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Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902

Edward S. Christenbury  
General Counsel

## COMMENT

April 27, 1998

### VIA FACSIMILE AND FEDERAL EXPRESS

Ms. Jean A. Webb  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, N.W.  
Washington, DC 20581

Re: Chicago Board of Trade Application for Designation as a Contract Market  
in TVA Hub Electricity Futures and Options 63 FR 16250 (April 2, 1998)

Dear Ms. Webb:

The Tennessee Valley Authority ("TVA") appreciates the opportunity to reply to statements made by certain parties providing comments to the Commodity Futures Trading Commission ("CFTC") on the Chicago Board of Trade's ("CBOT") application for designation as a contract market in TVA Hub Electricity Futures and Options. These comments purportedly pertain to issues which some commentators suggest raise doubts about the suitability of the TVA electric power transmission system to serve as the point of delivery for an electricity futures contract market. These comments in many respects seem to be based on a misunderstanding of the TVA system and how the TVA hub futures contract market would operate. TVA's purpose in responding is to ensure that the CFTC has before it complete information about these and other issues. Although many of the commentators' remarks are not material to the CFTC's determination, we think that TVA's response to their remarks would be helpful.

TVA is a wholly owned corporate agency and instrumentality of the United States established by the Tennessee Valley Authority Act of 1933, as amended ("Act"), with the objective of developing the resources of the Tennessee Valley region in order to strengthen the regional and national economy and the national defense. As part of its statutory mission, TVA operates one of the Nation's largest electric power systems, serving the needs of more than seven million citizens and businesses in parts of seven States.

The exercise of all TVA powers and activities, including those associated with the TVA electric power system, is directed by TVA's three-member Board of Directors. Like CFTC's Commissioners, TVA's Directors are appointed by the President of the United States, by and with the advice and consent of the United States Senate. In appointing Directors of the TVA Board, the President designates one to be the Chairman. Under the Act, TVA's Chairman and Directors are expressly prohibited from having "financial interest in any public-utility corporation engaged in the business of distributing and selling power to the public" and from having "any interest in any business that may be adversely affected by the success of [TVA] as a producer of electric power."

Two issues raised by commentors pertain to: (i) the provisions of the Act which limit the parties to whom TVA power may be supplied and (ii) the scope of the Federal Energy Regulatory Commission's ("FERC") regulatory authority over TVA transmission service policies and the inapplicability of the antitrust laws to TVA. As discussed below, in our opinion neither of these issues will affect the suitability of the TVA transmission system to be the proposed hub of an electricity futures contract market. TVA defers to CBOT with respect to the financial and technical issues raised by commentors.

#### Limitations on Supply of TVA Power

The Act directs that TVA "shall make no contracts for the sale or delivery of power which would have the effect of making [TVA] or its distributors, directly or indirectly, a source of power supply outside the area for which [TVA] or its distributors were the primary source of power supply on July 1, 1957 . . . (emphasis added)." This restriction on TVA actions has already been taken into account in CBOT's application, as acknowledged in the comments by several commentors. The TVA hub contract rules expressly address, and are entirely consistent with, this legal constraint by providing that TVA, as a:

. . . party that is restricted by law to which parties it may sell electric energy . . . must liquidate all short positions prior to the expiration of trading. Notwithstanding any provision of these Rules, the clearing member of a party subject to such a restriction shall liquidate all open short positions of that party prior to the close of trading on the last day of trading **(5409.01(E))**.

In addition, TVA, under current law, also could not satisfy the contract rules' express legal condition precedents for permitting physical delivery under a TVA hub futures contract because TVA cannot lawfully certify that "if short, the participant . . . is not restricted by law to which parties it may sell electric energy" **(5409.01(B)(2)(a))**.

There can be no violations of the Act's restrictions as the TVA hub has been designed to operate. On the contrary, as the TVA hub would operate under the express terms of the contract rules,

TVA's making a futures contract cannot possibly result in any supply of TVA power under that contract.\* Moreover, with regard to the possibility alleged by one commentor that some party to whom TVA may otherwise lawfully sell power might seek to resell that power under a TVA hub futures contract, TVA notes that such a party could only purchase power from TVA in the underlying cash market. In addition, Exhibit A (page 6) to the Consent Judgment, which is cited by that same commentor as to the legal limitations applicable to TVA, also expressly requires that TVA:

. . . will supply power under exchange power transactions with the understanding that such power is not being purchased for the purpose of reselling it to any such unauthorized third party. In the event TVA discovers that such power has been purchased for a purpose inconsistent with this policy, such transaction shall be terminated.

Likewise, there will be no violation of this restriction. Indeed, since all sales of power by TVA can only be consummated in the underlying cash market, the legal constraints currently in effect in the underlying cash market already operate adequately to prevent the resales described by that commentor.

Moreover, TVA notes that the CFTC just recently approved two new electricity futures contract markets based upon the transmission systems of utilities to which TVA lawfully sells its power in the underlying cash market, one of which has substantial transmission system interties with the TVA transmission system and makes substantial purchases of TVA power. The fact that significant amounts of TVA power are sold in the underlying cash market to those specific utilities (as well as some of the major utilities that border them) and flows into their respective transmission systems apparently did not cast any doubt on the appropriateness of the designation of those two futures contract markets. Neither, therefore, should TVA power sales to those same parties (as well as to other parties to whom TVA may lawfully sell power in the underlying cash market) be considered a legitimate issue with respect to the appropriateness of a TVA hub futures contract market.

In response to the assertion by one commentor that the Act's restrictions at issue somehow categorically prohibit TVA from being "a seller of a TVA Hub Contract," there is, in fact, no such prohibition, and TVA may sell a TVA hub futures contract. As already noted, the TVA hub contract rules expressly require that any short position by TVA must be liquidated prior to the end of the last trading day and, therefore, contracts sold by TVA can never go through the

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\* To the extent that TVA may participate in an "exchange for physical transaction" to replace futures contracts when TVA "is short," such an exchange for physical transaction would be consummated with a physical sale transaction in the underlying cash market and could be only entered into with a party to which TVA may lawfully sell power, consistent with the Act's restrictions.

TVA hub's process for matching buyers and sellers and establishing physical purchase and sale obligations upon the expiration of a contract's trading. Consequently, TVA's making of such a futures contract, in light of the TVA hub contract rules pending before the CFTC, cannot possibly "have the effect of making" TVA "a source of power supply" in violation of the Act.

### **FERC Regulation and Antitrust Laws**

Two commentors raised issues about how the scope of FERC regulation over the TVA transmission system and the inapplicability of antitrust laws to TVA may contribute to the potential for manipulation and abuse in a TVA hub futures contract market.

The scope of FERC's statutory jurisdiction over the TVA transmission system and the inapplicability of antitrust laws to TVA are due to TVA's status as a Federal agency and how Congress (in the case of FERC jurisdiction) and the courts (in the case of the antitrust laws) have determined that those laws should be applied (or not applied) to instrumentalities of the Federal Government and to other governmental entities. The current state of the law reflects the policy judgment that, with respect to business-like activities carried on by governmental entities such as TVA, the protection of the public interest does not require the same degree or types of regulation as have historically been imposed on investor-owned companies. In general, this is because such governmental entities, being directly owned by the public for the public's benefit, are not motivated by the same factors that warrant the degree of governmental regulation applied to private businesses.

There is simply no basis for the apparent suggestion by some commentors that an electric transmission system operated by a Federal agency, which in turn is governed by three individuals appointed by the President of the United States and confirmed by the United States Senate, is somehow so intrinsically susceptible to fraudulent manipulation and abuse as to raise doubt as to its ability to qualify as a futures contract market. If anything, it is exactly the opposite that should be presumed, given TVA's status as a nonprofit public agency and the fact that Congress or the courts have provided these exemptions to TVA.

TVA appreciates the importance and appropriateness of the economic and public interest review that CFTC undertakes during its consideration of proposed futures contract markets. However, a closer inspection of these particular TVA-specific comments made by others readily reveals that they are actually calling for changes in existing public policies established by law. In that regard, we think that Congress is the appropriate forum for evaluating whether (or the extent to which) the protection of the public interest might warrant making changes to existing law about the scope of FERC's regulation and the application of the antitrust laws to TVA, a Federal agency. We disagree with what seems to be a suggestion by some commentors that the CFTC should unilaterally take a position as to the need for changes in these laws independently and in advance of Congress's own ongoing deliberations and ultimate determinations as to whether or not the public interest would be served by expanding the applicability of these laws to cover TVA.

With respect to the extent to which FERC presently regulates the TVA transmission system, it is true that TVA, as well as other publicly owned electric power systems in the United States (which include municipalities, cooperatives, State instrumentalities, and Federal power agencies), is not currently required to submit a transmission service tariff to FERC for approval and is not otherwise directly subject to FERC Order No. 888 and related FERC orders. It is also true that TVA's transmission service agreements are not individually reviewed and approved by FERC.

In developing its TVA Board-approved, published Transmission Service Guidelines, TVA has voluntarily structured those Guidelines in a manner which it believes to be substantially similar to the pro forma open-access tariff approved by FERC. Moreover, as expressly stated by FERC in its decision in AES Power, Inc., 74 FERC 61,220 (1996), TVA "is subject to the same requirements regarding rates, and terms and conditions of [transmission] service as any other transmitting utility subject to sections 211 and 212." Consequently, the apparent suggestion by some commentators that TVA is capable of manipulating its transmission service policies and practices without constraint is both incorrect and misleading.

There is no question that TVA can be ordered by FERC to provide transmission service to others across the TVA transmission system and that FERC has authority to review the terms and conditions of TVA's transmission service arrangements. Notwithstanding the current specific exemptions noted above, TVA believes that FERC's wheeling jurisdiction over the TVA transmission system is meaningful regulatory oversight that provides an appropriate remedy for parties who might believe themselves aggrieved by TVA's transmission service practices. TVA respectfully disagrees with the characterization that such a remedy is "too little, too late." TVA observes that any party feeling aggrieved by a particular utility's transmission service would typically have to resort to an equally formal FERC process to obtain relief. Moreover, the FERC decisions and historical activity in the cash market presented to the CFTC thus far in this process do not indicate in any way that TVA transmission service customers are treated disadvantageously in comparison to transmission service customers of other utilities in the region or that TVA discriminates among its transmission service customers.

For example, notwithstanding an allegation incorrectly raised to the contrary, TVA's Transmission Service Guidelines do require TVA to take transmission service in making its own off-system sales and purchases under the same terms and conditions as it provides for others requesting similar service. TVA also takes exception to the unsubstantiated allegations of an improper calculation of TVA's transmission service charges and a failure to functionally separate its marketing business from its transmission service units.

TVA notes that the particular circumstance, with respect to which the above unsubstantiated allegations appear to be made, primarily involved the inability of a party requesting transmission service to fulfill TVA's minimum creditworthiness criteria without having to provide suitable security to ensure the payment of transmission services charges. TVA's creditworthiness requirement is identical to that provided for in the FERC-approved tariffs of private utilities.

Ms. Jean A. Webb

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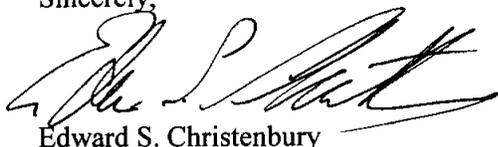
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As noted previously, in conjunction with any such request for FERC-ordered wheeling, the terms and conditions of the TVA transmission service being provided would be subject to FERC review. In addition, the commentors raising these items as issues did not note that FERC has imposed a reciprocity requirement on publicly owned electric systems (including TVA) so that those publicly owned systems can be refused transmission services from electric systems regulated by FERC if they do not also offer transmission services to such electric systems under terms and conditions that are comparable to the services that they are seeking. This provides further meaningful FERC regulatory oversight over TVA's practices in providing transmission service in the cash market.

In this regard, it should be noted that TVA has requested and is receiving transmission service from all of the private utilities which border the TVA system (and many of the private utilities that border them) and that, under this reciprocity requirement, TVA's provision of transmission services to them is and must be under terms and conditions that are comparable to the transmission services available under FERC-approved tariffs. We believe that the fact that those private utilities are providing transmission service to TVA is a clear indication that they agree that TVA is providing transmission service to them in a fair and equitable manner under terms and conditions that are comparable to the transmission services available under FERC-approved tariffs. Moreover, the assertion that TVA is somehow free to improperly manipulate its transmission service terms and conditions ignores the fact that, by doing so, its neighboring systems could in turn deny TVA the transmission services upon which it depends to access many off-system sources of electric power to meet its native load power supply responsibilities.

TVA hopes that these additional comments will be beneficial to the CFTC in providing a more complete presentation of these TVA-specific issues.

Sincerely,

A handwritten signature in black ink, appearing to read 'E. S. Christenbury', written over a horizontal line.

Edward S. Christenbury