthy, No. 07-cv-00885-EWN-BNB, 2008 U.S. Dist. LEXIS 15718, at *24-26 (D. Colo. Feb. 29, 2008).

79. *In re Bayou Hedge Fund Litig.*, 06-MDL-1755 (CM), 06-CV-2943 (CM), 2007 U.S. Dist. LEXIS 59145, at *32-36 (S.D.N.Y. July 31, 2007).

80. *Central Laborers’*, 497 F.3d at 552.

81. *ACA Fin. Guar. Corp. v. Advest, Inc.*, 512 F.3d 46, 66-67 (1st Cir. 2008).

82. *In re GeoPharma, Inc. Sec. Litig.*, 411 F. Supp. 2d 434, 437 & n.4 (S.D.N.Y. 2006).

83. *Teamsters Local 445 Freight Div. Pension Fund v. Bombardier, Inc.*, 05 Civ 1898 (SAS), 2005 U.S. Dist. LEXIS 19506, at *61-63 (S.D.N.Y. Sept. 6, 2005).

84. *Id.* at *62-65.

conditions are known,⁸⁵ as well as knowingly false corporate officer statements when insider sales are dramatically out of line with prior trading practices, and made at suspicious times of unexpected job resignations and during SEC investigation of insider trading,⁸⁶ allege intent.

2. *Scienter* unsupported

Claims that individuals lack education or training to make financial decisions or to set up internal inventory valuation controls may establish corporate mismanagement or negligence at most, but not intent under securities law.⁸⁷ While corporate compensation committee member approvals of backdated stock options may have been negligent, particularly alleged failures to recognize or pursue warning signs, including signing incorrect financial statements, such facts are insufficient without more.⁸⁸ Only an inference of negligence, not *scienter*, arises when plaintiffs show that accountants failed to investigate whether a bank had too many problem loans and insufficient reserves, or from a showing of relatively small loan collection fee increases or of state regulatory action not hidden but disclosed in an SEC Form 10-K.⁸⁹ An outside auditor's choice of the wrong joint venture accounting method does not show by itself that the alleged violation amounted to more than mere negligence, and thus no *scienter* is pleaded.⁹⁰ “[U]nwise business and management decisions,” even if considered collectively, fail to give rise to *scienter*.⁹¹

D. Are fraudulent reports, filings, or forms implicated?

Documents should be executed truthfully and carefully, as a matter of course.

1. Supporting *scienter*

Scienter is pleaded when an attorney allegedly knew of fabricated descriptions of investment performance and of other facts omitted from a securities brochure given to investors, and when the attorney's law firm assertedly took actions, including tactics at the SEC, “to conceal its role in the [securities] scheme.”⁹² Claims of telecommunications company overstatement of new customer line counts are particular as to showing intent to inflate the

85. *In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 433, 456-57 (S.D.N.Y. 2005).

86. *In re Nash Finch Co. Sec. Litig.*, 502 F. Supp. 2d 861, 882-83 (D. Minn. 2007).

87. *In re Silicon Storage Tech. Sec. Litig.*, No. C-05-0295 PJH, 2007 U.S. Dist. LEXIS 21953, at *82-84 (N.D. Cal. Mar. 9, 2007). Nor is Order No. 670 “intended to regulate negligent practices or corporate mismanagement . . .” Order No. 670, *supra* note 4, at P 5.

88. *In re Mercury Interactive Corp. Sec. Litig.*, No. C 05-3395 JF (PVT), 2007 U.S. Dist. LEXIS 59171, at *35-36 (N.D. Cal. July 30, 2007).

89. *Lewis v. Straka*, No. 05C1008, 2007 U.S. Dist. LEXIS 59054, at *5-6, *10-11 (E.D. Wis. Aug. 13, 2007).

90. *In re Nat'l Century Fin. Enter. Inc. Fin. Inv. Litig.*, No. 2:03-md-1565, 2007 U.S. Dist. LEXIS 59087, at *28-29 (S.D. Ohio Aug. 13, 2007); *accord In re Scottish Re Group Sec. Litig.*, 524 F. Supp. 2d 370, 398 (S.D.N.Y. 2007).

91. *In re Loudeye Corp. Sec. Litig.*, No. C06-1442MJP, 2007 U.S. Dist. LEXIS 60624, at *23 (W.D. Wash. Aug. 17, 2007).

92. *Cliff v. Hyman Lippitt, P.C.*, No. 05-72221, 2005 U.S. Dist. LEXIS 38144, at *10, *21-22, *27-29 (E.D. Mich. Dec. 29, 2005).

company's growth statistics publicly reported in press releases and financial statements filed with the SEC.⁹³ *Scienter* also is alleged for accounting entry fraud when a corporate official signed an SEC annual report while knowing the form was based incorrectly on a cancelled \$1,200,000 purchase.⁹⁴ Intent is alleged with facts that a chief executive officer and a chief financial officer, who oversaw, supervised, and controlled the options-granting process, approved backdated, bogus stock option grant documents.⁹⁵ Corporate officers allegedly had *scienter* in signing SEC filings containing misrepresentations while failing to learn of financial risk,⁹⁶ or in SEC Form 10-K certification by a senior manager, known within the company as the "guardian" of the spyware secret, that spyware was not relied on for any purpose.⁹⁷ While allegations of Generally Accepted Accounting Principles (GAAP) violations alone cannot support claimed securities fraud, the claim is sustainable when coupled with SEC Form 10-K statements failing to disclose a tax evasion scheme to move income from higher-tax to lower-tax jurisdictions.⁹⁸ Significant GAAP violations can make a powerful, indirect showing of *scienter*.⁹⁹ There is no legal requirement that a vice president of finance/chief financial officer, alleged to have committed securities fraud through accounting errors and financial restatements, has profited personally by his own conduct.¹⁰⁰ Failure to correct earlier, subsequently false, written certifications that no notice had been received of any pending, threatened, or intended governmental entity investigation or review of a gaming business showed intent to walk away from a faltering deal with \$5,000,000 rather than nothing.¹⁰¹

2. *Scienter* unsupported

Individual certifications of quarterly and annual report accuracy, required of all corporate officers and directors, say nothing about intent without also pleading reason to know of misleading statements in such reports.¹⁰² Internal financial reports contradicting sales growth statements do not plead *scienter* absent allegations that corporate officers saw the reports.¹⁰³ Intent to deceive by

93. *In re Adelphia Commc'ns Corp. Sec. and Derivative Litig.*, 398 F. Supp. 2d 244, 249-52 (S.D.N.Y. 2005).

94. *Wojtunik v. Kealy*, 394 F. Supp. 2d 1149, 1167-69 (D. Ariz. 2005).

95. *In re Zoran Corp. Derivative Litig.*, 511 F. Supp. 2d 986, 1013-14 (N.D. Cal. 2007).

96. *In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 433, 459-60 (S.D.N.Y. 2005). Various SEC filings touting the expected, long-term employment of top executives, when their significant tax problems placed their employment in serious doubt, inferred *scienter*. *New Jersey v. Sprint Corp.*, No. 03-2071-JWL, 2008 U.S. Dist. LEXIS 5277, at *28-30 (D. Kan. Jan. 23, 2008).

97. *In re Miva, Inc. Sec. Litig.*, No. 2:05-cv-201-FtM-29DNF, 2008 U.S. Dist. LEXIS 11631, at *21-22 (M.D. Fla. Feb. 15, 2008).

98. *In re Tommy Hilfiger Sec. Litig.*, No. 04-civ-7678, 2007 U.S. Dist. LEXIS 55088, at *2-3, *10-11 (S.D.N.Y. July 20, 2007).

99. *In re Impax Labs. Sec. Litig.*, No. C 04-04802 JW, 2007 U.S. Dist. LEXIS 52356, at *24 (N.D. Cal. July 18, 2007).

100. *In re Proquest Sec. Litig.*, 527 F. Supp. 2d 728, 733, 741 (E.D. Mich. 2007).

101. *CP St. Louis Casino, LLC v. Casino Queen, Inc.*, No. 07-cv-447-JPG, 2008 U.S. Dist. LEXIS 11469, at *11-12 (S.D. Ill. Feb. 15, 2008).

102. *In re United Am. Healthcare Corp. Sec. Litig.*, No. 2:05-CV-72112 (LPZ/RSW), 2007 U.S. Dist. LEXIS 6362, at *51-53 (E.D. Mich. Jan. 30, 2007).

103. *Selbst v. McDonald's Corp.*, 432 F. Supp. 2d 777, 780, 786-87 (N.D. Ill. 2006).

releasing incorrect financial reports is not shown when corporate tax accounting controls are disclosed repeatedly, independent third-party help is hired, and previous financial results are restated after investigation.¹⁰⁴ Broad, conclusory allegations of false and misleading initial public offering prospectuses are insufficient.¹⁰⁵ Nor is there intent when there is no obvious duty to disclose. For example, omitting detailed data from a press release about government approval of a prescription drug product does not support intent.¹⁰⁶ Failure to disclose informal and advisory Food and Drug Administration warning letters does not show *scienter*.¹⁰⁷ Companies have no duty to accuse themselves of wrongdoing, or to announce to the public their belief they are engaged in illegal activities, in their press releases or published articles.¹⁰⁸ The greater the time elapsed between an assertedly fraudulent statement or omission in a press release and a later disclosure of inconsistent information, the more intent allegations weaken.¹⁰⁹ Document background and specific references within documents are required, or documents are ineffective to show intent, such as purchase/sell orders failing to allege *scienter* to discriminate against customers by a stock options specialist and its clearinghouse.¹¹⁰

V. CONCLUSION

Congress explicitly has patterned the EAct 2005 prohibition of energy market manipulation and fraud on existing federal securities law prohibition of securities market manipulation and fraud. The burgeoning body of private securities litigation federal court decisions, according to the U.S. Supreme Court, functions as an indispensable tool to deter manipulation and fraud. Finally, no *scienter*, no violation. For those adequate reasons, PSLRA precedents are instructive and useful to FERC practitioners on the *scienter* requirement in FERC manipulation and fraud prosecutions.

Order No. 670 states the FERC's belief that it would be illogical simply to ignore the decades of useful guidance securities precedents can offer. The substantial body of PSLRA decision facts can guide FERC policy to apply *scienter* to its enforcements, just as *scienter* applies to SEC Rule 10b-5 enforcements. PSLRA decision facts work as do canaries in coal mines, helping the FERC, with its substantial new penalty powers at hand, and its OE to abstain from insufficient, vague, or conclusory allegations, and aiding other energy industry participants to forgo at least those behaviors determined previously for securities industry markets to signify intent to manipulate or defraud.

104. *In re H&R Block Sec. Litig.*, No. 06-0236-CV-W-ODS, 2008 U.S. Dist. LEXIS 12122, at *21 (W.D. Mo. Feb. 19, 2008).

105. *Miller v. Lazard, Ltd.*, 473 F. Supp. 2d 571, 588-90 (S.D.N.Y. 2007).

106. *In re GeoPharma, Inc. Sec. Litig.*, 411 F. Supp. 2d 434, 446-48 (S.D.N.Y. 2006).

107. *In re Boston Scientific Corp. Sec. Litig.*, 490 F. Supp. 2d 142, 161 (D. Mass. 2007).

108. *Indiana State Dist. Council of Laborers & Hod Carriers Pension & Welfare Fund v. Omnicare, Inc.*, 527 F. Supp. 2d 698, 709-10 (E.D. Ky. 2007).

109. *In re NVE Corp. Sec. Litig.*, No. 06-574, 2007 U.S. Dist. LEXIS 49137, at *4, *31-34 (D. Minn. July 3, 2007).

110. *Gurfein v. Ameritrade, Inc.*, 411 F. Supp. 2d 416, 425-26 (S.D.N.Y. 2006).