

September 27, 2012

Sauntia Warfield, Assistant Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

VIA ELECTRONIC MAIL

Re: *Proposed Order and Request for Comment on RTO and ISO Exemption for Certain Specified Transactions*

Dear Ms. Warfield:

I. INTRODUCTION.

On behalf of The Commercial Energy Working Group (the “Working Group”), Sutherland Asbill & Brennan LLP hereby submits these comments in response to the proposed order issued by the Commodity Futures Trading Commission (the “CFTC” or “Commission”) in response to a consolidated petition from certain regional transmission organizations (“RTOs”) and independent system operators (“ISOs”) exempting specified transactions from certain provisions of the Commodity Exchange Act (the “Act”) and Commission regulations (the “Proposed Order”).¹ The Working Group appreciates the opportunity to provide the comments set forth herein and respectfully requests the Commission’s consideration of such comments.

The Working Group is a diverse group of commercial firms in the energy industry whose primary business activity is the physical delivery of one or more energy commodities to others, including industrial, commercial, and residential consumers. Members of the Working Group are energy producers, marketers, and utilities. The Working Group considers and responds to requests for comment regarding regulatory and legislative developments with respect to the trading of energy commodities, including derivatives and other contracts that reference energy commodities.

II. COMMENTS OF THE WORKING GROUP.

The Working Group supports the Proposed Order and offers some recommendations for improvement below. RTOs and ISOs play a key role in assuring that reliable electricity is

¹ See *Proposed Order and Request for Comment on 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 Commission or the Public Energy Commission of Texas from Certain Provisions of the Commodity Exchange Act*, 77 Fed. Reg. 52,138 (Aug. 28, 2012) (the “Proposed Order”).

available for all aspects of the U.S. economy. The markets for electricity and related commodities and services within RTOs and ISOs are integral to the efficient operation of the electricity market. The Commission offers legal certainty in the Proposed Order, and we commend the CFTC for eliminating an unnecessary layer of regulation in an area that is already highly complex and highly regulated. Accordingly, we urge the Commission to issue a final order as quickly as possible.

We also recommend that the Commission make the amendments discussed below to the Proposed Order when it issues the final order.

A. Interim Relief.

The Commission currently has a lot on its agenda to complete its rulemakings under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) and to handle related matters. The Proposed Order will add tremendous legal certainty to the energy markets, even in its current form. Thus, while the Commission considers comments it receives about the Proposed Order, it should instruct staff to provide temporary no-action relief permitting firms to rely on the Proposed Order during the Commission’s deliberation period.

B. Clarify That Existing Products Fall Within the Exempt Categories.

The Commission should clarify that all contracts, agreements, or transactions currently offered or entered into in markets administered by the petitioners, pursuant to each petitioner’s respective tariff or protocol (“Existing Products”), are transactions subject to the exemption described in the Proposed Order. If there are any Existing Products that the Commission intends to exclude from such exemption, these contracts, agreements or transactions should be identified specifically to provide legal certainty to market participants. While certain Existing Products, such as “auction revenue rights,” “financial schedules,” “increment offers,” “decrement bids,” “virtual bids,” “virtual offers” and “internal bilateral transactions,” for example, are not discussed specifically in the Proposed Order, each of these Existing Products can be appropriately placed in one of the four enumerated categories of transactions as each is defined in the Proposed Order. They are all integral to the operation of the physical market for electricity.²

C. Defer to RTOs and ISOs on Market Participant Standards.

The Commission should defer to each RTO and ISO to establish suitability standards for market participants in its organized market. The Commission comments that its authority to

² The RTOs and ISOs may develop new transactions to accommodate changes in the physical markets for electricity, which changes may stem from such things as better technology or changes in market design to account for other federal or state regulations. So long as the RTOs and ISOs designate these new transactions as related to the physical market for electricity, particularly if approved by the FERC or the PUCT, as applicable, such new transactions should be deemed within the four enumerated transaction types subject to the Proposed Order without further rulemaking by the Commission.

issue the final order must meet the criteria of Section 4(c) of the Act, which limits the Commission's authority to grant exemption to "appropriate persons." Among the class of persons enumerated in Section 4(c)(3) are:

(K) such other person that the Commission determines to be appropriate in light of their financial or other qualification, or the applicability of appropriate regulatory protections.³

The Commission should defer to RTOs and ISOs to define which persons come within such categories. RTOs and ISOs have far greater understanding of the necessary minimum suitability criteria for market participants. Given that RTOs and ISOs oversee a physical market that is critical to the economy, they have no incentive to relax the suitability standards, but to the contrary have concerns not only with a party's financial wherewithal, but also its operational sophistication.⁴

The market participant standards outlined in each RTO and ISO tariff have been developed through an open stakeholder process. Losses incurred by RTOs and ISOs due to an event of default by a market participant are mutualized among members based on each member's level of market participation at the time of the loss. Thus, the parties at risk of loss due to a default are the ones who have set the standards. Additionally, the RTO and ISO market participant standards are approved by the Federal Energy Regulatory Commission ("FERC") and the Public Utility Commission of Texas ("PUC"), as applicable. Thus, there is no regulatory gap in the oversight of the RTO and ISO markets.

If certain current participants in the RTO/ISO markets are not deemed "appropriate persons," the Proposed Order, as finally issued, forces them to exit the market. Their departure may cause volatility and a decrease in liquidity for the physical market for electricity. Remaining participants who serve the load of the withdrawing market participants likely will face higher prices to procure the additional power needed. Existing load forecasts may also be inaccurate as these new customers will not factor into the remaining participants' forecast models. The electricity markets work best if a larger number of players, rather than a smaller pool, participate. Forcing participants to exit will diminish market competition and limit

³ *Proposed Order* at 52,143 n.80.

⁴ In general, the Working Group advocates that the Proposed Order, when issued in final form, should cause as little disruption, ideally none, to the operation of the RTO/ISO markets. We understand that the Commission has requested a deviation from current notice practices with respect to inquiries about bidding behavior. Under the terms of most RTO/ISO tariffs, a request for such information by an interested regulator results in the applicable RTO/ISO sending a notice of such inquiry to the applicable market participant. The Commission, as a condition to the exemption, requires that no notice of inquiry be sent by the RTO or ISO to the market participant. To avoid the RTO or ISO violating its own tariff, the tariff must be amended to accommodate the Commission's proposed condition. Reopening a tariff could result in multiple issues arising, many of which have nothing to do with the notice of inquiry, and may result in undue delay. To avoid this complication, the Working Group urges the Commission to not condition the exemption so as to prohibit RTOs and ISOs from providing notice to market participants when the Commission inquires about their bidding behavior.

available power in instances of unplanned outages, thereby increasing the risks posed to the remaining providers, RTO/ISOs and the marketplace as a whole.

It is not yet known how many market participants would qualify for “appropriate person” status, but due to the complexity and nuance market characteristics associated with the power grid and electricity markets, even minor disruptions to the participant pool could have severe and longstanding impacts. The Working Group requests that the Commission defer to each RTO’s and ISO’s market participant standards to identify “appropriate persons.” Based on (i) each RTO/ISO’s market oversight role, (ii) the stakeholder process involved, (iii) regulatory oversight already established for RTO and ISO market participant standards, and (iv) the real risk imposed on the markets if forced to deviate from the market participant standards, the Commission should defer to these procedures to identify what persons, in the context of the RTO and ISO markets, fall within the term “appropriate person” pursuant to Section 4(c)(3)(K) of the Act.

D. Order No. 741 Compliance Satisfies the Public Interest Standard.

The Commission identifies compliance with FERC’s credit policy reform⁵ as evidence that the proposed exemption is consistent with the public interest and the purposes of the Act.⁶ The Working Group requests clarification that if FERC approves an RTO’s or ISO’s Order No. 741 compliance filing, then no additional support for granting the exemption need be provided. The Commission should allow the RTO and ISO markets to exist largely as they currently do and should not require RTOs and ISOs to comply with the derivatives clearing organization (“DCO”) or swap execution facility (“SEF”) core principles or any other requirements that overlap with other compliance obligations. As revealed by the Commission’s comparison of Order No. 741 and the DCO core principles,⁷ compliance with Order No. 741 sufficiently demonstrates that the proposed exemption is consistent with the public interest and the purposes of the Act. What FERC has approved for purposes of Order No. 741 compliance should be deemed adequate by the Commission to exempt certain market transactions traditionally overseen by FERC.

E. Preliminary Approval While PUCT Negotiations Are Ongoing.

The Commission conditions the proposed exemption on having information sharing agreements in full force and effect between the CFTC and FERC and the CFTC and the PUCT.⁸ The Commission should provide preliminary approval of the exemption for the Electric Reliability Council of Texas (“ERCOT”) while discussions between the Commission and the PUCT to develop an information sharing agreement remain ongoing. The Proposed Order does not provide a timeline in which the information sharing agreement must be in place, but given ERCOT’s comparable market position to the other RTO and ISO petitioners, delay caused by

⁵ *Credit Reforms in Organized Wholesale Electric Markets*, 75 Fed. Reg. 65,942 (Oct. 27, 2010) (“Order No. 741”).

⁶ *Proposed Order* at Section V.C.

⁷ *Proposed Order* at Section V.C.

⁸ *Proposed Order* at 52,165.

ongoing negotiations between the Commission and the PUCT should not prevent ERCOT from timely accessing the proposed exemption.

III. CONCLUSION.

The Working Group supports appropriate regulation that brings transparency and stability to the swap markets worldwide. The Working Group appreciates this opportunity to provide comments on the Proposed Order and respectfully requests that the Commission consider the comments set forth herein as it develops its final order regarding these matters.

If you have any questions, please contact the undersigned.

Respectfully submitted,

/s/ David T. McIndoe

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Working Group*