

February 24, 2016

Via Electronic Submission

Christopher Kirkpatrick
Secretary of the Commission
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: *Notice of Proposed Order and Request for Comment on an Application for an Exemptive Order From Southwest Power Pool, Inc. From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in Section 4(c)(6) of the Act*

Dear Secretary Kirkpatrick:

We are submitting this written statement to the Energy and Environmental Markets Advisory Committee (“EEMAC”) of the Commodity Futures Trading Commission (“CFTC” or “Commission”) on behalf of the independent system operators (“ISOs”) and regional transmission organization (“RTOs”) that submitted comments in response to the Commission’s proposed order to grant a public interest exemption for certain transactions in the wholesale electricity markets operated by the Southwest Power Pool (“SPP”), SPP members, and SPP from all but the anti-manipulation and anti-fraud provisions of the Commodity Exchange Act (“CEA”).¹

I. Introduction

We represented PJM Interconnection, L.L.C. (“PJM”) and the Electric Reliability Council of Texas (“ERCOT”) in applying for and receiving a public interest exemption under Section 4(c) of the CEA. In the application, which was submitted on February 7, 2012, and updated on June 11, 2012, PJM, ERCOT, and four other ISOs and RTOs, including the California Independent System Operator (“CAISO”), ISO New England Inc., the Midwest Independent System Transmission System Operator, Inc. and the New York Independent System Operator, Inc., requested a public interest exemption for specified transactions in the ISO-RTO markets, the ISOs and RTOs, and any person or class of persons offering, entering into, rendering advice, or rendering other services with respect to such transactions from all but the

¹ Notice of Proposed Order and Request for Comment on an Application for an Exemptive Order From Southwest Power Pool, Inc. From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in Section 4(c)(6) of the Act, 80 Fed. Reg. 29490 (May 19, 2015) (“**Proposed SPP Order**”).

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anti-manipulation and anti-fraud provisions of the CEA. On April 2, 2013, the Commission issued a final order granting the requested exemption (the “**ISO-RTO Final Order**”).²

Separately, we submitted comments on behalf of PJM, ERCOT, and CAISO in response to the Proposed SPP Order. In addition, we filed an *amicus curiae* brief on behalf of PJM, ERCOT, and CAISO in *Aspire Commodities LP and Raiden Commodities LP v. GDF Suez Energy North America Inc. et al.*, a case in which Aspire Commodities L.P. and Raiden Commodities, L.P. filed a private claim against GDF-Suez Energy, North America, Inc. and six of its affiliates under CEA section 22 for allegedly manipulating electricity prices in the ERCOT market.

This statement addresses the following three points:

- The benefits of section 4(c) public interest exemptions for the ISOs and RTOs, the CFTC, and the public;
- The history of the Commission’s section 4(c) exemptions; and
- The adverse consequences of allowing private rights of action for transactions solely in ISO and RTO markets.

II. The Benefits of Section 4(c) Public Interest Exemptions for the ISOs and RTOs, the CFTC and the Public

Questions about the regulatory certainty under the CEA of ISO and RTO transactions have been before the Commission for many years. In 1998, PJM submitted the first of several requests for no-action relief from the Commission to confirm that it would not regulate various PJM transactions as futures contracts. In 2010, twelve years after PJM submitted its first no-action request, and as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), Congress sought to avoid jurisdictional disputes between the CFTC, the Federal Energy Regulatory Commission (“FERC”), and the Public Utility Commission of Texas (“PUCT”) over the regulation of ISO and RTO transactions by adding a specific provision to section 4(c) directing the Commission to grant exemptions for transactions made pursuant to a FERC-approved tariff or a protocol permitted to take effect by the PUCT if, as the CFTC found in the ISO-RTO Final Order, such an exemption is in the public interest.³

² Final Order in Response to a Petition from Certain Independent System Operators and Regional Transmission Organizations to Exempt Specified Transactions Authorized by a Tariff or Protocol Approved by the Federal Energy Regulatory Commission or the Public Utility Commission of Texas From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in the Act, 78 Fed. Reg. 19880 (Apr. 2, 2013).

³ 7 U.S.C. § 6(c)(6).

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A public interest exemption provides the ISOs and RTOs and their members with legal certainty about how they, and their transactions in the organized wholesale electricity markets, will be regulated. Because FERC and the PUCT comprehensively regulate the organized wholesale electricity markets, an exemption protects ISOs and RTOs against duplicative and conflicting regulations. An exemption also provides ISOs and RTOs and their members with legal certainty about the enforceability of their transactions. Legal certainty about the regulation and enforceability of ISO and RTO transactions is critical to efficient federal and state regulation, and the “responsible economic or financial innovation and fair competition” that public interest exemptions are designed to promote.⁴

At the same time, an exemption benefits the CFTC by avoiding counterproductive disputes between sister regulators about which agency has regulatory jurisdiction – an outcome that Congress expressly sought to achieve when it called for the CFTC and the FERC to exercise their respective authorities in a manner that would “ensure effective and efficient regulation in the public interest.”⁵ Granting an exemption also conserves the CFTC’s limited resources by enabling it to defer to the comprehensive regulation of ISOs and RTOs by the FERC and the PUCT. Finally, and as discussed in greater detail below, an exemption preserves the CFTC’s ability, in a deliberate and controlled manner, to take enforcement action against wrongdoers who manipulate ISO and RTO markets. Importantly, one of the remedies that the CFTC can seek in an enforcement action is restitution to customers of damages caused by the defendant’s illegal conduct.⁶

Finally, an exemption benefits the public by ensuring that the complex wholesale electricity markets operated by the ISOs and RTOs are regulated by expert agencies, the FERC and the PUCT, in a manner that produces just and reasonable rates.

III. The History of the Commission’s Section 4(c) Exemptions

Section 4(c) was added to the CEA in 1992. As far as we have been able to determine, over the past 24 years the Commission has expressly preserved a private right of action in broad public interest exemptions only two times. Those two exemptions were superseded within eight days by Congress with statutory exemptions that did not permit private rights of action in

⁴ 7 U.S.C. § 6(c)(1).

⁵ Section 720(a)(1)(A) of the Dodd-Frank Act; 15 U.S.C. § 8308(a)(1) (Directing the CFTC and FERC to “negotiate a memorandum of understanding to establish procedure: (A) for applying their respective authorities in a manner so as to ensure effective and efficient regulation in the public interest; (B) resolving conflicts concerning overlapping jurisdiction between the 2 agencies; and (C) avoiding, to the extent possible, conflicting or duplicative regulation.”).

⁶ 7 U.S.C. § 9.

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connection with exempt transactions.⁷ Similarly, in issuing an exemptive order for the effective date of certain provisions of the CEA that were amended by the Dodd-Frank Act, the Commission expressly stated that: “[t]o the extent that the Final Order provides [4(c)] exemptive relief [from certain provisions of the CEA], such exemptive relief would, in effect, *preclude a person from succeeding in a private right of action under CEA section 22(a)* for violation of such provisions.”⁸ In the same regard, the ISO-RTO Final Order also does not preserve CEA section 22 as continuing to apply to ISO and RTO transactions. Thus, the Commission’s statement in the preamble to the Proposed SPP Order that it would be “highly unusual” for the Commission to preserve its own manipulation and fraud enforcement authority while excluding a private right of action for the same violations is inconsistent with its regular and long-standing practice in granting public interest exemptions.

IV. The Adverse Consequences of Allowing Private Rights of Action Based Solely Upon ISO and RTO Transactions

Preserving private rights of action in public interest exemptions for ISO and RTO transactions will have many adverse consequences. Section 4(c) enables the Commission to exempt transactions from CEA regulation without determining whether those transactions are swaps or futures contracts.⁹ In the case of ISO and RTO transactions, this mechanism is precisely how a public interest exemption avoids jurisdictional disputes between sister regulators.

Allowing private actions will undermine the legal certainty provided by the exemptions and potentially could divest FERC and the PUCT of jurisdiction over certain ISO and RTO transactions. The following scenario, which focuses exclusively on a hypothetical manipulation of ISO-RTO transactions, not on a cross-market manipulation scheme that involves transactions regulated by the CFTC, demonstrates how allowing private claims related to ISO and RTO transactions would lead to significant regulatory uncertainty. Assume that:

⁷ On December 13, 2000, the Commission issued two rules that preserved Section 22 in connection with Section 4(c) exemption orders. *See A New Regulatory Framework for Clearing Organizations*, 65 Fed. Reg. 78020 (Dec. 13, 2000) (Section 39.5 Enforceability); *see also Exemption of Transactions on a Derivatives Transaction Facility*, 65 Fed. Reg. 77962, 77986 (Dec. 13, 2000) (Section 37.8 Enforceability). Eight days later, in the Commodity Futures Modernization Act, Congress amended the CEA to grant statutory exemptive relief for certain types of transactions and did not preserve private rights of action. *See* former CEA Sections 2(d), (g) and (h). As a result, the CFTC was forced to withdraw its regulations. *See A New Regulatory Framework for Multilateral Transaction Execution Facilities, Intermediaries and Clearing Organizations; Rules Relating to Intermediaries of Commodity Interest Transactions; A New Regulatory Framework for Clearing Organizations; Exemption for Bilateral Transactions*, 65 Fed. Reg. 82278 (Dec. 28, 2000).

⁸ *See Effective Date for Swap Regulation*, 76 Fed. Reg. 42508, 42517 (Jul. 19, 2011).

⁹ Indeed, in applying for the 4(c) exemption, the ISOs and RTOs expressly stated that they did not presume that transactions in the ISO and RTO markets are subject to the regulatory oversight of the CFTC. And in its ISO-RTO Final Order, the Commission took no position on this issue.

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- Party A sues Party B for manipulating the price of a financial transmission right or congestion revenue right (collectively for this hypothetical, “FTR”) transaction in an ISO or RTO;
- To prevail on a private claim under CEA section 22, Party A first must prove that an FTR is a swap or futures contract;
- The district court and, ultimately, a court of appeals rules that an FTR is a swap, and consequently that the ISO or RTO, which acts as a central counterparty, is a designated contract market or swap execution facility;
- FERC then brings an enforcement action against Party B for manipulating the price of the same FTR transactions that are the subject of the private claim;
- Party B asserts that the CFTC’s exclusive jurisdiction over swap transactions precludes FERC’s claim and, on direct appeal to the same court of appeals that ruled in the civil suit, the court agrees, being bound by its precedent in the civil suit;
- Repeat this scenario in multiple jurisdictions across the United States;
- Because the CFTC’s jurisdiction over swaps is “exclusive,” if a number of federal circuits hold that FTRs or other ISO and RTO transactions are swaps or futures contracts, no other federal or state agency could regulate ISOs and RTOs or their transactions.

It would not serve the public interest if allowing private rights of action based upon RTO and ISO transactions had the effect of precluding the FERC and the PUCT from regulating ISOs and RTOs or their transactions. By directing the CFTC to grant public interest exemptions for RTO and ISO transactions, Congress surely did not intend that the CFTC should either create or fill such a regulatory void. It is more sensible for the Commission to devote its limited resources to the primary markets, persons and transactions that it is charged to regulate rather than to divert resources to complex organized wholesale electricity markets that it does not have the expertise or experience to regulate.

Importantly, a CFTC enforcement action does not raise the same jurisdictional problems as a private claim because the CFTC’s anti-manipulation authority is not limited to swaps and futures contracts.¹⁰ The CFTC can prosecute manipulation of the price of a commodity in interstate commerce regardless of the legal characterization of the transactions involved. Consequently, the CFTC can prosecute manipulation of the price of an FTR without proving that

¹⁰ The definition of swap includes options. 7 U.S.C. 1a(47)(A)(i).

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an FTR is a swap or a futures contract and, therefore, without divesting the FERC and the PUCT of jurisdiction over ISO and RTO transactions.

There are several other adverse consequences to allowing private claims under the CEA for ISO and RTO transactions. As the ISO-RTO Commenters explained in the comments on the Proposed SPP Order, private claims will enable plaintiffs to collaterally attack rules approved by FERC or permitted to take effect by the PUCT by claiming that the ISO and RTO transactions made in compliance with those rules are unlawful. In addition, private claims will enable private parties to challenge "filed rates," something that the courts historically have left only to the FERC and the PUCT. Finally, private claims will interfere with the ability of the CFTC and the FERC to determine via their memorandum of understanding how to exercise their respective jurisdiction over ISO and RTO transactions and market participants.

V. Conclusion

For the foregoing reasons, the Commission should not preserve private rights of action in the ISO and RTO exemption orders. Instead, the Commission should continue to cooperate with the FERC and PUCT, and to rely on its existing enforcement authority, if and when necessary, to police manipulation and fraud in the ISO and RTO markets.

Respectfully submitted,


Paul J. Pantano, Jr.

cc: Ajay B. Sutaria, Secretary
Energy & Environmental Markets Advisory Committee
U.S. Commodity Futures Trading Commission