

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Collection of Connected Entity Data from
Regional Transmission Organizations and
Independent System Operators

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Docket No. RM15-23-000

**COMMENTS OF THE
INDEPENDENT MARKET MONITOR FOR PJM**

Pursuant to a notice of proposed rulemaking issued in this docket on September 17, 2015 (“NOPR”), Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM (“Market Monitor”), submits these comments on the Commission’s proposal to amend its regulations to require that PJM Interconnection, L.L.C. (“PJM”) and other regional transmission organization (RTOs) and independent system operator (ISOs) electronically deliver to the Commission, on an ongoing basis, data required from market participants that would: (i) identify the market participants by means of a common alphanumeric identifier; (ii) list their Connected Entities, which include entities that have certain ownership, employment, debt, or contractual relationships to the market participants, as specified in this NOPR; and (iii) describe in brief the nature of the relationship of each Connected Entity.

The NOPR explains that such information will assist screening and investigative efforts to detect market manipulation, an enforcement priority of the Commission. The Commission further explains (at P 1): “Unless the RTOs and ISOs request continuation of existing affiliate disclosure requirements based on a particularized need, the Commission expects that this new disclosure obligation will supplant all existing affiliate disclosures requirements contained in the RTOs and ISOs tariffs.”

The Market Monitor strongly supports the NOPR, but is concerned that a final rule establishing reporting thresholds not supplant existing or future market rules that define the threshold for when a market power or manipulation test or rule applies that are more stringent than those proposed in the NOPR. The Market Monitor recommends ways in which the proposal could be enhanced.

I. COMMENTS

A. Need for Connected Entity Information

The Commission cannot effectively protect the integrity of the markets without understanding the relationships between and among participants, and cannot do so efficiently without rules requiring connected entity information. Corporate and other legal distinctions between connected entities obscure the actual structural and financial relationships that result in the behavioral incentives that lead to the exercise of market power and manipulation. If ownership and control and common interest relationships are ignored, or obfuscated or inadequately understood, mitigation and other market protection rules can be easily circumvented. Investigations, including threshold decisions about whether an investigation is needed, often turn on the nature of participant relationships. The lack of current, readily available information in a common electronic format, on ownership in RTO/ISO markets is a vulnerability that should be addressed. The Commission's NOPR addresses the issue.

The fact that most entities will not attempt to exercise market power or to manipulate the markets is not a reason for the Commission not to act on this NOPR. The fact that some entities will attempt to exercise market power and to manipulate the markets is the reason that the Commission needs this information, both to confidently rule out good behavior and to correctly identify bad behavior.

Some commenters have asserted that the reporting requirements in the NOPR would create a substantial reporting burden on ISOs/RTOs and participant members. While the NOPR would impose additional reporting requirements on participants, it is essential

that the agency tasked with the oversight and surveillance of the wholesale power markets have all the information required to do so and that market monitors who identify market power issues for the Commission have access to that information.

The need for data to be readily available and be provided in a common electronic format to facilitate effective monitoring outweighs the desire of participants to minimize burdens. It is critical that the Commission enforce stringent reporting requirements for connected entity data that are required in order to track market transactions and are essential to the ability of the Commission and market monitors to effectively perform their duties with respect to market surveillance which in turn are essential to ensuring that wholesale power markets are competitive.

It is appropriate for the Commission to look for ways to consolidate information requirements and cull requirements for information that is not needed. Proposing a uniform rule across all markets as provided in the NOPR is consistent with that objective.¹ Participants can also look for ways to reduce the burden themselves by reviewing the way they organize and administer their own organizations. The public's need for the Commission to have ready access to timely information should not be compromised.

It is important to note that the information that would be reported is not new information and it is information that market participants must have available. The information is about the ownership structure of market participants, and their key leadership and trading personnel, debt and contracts. In many cases, the information has been assembled, and the requirement is to report that information to RTO/ISOs in a convenient format. The Commission is simply requesting that existing information be compiled into an easily usable and standard format.

¹ See NOPR at P 8.

The NOPR states (at P 13): “We invite comment on the desirability and feasibility of expanding our proposal to require the submission of Connected Entity information from non-RTO/ISO market participants, and on any difficulties commentators might perceive to exist in doing so.”

The NOPR should be expanded to cover all entities that have market-based rates authorization without regard to whether such entity participates in an RTO/ISO. Such entities should report directly to the Commission. It is essential that potential market power and manipulation be addressed wherever the Commission relies on competition-based regulation. Regions of the country lacking organized transparent markets are exposed to market power and manipulation where it is harder to detect than in organized markets.

B. Market Monitor Access to Connected Entity Data

Market monitors are entities whose function and responsibility to monitor the markets for market power and manipulation require use of Connected Entity information. The final rule should specify that market monitors have immediate access to Connected Entity data collected by the associated RTO/ISO. If an RTO/ISO does not want to collect Connected Entity information, the final rule should allow a willing market monitor to assume the responsibility.

C. Disclosure Thresholds

The NOPR specifies four thresholds that define (at P 23) a Connected Entity:

- a. An entity that directly or indirectly owns, controls, or holds with power to vote, 10 percent or more of the ownership instruments of the market participant, including but not limited to voting and non-voting stock and general and limited partnership shares; or an entity 10 percent or more of whose ownership instruments are owned, controlled, or held with power to vote, directly or indirectly, by a market participant; or an entity engaged in Commission-jurisdictional markets that is under common control with the market participant;
- b. The chief executive officer, chief financial officer, chief compliance officer, and the traders of a market participant (or

employees who function in those roles, regardless of their titles);

- c. An entity that is the holder or issuer of a debt interest or structured transaction that gives it the right to share in the market participant's profitability, above a *de minimis* amount, or that is convertible to an ownership interest that, in connection with other ownership interests, gives the entity, directly or indirectly, 10 percent or more of the ownership instruments of the market participant; or an entity 10 percent or more of whose ownership instruments could, with the conversion of debt or structured products and in combination with other ownership interests, be owned or controlled, directly or indirectly, by a market participant; or
- d. Entities that have entered into an agreement with the market participant that relates to the management of resources that participate in Commission-jurisdictional markets, or otherwise relates to operational or financial control of such resources, such as a tolling agreement,[fn: Tolling agreements are common in the energy industry, and in essence function as leasing contracts or options on a generating plant wherein the "toller" has the right to the plant output at his or her discretion.] an energy management agreement, an asset management agreement,[fn: Asset management agreements, in general, are contractual relationships where a party agrees to manage fuel supply and delivery arrangements, including transportation, for another party, and to consume the electricity produced or share in some fashion in the revenues from the sale of that electricity.] a fuel management agreement, an operating management agreement, an energy marketing agreement, or the like.[footnote omitted]

The Market Monitor supports the proposed definition as generally applied to RTO/ISO market participants and all related entities, including natural persons with some suggestions for clarifying and strengthening. The definition is reasonable when applied broadly to all participants and other entities, many of which may not be directly involved in the electric industry. In some particular cases, concerns about potential exercise of market power and manipulation are elevated and the thresholds for reporting should be tighter.

The Market Monitor recommends that category A on ownership be tightened when two entities both participate in an RTO/ISO market (not necessarily the same market). In that case, the threshold level should be reduced to five percent. Five percent would be consistent with the Securities and Exchange Commission's threshold for the requirement that beneficial owners of a class of equity securities of a publicly traded company file a report.² A tighter threshold is appropriate because the potential for the exercise of market power and market manipulation is higher when both entities are market participants.

The ownership reporting threshold should apply only to publicly traded companies. Category A should apply a tighter standard to privately held entities. If two entities are participants in an RTO/ISO market and are privately held, then no percentage ownership threshold should apply to the reporting requirement. Full disclosure is warranted because there is little publicly available information about privately held entities.

Category D on contractual relationships should be enhanced by including two additional example type agreements. Joint venture agreements should establish connected entities. Likewise, derivative instruments which are linked directly or indirectly to market results in an RTO/ISO market should establish connected entities. For example, a derivative

² 17 CFR § 240.13d-1(d). This SEC regulation promulgates Section 13 of the Securities Exchange Act of 1934, which requires certain investors to submit beneficial ownership reports. Such reports must disclose details such as the investor's identity and other holdings. The purpose of Section 13 is "to promptly arm market participants with information concerning potential changes in corporate control in order to allow them to make more informed investment decisions." Adam O. Emerich, et al., *Fair Markets and Fair Disclosure: Some Thoughts on the Law and Economics of Blockholder Disclosure, and the Use and Abuse of Shareholder Power*, 3 *Harv. Bus. L. Rev.* 135, 144 (2013), citing S. REP. NO. 90-550 at 3 (1967) ("The bill is designed to require full and fair disclosure for the benefit of investors while at the same time providing the offeror and management equal opportunity to fairly present their case."); *see also id.* at 4 ("The bill would correct the current gap in our securities laws by amending the Securities Exchange Act of 1934 to provide for full disclosure in connection with cash tender offers and other techniques for accumulating large blocks of equity securities of publicly held companies."); H.R. REP. NO. 90-1711 at 8 (1968) ("The purpose of section 13(d) is to require disclosure of information by persons who have acquired a substantial interest, or increased their interest in the equity securities of a company by a substantial amount, within a relatively short period of time.").

instrument that references FTR payouts could create benefits from virtual trades affecting an FTR position that a participant does not actually hold. Such an arrangement could create the same incentive for uneconomic and manipulative behavior that an unchecked opportunity to trade virtuals on FTR positions creates. To take another example, a joint venture arrangement could be used as conduit to share information to facilitate collusion. Joint venture agreements and derivative instruments are strong examples of contractual links that could be exploited to exercise market power or to engage in market manipulation.

Category D should also explicitly include as reportable contractual arrangements every case where an entity is responsible for deciding how a market participant behaves in the market.

Category D should also require market participants to provide the underlying contracts to market monitors, the Commission and RTO/ISOs when requested as part of an investigation.

D. Existing Disclosure Requirements

The Commission states (at P 1): “Unless the RTOs and ISOs request continuation of existing affiliate disclosure requirements based on a particularized need, the Commission expects that this new disclosure obligation will supplant all existing affiliate disclosures requirements contained in the RTOs and ISOs tariffs.”

The Connected Entity definition should serve as a threshold for standardized reporting only. The definition should not supplant existing or future standards that define the threshold for when a market power or manipulation test or rule applies, and the information that a participant may need to supply to enable the RTO/ISO’s implementation of the market power or manipulation test or rule or to enable the Market Monitor’s fulfilment of its functions and responsibilities or to enable the Commission’s enforcement of market power and manipulation rules.

The ownership and control tests and rules applied to market participants as they relate to other market participants under various market power and manipulation rules,

such as the three pivotal supplier test, must be subject to a more stringent threshold than the Connected Entity threshold, particularly the ten percent threshold applied to ownership in category A. Examples from current market participants show that some members have very complex webs of interconnected affiliates and other relationships which make it difficult and/or ambiguous to infer or define the exact ownership share held by connected entities. Ownership interests of less than ten percent can be material to creating incentives for the exercise of market power or manipulation.

The Market Monitor is concerned, for example, to ensure the continued functioning of the FTR forfeiture rule, which has prevented market participants from using virtual trades to manipulate the value of FTR positions. The protection afforded by the FTR forfeiture rule is critical and should not be disturbed. Use of virtuals to manipulate FTR positions in unprotected markets has resulted in multi-million dollar fines.³ The FTR forfeiture rule uses the term “FTR holder” to define an entity or related entities that could benefit from the use of virtuals to manipulate the value of FTR positions. PJM and the Market Monitor have interpreted and applied the term FTR holder broadly to account for relationships material to the behavior that the rule is designed to automatically detect and prevent. Based on its experience implementing the rule, the Market Monitor’s position is that a ten percent threshold is too high as an enforcement threshold.⁴

For example, the Market Monitor has developed the following definition:

“Effective FTR Holder” shall mean an FTR Holder, any Affiliate, a subsidiary or parent of the FTR Holder, or any other entity that is under common ownership (including passive ownership), directly or indirectly, wholly or partly, with the FTR Holder, except that common ownership shall not include an individual’s passive

³ See *MISO Virtual and FTR Trading*, 146 FERC ¶ 61,072 (2014); *Deutsche Bank Energy Trading, LLC*, 142 FERC ¶ 61,056 (2013).

⁴ See *RTO Energy Trading, LLC, Petition for Declaratory Order of RTO Energy Trading, LLC and Request for Confidential Treatment*, Docket No. EL15-38-000 (January 26, 2015).

ownership of less than one percent of an entity's publicly traded securities.

If the market monitors and ISOs/RTOs and Commission have more stringent thresholds for market power and manipulation screens or develop such screens in the future, the market monitors and ISOs/RTOs and the Commission should be allowed to use the information collected independently for mitigation and anti-manipulation actions.

Defining hard thresholds, such as ten percent ownership levels, and other aspects of the tests for ownership and control invite stratagems to circumvent the rule's protection. As Commissioner Clark has observed:

[A] regulator like FERC cannot possibly create an all-inclusive list of prohibited activities.[footnote omitted] There simply is no exhaustive or comprehensive rulebook of all possible scenarios that would result in violations of our anti-manipulation rule—so market participants, shareholders, and regulators must rely on the *use of judgment*. Industry may demand clear instructions via proscriptive rules, but industry still must make judgment calls.⁵

If the NOPR definition is accepted, particularly if the NOPR is finalized without the additional subcategories for Connected Entity status that the Market Monitor recommended, the NOPR should explicitly permit the Commission, market monitors and RTO/ISOs to preserve existing rules or develop new rules that apply a lower threshold and/or case-by-case thresholds to relationships between or among market participants.

For some other existing applications the Connected Entities reporting thresholds may also be too high. The Market Monitor agrees with the IRC/RTO Council that some rules including code of conduct rules and the calculation of credit limits require tighter thresholds than defined by the Connected Entities NOPR.⁶

⁵ Tony Clark and Robin Z. Meidhof, "Speeches: Ensuring Reliability and a Fair Energy Marketplace," Colorado Nat. Res., Energy & Env. L. R. v. 25, Issue 2, which can be accessed at: <<http://www.colorado.edu/law/sites/default/files/Clark%20%26%20Meidhof%2025-2.pdf>>.

⁶ Comments of the RTO/ISO Council, Docket No. RM15-23-000 (January 22, 2016) at 4.

The Market Monitor recommends that a final rule remove the NOPR's requirement "eliminating all existing affiliate disclosure requirements."⁷ Likewise the requirement that RTO/ISOs specify requirements to be retained and provide "justifications for such retentions" should be removed. RTO/ISOs should be encouraged to streamline their requirements where appropriate and where they serve no protective purpose, but they should not be required to do so. The legal and administrative burden should continue to rest with those seeking to change RTO/ISO rules, including disclosure requirements that require more information than the information provided regarding Connected Entities.⁸

The NOPR states (at P 23): "We invite comment on the appropriate threshold for a *de minimis* share of a company's profits." The Market Monitor recommends not attempting to define *de minimis* share of a company's profits. If the underlying agreements provide for sharing of profits, by definition the rights to those profits are worth defining and are significant and not *de minimis*.

E. Reliance on LEI System

The NOPR states (at P 23): "we invite comments on the feasibility of [the LEI system's] use, on whether any other system besides LEIs would be a preferable method of achieving uniform identification, and on whether waivers might be appropriate in given situations." The Market Monitor agrees that there must be an accurate, unique identifier for every Connected Entity. The LEI system appears to meet the Commission requirements for a unique identifier, but the Market Monitor takes no position on whether there is another source of unique company identifiers.

The proposed rule provides:

"...The submittal shall include information concerning each market participant's Connected Entities, together with the Legal

⁷ NOPR at P 35.

⁸ *Id.*

Entity Identifiers of the market participants and their Connected Entities (*if known*), as submitted to the regional transmission organization or independent system operator by the market participants...”

The parenthetical phrase “if known” is potentially confusing, and it could be interpreted as a way to avoid compliance. If an entity does not know its LEI, it should have the burden to discover and report it. If an entity has no LEI, it should be required to secure an LEI.

F. Formatting Requirements

The NOPR states (at P 34): “We invite comments on formatting suggestions...”

It is essential that information be provided electronically in a format that facilitates ease of use, including the ability to efficiently search and sort.

A number of commenters have suggested that the NOPR may result in duplicative reporting requirements. None have suggested that there is an efficient way for the Commission to have ready and efficient access to any such information that may be filed with other agencies or even with the Commission in hard copy or in PDF or other relatively inaccessible formats. That is one essential change that the NOPR would bring. Without that immediate access in electronic form, the data is essentially useless. The NOPR is likely to be a path towards streamlining reporting requirements rather than imposing duplicative requirements. Under the NOPR, the data would be timely and required to be kept up to date, a requirement that is frequently not included in other reporting requirements cited by commenters.

G. Audit Authority

The NOPR states (at P 31): “We propose that the RTOs and ISOs include in their tariffs the authority (although not the obligation) to audit market participants to determine if their submitted Connected Entity data is accurate, complete, and up to date.” In comments filed in the technical conference, the ISO/RTO Council indicated that some of its constituents “may not be adequately staffed to perform this function, nor would it be

within their jurisdictional responsibility to audit the relationships that establish a Connected Entity designation.”⁹

The Market Monitor supports the proposal, and recommends that separate authority be conferred on RTO/ISO market monitors. The PJM Independent Market Monitor currently researches, tracks, updates and maintains the affiliate and corporate ownership information of PJM market participants. The Market Monitor provides this data to PJM on an ongoing basis. Assigning audit authority to market monitors would leverage the market monitors’ expertise in tracking and evaluating affiliate relationships. The Market Monitor recommends giving market monitors the authority to audit the ownership data either in place of, if the RTOs/ISOs do not want the authority, or in addition to the RTO/ISOs.

H. Condition for Market Participation

The NOPR states (at P 30): “As a condition of participating in any of the RTO/ISO markets, the market participants would have to have on file with that RTO or ISO their Connected Entity data, which must be updated within 15 days of a change in status of the data.” Requiring participants to maintain current information is appropriate. The burden of maintaining accurate data belongs on the participants and not on the ISOs/RTOs (or market monitors) that collect the data.

The Market Monitor supports this requirement because it creates a significant and appropriate incentive for compliance.

I. Benefits of Collecting Connected Entity Information

The NOPR states (at P 18): “Establishing common identifiers and a uniform definition of Connected Entity, as is proposed in this NOPR, would have the additional benefit of assisting the RTO/ISO market monitors in their responsibilities to oversee the markets.”

⁹ Comments of the ISO/RTO Council, Docket No. RM15-23-000 (January 22, 2016) at 2.

The Market Monitor supports this requirement and proposes specific areas of the NOPR in which this requirement should be made explicit in addition to the general requirement.

There is also a significant benefit to the markets when ex-ante market power mitigation and ex-post screens for market power and market manipulation are applied using the best available information. In PJM, the three pivotal supplier (TPS) test is embedded in the unit commitment and dispatch software in the PJM Day-Ahead Energy Market, the PJM Real-Time Energy Market, the PJM Regulation Market and the PJM Capacity Market. The TPS test is a test for structural market power in local markets created by transmission constraints and is based on pivotal supplier analysis on a supplier/owner level. The TPS test requires accurate information on ownership.

The PJM FTR forfeiture rule also relies on accurate information on ownership. The FTR forfeiture rule requires the forfeiture of FTR profits when the virtual activity of the market participant increases the value of congestion on the FTR path above the real-time congestion value. It is possible to attempt to evade the rule by having one affiliate trade FTRs and another trade virtuals or one entity coordinate market activity across seemingly unrelated entities. It is essential to know the relationships among entities in order to accurately implement the PJM FTR forfeiture rule.

The Connected Entity information collected by the RTOs/ISOs and the associated rules on updating and maintaining the data would directly help in accurately administering the TPS test, the FTR forfeiture rule and the associated market power mitigation actions.

J. Scope of Data Collection

While the Commission's scope of this NOPR is collecting information from participants in power markets to enhance monitoring wholesale power markets, a number of participants in the power markets have affiliates that have business operations in the natural gas, oil and other energy markets that the Commission also oversees. These affiliate entities often trade among each other for fuel procurement purposes, and this effort will

enhance the monitoring of possible cross market manipulation among the different energy markets.

K. Burden and Impact

The information on participant relationships identified by the Commission is essential to monitoring the wholesale power markets. It is nonetheless appropriate to carefully consider the potential impacts on market and non-market participants. In that consideration, the burden should be on those entities who believe that certain data should not be collected to demonstrate that the requested data is not relevant to the monitoring and oversight of the wholesale power markets. Market participants are, in some cases, part of complex corporate structures which may or may not be relevant to behavior in the wholesale power markets. Market participants, in some cases, have created complex corporate structures for the purpose of obfuscating actual control relationships.

The presentation of either actual examples or examples based closely on actual experience could help illustrate the concerns of commenters and enable the objective evaluation of those concerns and the appropriate modification of the NOPR if appropriate.

Concerns about regulatory risk are misplaced. The regulatory risk now falls on the Commission, the RTO/ISOs, the market monitors and other market participants. This means that the risk is borne by all market participants including producers and consumers that the Commission, the RTO/ISOs and the market monitors have the duty to protect. The NOPR, if implemented, will appropriately place the risk associated with exercising market power or manipulating markets across Connected Entities appropriately on those entities.

II. CONCLUSION

The Market Monitor respectfully requests that the Commission afford due consideration to these comments as the Commission resolves the issues raised in this proceeding.

Respectfully submitted,



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