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955 Jefferson Avenue
Valley Forge Corporate Center
Norristown, PA 19403-2497

Vincent P. Duane
Vice President and General Counsel
610.666.4367
610.666.4281 FAX
duanev@pjm.com

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**Received CFTC
Records Section**

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COMMENT

David A. Stawick
Secretary
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Notice of Intent To Undertake a Determination Whether Certain PJM Contracts Offered for Trading on the IntercontinentalExchange, Inc., Perform Significant Price Discovery Functions

Dear Mr. Stawick:

PJM Interconnection, L.L.C. ("PJM") respectfully submits the following comments in response to the U.S. Commodity Futures Trading Commission's (the "Commission") Notice of Intent, Pursuant to the Authority in Section 2(h)(7) of the Commodity Exchange Act ("CEA") and Commission Rule 36.3(c)(3), to Undertake a Determination Whether the PJM WH Real Time Peak Daily Contract; PJM WH Real Time Peak Contract; PJM WH Real Time Off-Peak Contract; PJM WH Day Ahead LMP Peak Daily Contract; and PJM WH Real Time Off-Peak Daily Contract Offered For Trading on the IntercontinentalExchange, Inc. (collectively, the "ICE Contracts"), Perform Significant Price Discovery Functions.¹ PJM's comments apply to each of the five contracts included in Commission's Notice of Intent.

I. PJM'S PRODUCTS AND MEMBERS

PJM is a Regional Transmission Organization ("RTO") approved by the Federal Energy Regulatory Commission ("FERC") to coordinate the transmission of wholesale electricity in all or parts of 13 states and the District of Columbia.² PJM currently has approximately 550 members, including transmission owners, load serving entities, generation owners, electric distributors, end-use commercial and industrial customers, and other suppliers (e.g., power marketers), among others.

¹ Notice of Intent, Pursuant to the Authority in Section 2(h)(7) of the Commodity Exchange Act and Commission Rule 36.3(c)(3), to Undertake a Determination Whether the PJM WH Real Time Peak Daily Contract, PJM WH Real Time Peak Contract, PJM WH Real Time Off-Peak Contract, PJM WH Day Ahead LMP Peak Daily Contract, and PJM WH Real Time Off-Peak Daily Contract, Offered for Trading on the IntercontinentalExchange, Inc., Perform Significant Price Discovery Functions, 74 Fed. Reg. 54,966, 54,969 (Oct. 26, 2009) (the "Notice of Intent").

² *Pennsylvania-New Jersey-Maryland Interconnection*, 81 FERC ¶ 61,252 (1997), *reh'g denied*, 92 FERC ¶ 61,282 (2000); *PJM Interconnection, L.L.C.*, 101 FERC ¶ 61,345 (2002); *PJM Interconnection, L.L.C.*, 81 FERC ¶ 61,257 (1997), and *PJM Interconnection L.L.C.*, 96 FERC ¶ 61,061 (2001), order on compliance filing, 98 FERC ¶ 61,072 (2002). See also *Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 31,089 (1999), *order on reh'g*. Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092 (2000), *aff'd sub nom, Pub. Util. Dist. No. 1 v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

PJM began operating a wholesale electricity spot market in 1997, pursuant to FERC's Order No. 888, which introduced independent operation of the grid as a policy initiative to "meet the demands of the competitive marketplace."³ PJM administers auctions and markets that provide for the purchase and sale of energy and energy-related products and services, including short- and long-term transmission rights products, a day-ahead (spot) energy market, a real-time (day of/spot) energy market, a capacity market, and several ancillary services markets.

PJM's electricity markets establish wholesale prices for electricity through the use of Locational Marginal Pricing ("LMP"). The LMP construct allows prices to reflect the actual, real-time cost of providing electricity to specific locations or "nodes" throughout the PJM system. Location-specific, real-time price signals improve the efficiency of the PJM wholesale electricity markets by allocating resources economically and encouraging an appropriate level of conservation and new development of electricity generation and transmission resources.⁴ The LMP construct additionally sends price signals to both supply and demand side participants to encourage response in a manner that most efficiently ensures the continued reliable operation of the power grid. LMPs also are essential components of the five contracts included in Commission's Notice of Intent.

II. PJM'S COMMENTS

PJM appreciates the opportunity to comment in connection with the Commission's determination as to whether the ICE Contracts perform significant price discovery functions. Although PJM takes no position as to whether the ICE Contracts should be regulated as significant price discovery contracts, PJM believes that two fundamental attributes of its LMP-based products and markets will inform the Commission in making the threshold determination as to whether the ICE Contracts perform a significant price discovery function.

A. LMPs Represent Prices in the Spot Market

PJM operates day-ahead and real-time electricity markets. The day-ahead market is a forward market in which hourly LMPs are calculated for the next operating day based on generation offers, demand bids and scheduled bilateral transactions. The real-time market is a spot market in which current LMPs are calculated at five-minute intervals based on actual grid operating conditions. The day-ahead and real-time electricity markets are spot markets within the meaning of the CEA because all transactions clear and settle within two days of execution.

B. LMPs Represent Actual Supply and Demand in the Physical Energy Market

LMPs reflect the value of electricity at the specific location and time of delivery. As the Commission correctly describes in its Notice of Intent, each LMP has three components: the marginal cost

³ *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 FR 21540 (May 10, 1996), FERC Stats. & Regs. ¶ 31,036 (1996), *order on reh'g*, Order No. 888-A, 62 FR 12274 (Mar. 14, 1997), FERC Stats. & Regs. ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002).

⁴ *See generally Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 31,089 (1999), *order on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092 (2000) ("Order 2000").

of energy, marginal losses, and marginal congestion costs.⁵ In practice, this means that if the lowest-priced electricity can reach all locations without impediment, the price of electricity will be the same across the entire grid, taking account for losses that are attendant to the physics of moving electrons over longer distances (marginal losses). If, however, a transmission constraint system outage, or other physical limitation of the PJM system prevents electricity from flowing freely to certain areas (*i.e.*, congestion), more-expensive electricity must be dispatched to meet demand located behind the constraint. As a result, LMPs will be higher in those physically constrained locations.

Stated broadly, the price of electricity in the PJM LMP-based markets is determined by (i) actual physical conditions affecting supply (such as outages or deratings of generation and transmission facilities) and demand (driven significantly by weather) and (ii) market based offers made by sellers in PJM's markets. Bilateral trading activity, including financial transactions undertaken in over the counter environments would appear to have, at best attenuated and more likely, no impact on LMP outcomes. LMPs instead are driven by actual physical conditions affecting PJM's ability to dispatch generation to meet needed demand.

In other words, the ICE Contracts do not determine LMPs in PJM's day-ahead and real-time electricity markets. Rather, the prices of the ICE Contracts are driven by prices in PJM's LMP-based markets.

Finally, it should be noted that the processes (broadly described above) that contribute to the forming of LMPs are subject to exhaustive regulatory oversight by the FERC and are filed by PJM with that agency in the form of a tariff. Moreover, LMP outcomes are subject to a "just and reasonableness" standard under the Federal Power Act wherein prices must be free from the exercise of market power and market manipulation. PJM's markets are overseen by extensive and independent market monitoring and by the FERC's oversight, investigation and enforcement resources.

III. CONCLUSION

PJM respectfully requests that the Commission consider its comments in connection with the determination as to whether the ICE Contracts perform significant price discovery functions. If you have any questions regarding PJM's comments, please contact Vincent Duane, General Counsel, at (610) 666-4367.

Respectfully submitted,



Vincent P. Duane

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⁵ 74 Fed. Reg. 54,966; see also PJM Open Access Transmission Tariff ("OATT"), Attach. K – Appendix § 2.6.