Kenneth W. Anderson, Jr.
Commissioner

Public Utility Commission of Texas

June 22, 2015

By electronic submission

Chris Kirkpatrick
Secretary of the Commission
U.S. Commodities Future Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, D.C. 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:

On behalf of and as authorized by the Public Utility Commission of Texas (PUCT),[1] the undersigned appreciates the opportunity to comment on the Proposed Order and Request for Comment on an Application for an Exemptive Order from the Southwest Power Pool (the Proposed Order)[2] issued by the Commodities Futures Trading Commission (Commission) on May 21, 2015. In this proceeding, the Southwest Power Pool, Inc. (SPP) has sought the same exemptive relief the Commission has granted other Regional Transmission Organizations (RTOs) and Independent System Operators (ISOs), including the Electric Reliability Council of Texas (ERCOT),[3] in its final order exempting specified transactions from certain provisions of the Commodity Exchange Act in April of 2013 (the RTO-ISO Order).[4]

[1] Chairman Donna L. Nelson, Commissioner Kenneth W. Anderson, Jr., and Commissioner Brandy Marty Marquez.
[2] 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 21, 2015).
[3] ERCOT is an ISO, but for the purposes of these comments, statements regarding to RTOs are equally applicable to ISOs and the terms are used interchangably.
[4] 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

The PUCT commends the Commission's efforts in addressing the various RTOs' requests for exemptive relief. While the PUCT agrees that the type of exemptive relief provided in the RTO-ISO Order should extend to SPP, we have a serious concern regarding the Commission's inclusion of preamble language reserving private causes of action under Section 22 of the Commodity Exchange Act (CEA). By this letter, the PUCT provides comments addressing this concern.

I. BACKGROUND

Acting under authority delegated under the Public Utility Regulatory Act (PURA), the PUCT is responsible for ensuring the reliability of the ERCOT system and protecting the public interest inherent in the production and delivery of electricity among generators and all other market participants in the electricity sector.[5] The PUCT oversees ERCOT, the independent system operator for the electric grid, and the unbundled and restructured energy-only market operated on that grid. The ERCOT region covers approximately 75% of the Texas land mass and nearly 90% of its electric load. Importantly, the PUCT is responsible for detecting and taking enforcement action against market manipulation and other forms of market power abuse within the ERCOT region.[6] Unlike other RTOs, ERCOT's market rules are subject to the PUCT's exclusive jurisdiction rather than FERC oversight.

Beyond the ERCOT region, the PUCT regulates traditional vertically integrated electric utilities operating in other RTOs whose territories cover portions of Texas, including electric utilities operating in the Texas segment of SPP.

II. COMMENTS IN RESPONSE TO THE PROPOSED ORDER

Both the RTO-ISO Order and the Proposed Order preserve the Commission's anti-fraud and anti-manipulation authority under CEA and its implementing regulations. However, for the first time, the Commission stated in the Proposed Order's preamble that the RTO-ISO Order and

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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) (RTO-ISO Order).

[5] Public Utility Regulatory Act, TEX. UTIL. CODE ANN. § 39.151(d) (Vernon & Supp. 2012).

[6] PURA §§ 39.151 and 39.1515.

the Proposed Order did not preclude private causes of action brought under Section 22 of the CEA. In relevant part, the Commission stated:

> It would be highly unusual for the Commission to reserve to itself the power to pursue claims for fraud and manipulation—a power that includes the option of seeking restitution for persons who have sustained losses from such violations or a disgorgement of gains received in connection with such violations—while at the same time denying private rights of action and damages remedies for the same violations. Moreover, if the Commission intended to take such a differentiated approach (i.e., to limit the rights of private persons to bring such claims while reserving to itself the right to bring the same claims), the RTO-ISO Order would have included a discussion or analysis of the reasons therefore. Thus, the Commission did not intend to create such a limitation, and believes that the RTO-ISO Order does not prevent private claims for fraud or manipulation under the Act. For the avoidance of doubt, the Commission notes that this view equally applies to [the Proposed Order]. Therefore, the [Proposed Order] also would not preclude such private claims.[7]

This new interpretation of the RTO-ISO Order represents a significant and problematic departure from the commonly understood jurisdictional limits of the CEA as applied under the RTO-ISO Order. Indeed, such an interpretation poses a considerable risk to ERCOT and other RTOs because it has the potential to undermine carefully structured power market rules that allow for the efficient and economical production, sale, and delivery of electricity in Texas as well as other parts of the country.

A. Retroactive Alteration of the RTO-ISO Order Is Manifestly Unjust

The parties affected by the RTO-ISO Order are entitled to rely on the order's plain language declaring a specific set of transactions as exempt from the CEA yet reserving an unambiguous, enumerated list of CEA provisions that would continue to apply to those transactions.[8] The RTO-ISO Order's enumerated list of reserved provisions does not include Section 22 of the CEA. The Proposed Order's preamble declaration that the RTO-ISO Order did

[7] Proposed Order at 29493.
[8] RTO-ISO Order at 19912 (specifically the RTO-ISO Order reserves "the Commission's general antifraud and anti-manipulation authority, and scienter-based prohibitions, under CEA sections 2(a)(1)(B), 4(d), 4b, 4c(b), 4o, 4s(h)(1)(A), 4s(h)(4)(A), 6(c), 6(d), 6(e), 6c, 6d, 8, 9, and 13 and any implementing regulations promulgated under these sections including, but not limited to, Commission regulations 23.410(a) and (b), 32.4, and part 180.")

not preclude private parties from bringing Section 22 claims under the CEA directly controverts the list of reserved provisions in the RTO-ISO Order. In fact, this new language effectively attempts to add Section 22 to the list of reserved provisions in the RTO-ISO Order in a retroactive manner.

If the Commission wished to reserve Section 22 claims under the RTO-ISO Order then it should have included that provision among the enumerated list of reserved provisions upon issuance of the RTO-ISO Order. If the Commission had done so then affected parties would have had notice of the inclusion and an opportunity to object to it consistent with the requirements of the Commission's exemptive relief authority under the CEA.[9] Instead, the Commission now seeks to alter the scope of the RTO-ISO Order in dicta that appears in a proposed order in a separate proceeding over two years after the issuance of the RTO-ISO Order. Such alteration deprives parties of their due process right to object to the new scope of the RTO-ISO Order and seeks to vitiate their reasonable reliance on the plain language of the order. This result is plainly unjust and accordingly calls for removal of the offending preamble language from the Proposed Order.

Upon a public interest finding, Section 4(c)(6) of the CEA directs the Commission to exempt certain electricity transactions from specific provisions of the CEA.[10] Section 4(c)(6) recognizes that RTOs are subject to extensive regulation by FERC (or in the case of ERCOT, by the PUCT), and without exemptive relief the electricity markets would be subject to overlapping and potentially conflicting oversight regimes. The CEA's exemptive relief provision is accordingly consistent with Section 222 of the Federal Power Act, which prohibits manipulative or deceptive trade practices in the electricity markets, but expressly does not create any private cause of action.[11] The exemptive relief provision of the CEA should be similarly construed to preclude private causes of action so that FERC and the PUCT retain their respective exclusive oversight of the markets under their jurisdiction. By contrast, allowing private causes of action subjects the RTOs to the claims of private litigants, which increases the costs associated with operating those markets. This is particularly harmful for ERCOT, a non-profit entity, because electricity consumers ultimately bear the costs of ERCOT system administration. Accordingly,

[9] Section 4(c)(1) of the CEA allows the Commission to grant exemptive relief only "after notice and opportunity for hearing." 7 U.S.C. § 6(c)(1).
[10] 7 U.S.C. § 6(c)(6).
[11] 16 U.S.C. § 824v.

an interpretation of the CEA that allows private causes of action under Section 22 potentially harms the public interest and should be rejected.

B. Private Section 22 Claims under the CEA Would Compromise the PUCT's Oversight Authority

Allowing private parties to litigate causes of action under Section 22 of the CEA could have harmful effects on the oversight authority of the PUCT as well as the administration and operation of the ERCOT market. Under authority granted by the Texas Legislature, the PUCT has established a complex regulatory scheme designed to facilitate electricity transactions in ERCOT's restructured and unbundled market. ERCOT is unique in that it is the sole energy-only market in the United States, meaning that the PUCT does not impose a system-wide mandatory minimum reserve capacity margin on load serving entities. These unique attributes of ERCOT require a regulator with intimate knowledge of the ERCOT market to develop a regulatory structure that encourages competition, ensures reliability, and protects consumers. Throughout the evolution of the ERCOT market, the PUCT has promulgated rules to address the behavior of market participants, which include competitive retail electric providers, transmission and distribution service providers, and competitive electric generators. These rules have been implemented after careful consideration of stakeholder input to ensure that oversight rules appropriately balance the varying interests of the different types of ERCOT market participants, including consumers.

Furthermore, ERCOT has its own protocol development process to implement market rules providing for efficient and fair electricity transactions.[12] The ERCOT protocols address a broad set of issues related to the administration of the electricity market, ranging from reliability requirements for generation and transmission companies to the settlement of financial transactions for buyers and sellers. Like PUCT rules, stakeholders provide their perspective in the development of the ERCOT protocols to achieve a coherent and workable protocol framework.

Private causes of action brought under the CEA have the potential to compromise carefully structured markets established by regulators and RTOs because such private claims may collaterally attack the rules that constitute the structure of a market's regulatory scheme. If

[12] The ERCOT market rules are available at www.ercot.com/mktrules.

private litigants are able to raise claims under Section 22 of the CEA then those claims may be premised on activities undertaken pursuant to market rules that allow or prohibit particular behavior within ERCOT or other RTOs, as applicable. One problem with this type of claim is that it may allow a litigant to challenge a market rule in a federal forum where the regulator and/or RTO may not be a party to the lawsuit. State regulators and RTOs have invested considerable time, effort, and thought in the development of their respective market rules. However, the critical objectives of those market rules could be significantly compromised if a federal court were to declare certain activity undertaken in compliance with local rules problematic under the CEA based on an interpretation of federal law brought by a private litigant seeking damages.

Perhaps an even more troubling aspect of the Commission's reservation of Section 22 CEA claims is that a private litigant could sue an RTO directly for activities undertaken in that RTO. This is particularly problematic for ERCOT because ERCOT is a non-profit entity whose costs are funded by load serving entities. Accordingly, ERCOT funds devoted to defending private lawsuits brought under the CEA would be imposed on load serving entities that, in turn, would be passed to their customers, ultimately raising the cost of electric services.[13]

In short, the goals of private causes of action brought under Section 22 of the CEA and the goals of market rules developed by state regulators and RTOs do not coincide. Consequently, allowing CEA lawsuits brought by private parties to disrupt carefully structured electricity markets could have crippling effects on the fair and efficient administration of those markets.

Proper oversight authority for market participant behavior in ERCOT rests with the PUCT, not with private litigants seeking to pursue claims under the CEA in federal courts. The PUCT has significant experience and expertise in regulating the activities of market participants in the ERCOT market. Market participants in ERCOT aggrieved by the activities of other participants may bring complaint actions to ERCOT to adjudicate their claims. ERCOT decisions in those complaint cases are then ultimately subject to PUCT review on appeal. If the

[13] For purposes of these comments, the terms customer and ratepayer are used interchangeably. However, technically, customers are those that are served by a competitive retail electric provider while ratepayers are the customers of public power entities such as electric cooperatives and municipal utilities. In spite of the distinction, both ratepayers and customers would ultimately be responsible for funding ERCOT's legal costs associated with defending CEA claims.

non-prevailing party is dissatisfied with the PUCT's determination then it may seek appellate review in Texas state courts. This complaint process is designed to accommodate claims of fraud and market manipulation.

By law, the PUCT must select an independent market monitor to detect and prevent market manipulation strategies and recommend measures to enhance the efficiency of the ERCOT wholesale market.[14] ERCOT's independent market monitor works closely with the PUCT's Oversight and Enforcement Division to ensure that market participants act in accordance with state law, PUCT regulations, and ERCOT market rules. The PUCT's Oversight and Enforcement division and the independent market monitor review all facets of ERCOT activity, including without limitation, instances of potential ERCOT market manipulation. Importantly, the PUCT's Oversight and Enforcement Division and the independent market monitor undertake review of market participant behavior with a view toward upholding the rules that support the ERCOT market to advance the common benefit of all market participants and electricity consumers. Additionally, these entities have an intimate understanding of the unique attributes of the ERCOT market along with a contextual understanding of how PUCT and ERCOT rules affect and support the electricity market. Simply stated, ERCOT already has a proficient and robust oversight scheme to detect and take action against market manipulation within its market. Allowing private litigants to bring Section 22 CEA claims would conflict with and undermine the PUCT's vigorous oversight mechanisms established to ensure the viability of the ERCOT market.

C. *Aspire Commodities, LP v. GDF Suez Energy N. Am. Inc.*

Recently, a federal district court in Texas' southern district addressed a private claim brought under the CEA against an ERCOT market participant.[15] Although the judge held that the RTO-ISO Order precluded such a claim, the case provides an example of the potential confusion and harm that private CEA Section 22 claims could inflict on the ERCOT market. The plaintiffs in *Aspire* alleged that the defendant engaged in manipulative behavior by submitting offers for electricity in ERCOT with the intent to manipulate prices in the derivative commodities market.[16] The plaintiffs asserted that the defendant was able to engage in such

[14] PURA §§ 39.1515 and 39.157. The independent market monitor for ERCOT is Potomac Economics.
[15] *Aspire Commodities, LP v. GDF Suez Energy N. Am. Inc.*, No. H-14-1111 (S.D. Tex. Feb. 3, 2015).
[16] *Id.* at 4.

behavior because of a provision of the PUCT Substantive Rules that deems electricity generators controlling less than 5% of the total installed generation capacity in the ERCOT region as not having market power, which is a prerequisite for exercising market power abuse.[17] This rule is commonly referred to as the "Small Fish Rule" and is so called in these comments.

The Small Fish Rule serves an important purpose in the ERCOT market and any private party lawsuit that jeopardizes the validity of the Small Fish Rule would frustrate that purpose. The PUCT adopted the Small Fish Rule to provide certainty to small suppliers that they would not be found to have market power.[18] The Small Fish Rule, which has been in effect for almost nine years, thus furthers PURA's objective to develop a robust, competitive wholesale market. The Small Fish Rule does so by encouraging increased participation because it shields small new entrants in the generation market from claims of market power abuse by allowing smaller generation owners greater flexibility in their energy bidding behavior. This, in turn, permits energy prices to reach levels that provide the opportunity for a sufficient return on investment in order to further encourage new generation, which results in enhanced competition.[19] Because it removes potential uncertainty that might otherwise discourage the entry of new generation, the Small Fish Rule plays an important part in ERCOT's energy-only market. The PUCT market rules, including the Small Fish Rule, are designed to strike the appropriate balance to allow open, unrestricted competition among new generation resources while also preventing market power abuse. It is precisely that balance that the PUCT sought to achieve by implementing the Small Fish Rule after careful consideration of comments presented by interested parties in a rulemaking

[17] *Id.* at 3; 16 Texas Admin. Code § 25.504(c). § 25.504(c) reads as follows:

> **Exemption based on installed generation capacity.** A single generation entity that controls less than 5% of the installed generation capacity in ERCOT, as the term "installed generation capacity" is defined in §25.5 of this title (relating to Definitions), excluding uncontrollable renewable resources, is deemed not to have ERCOT-wide market power. Controlling 5% or more of the installed generation capacity in ERCOT does not, of itself, mean that a generating entity has market power.

[18] Rulemaking on Wholesale Electric Market Power and Resource Adequacy in the ERCOT Power Region, PUCT Project No. 31972, Order Adopting Amendment to §25.502, New § 25.504 and New § 25.505 as Approved at the August 10, 2006 Open Meeting at 89-90 (Aug. 24, 2006).

[19] PURA 31.001(c) ("The development of a competitive wholesale market that allows for increased participation by electric utilities and certain nonutilities is in the public interest."); Mark Watson, *Texas PUC Urged to Abolish "Small Fish" Rule*, MEGAWATT DAILY, Apr. 23, 2014 at 1.

proceeding that was commenced over nine years ago.[20] History has shown that this approach has succeeded in delivering competitive market outcomes.[21]

Upon adoption of the Small Fish Rule, the PUCT stated that it was "not a free pass for entities to abuse the market in whatever way they wish."[22] The PUCT explained that the independent market monitor would continue to examine the behavior of small suppliers for instances of local market power and advise the commission of possible violations no matter the size of the entities.[23] Indeed, in the most recent ERCOT State of the Market Report, the independent market monitor specifically addressed the offer behavior of suppliers covered by the Small Fish Rule and whether those suppliers attempted to exercise market power.[24] Lastly, it is worth mention that the Small Fish Rule does not implicate federal antitrust laws because a refusal to sell in the absence of collusion does not constitute a restraint of trade.[25]

Recently, the PUCT had the opportunity to reconsider the Small Fish Rule and, after extensive stakeholder comment and study, declined to do so. In April of 2014, Raiden Commodities, LP filed a petition asking the PUCT to eliminate or modify the Small Fish Rule.[26] Interestingly, in that proceeding, all commenting stakeholders except the petitioner agreed that the Small Fish Rule should be retained without modification.[27] These stakeholders represented a variety of interests in the electricity sector, including public power providers,[28] small and large private generators, and consumers.

In sum, ERCOT benefits from the certainty that the Small Fish Rule provides because it allows market participants to rely on a clear and stable market rule that enhances competition in

[20] Rulemaking on Wholesale Electric Market Power and Resource Adequacy in the ERCOT Power Region, PUCT Project No. 31972.
[21] 2013 State of the Market Report for the ERCOT Wholesale Electricity Markets, Potomac Economics, Ltd at i (Sep. 2014) *available at* potomaceconomics.com/uploads/ercot_documents/2013_ERCOT_SOM_REPORT.pdf. Earlier State of the Market Reports are available at potomaceconomics.com/index.php/markets_monitored/ERCOT.
[22] Rulemaking on Wholesale Electric Market Power and Resource Adequacy in the ERCOT Power Region, PUCT Project No. 31972, Order Adopting Amendment to §25.502, New § 25.504 and New § 25.505 as Approved at the August 10, 2006 Open Meeting at 90 (Aug. 24, 2006).
[23] *Id.*
[24] 2013 State of the Market Report for the ERCOT Wholesale Electricity Markets, at 107-116 (Sep. 2014).
[25] *United States v. Colgate & Co*., 250 U.S. 300, 307 (1919).
[26] Petition of Raiden Commodities, LP for Rulemaking to Remove § 25.504(c), the Exemption from the Market Power Definition for Entities Controlling Less Than 5% of the Generation Capacity in the ERCOT Region, PUCT Project No. 42424, Order Denying the Petition for Rulemaking (Jun. 20, 2014).
[27] *Id.* at 11.
[28] In Texas, public power providers include electric cooperatives (both those who own generation and those who do not), municipal utilities (who own generation), and municipal distribution-only utilities.

the ERCOT market. However, if activity undertaken in compliance with the Small Fish Rule were subject to judicial scrutiny under a private CEA claim then the federal proceeding could raise doubts about the prudence of relying on the rule. The effect would be to impair a market rule that is designed to benefit electricity consumers.

III. CONCLUSION

For the reasons discussed in this letter, the PUCT urges the Commission to remove the Proposed Order's preamble language regarding the reservation of private causes of action under Section 22 of the CEA from exempt transactions under the RTO-ISO Order and the Proposed Order. The PUCT otherwise supports the Proposed Order insofar as it extends exemptive relief to SPP. We thank the Commission in advance for its consideration of these comments.

Very truly yours,

Kenneth W. Anderson, Jr.
Commissioner