

JOSEPH T. KELLIHER

September 30, 2003

The Honorable Ron Wyden
United States Senate
Washington, D.C. 20510

Dear Senator Wyden:

I am writing to clarify my views on two issues of importance to you: Standard Market Design and market manipulation.

You have forcefully stated your opposition to the Commission's Standard Market Design. In particular, you have expressed concern that market rules developed in other regions of the country may not work in the Pacific Northwest, and emphasized the potential economic impact of the proposal on your region.

I recognize electricity markets are not national, but regional. There are significant differences among the regions – the transmission grids are different, the generation mixes are different, and the market structures are different. There are also significant legal differences – the role of nonjurisdictional utilities such as the Bonneville Power Administration and municipal utilities is more significant in the Pacific Northwest than other regions. It is essential that market rules reflect these important regional differences.

For these reasons, I do not believe imposition of uniform national market rules on your region is appropriate. I support regional flexibility, and if confirmed by the Senate I would give great deference to the views of your region. Further, I am not convinced there is a need for a final rule on Standard Market Design. A better means of achieving regional flexibility may be through regional proceedings.

Because of the unique regional characteristics in the Pacific Northwest, I believe any effort to form a regional transmission organization should be voluntary. In my view, the Commission could not successfully mandate the establishment of a regional transmission organization for the Pacific Northwest, nor should it attempt to do so.

Markets that are subject to manipulation cannot operate properly. For that reason, I believe there is an urgent need to proscribe manipulation of electricity markets. There is no express prohibition of market manipulation in the Federal Power Act. That stands in contrast with the regulatory laws governing other industries, such as securities and commodities. Market manipulation should be expressly prohibited.

In addition, penalties must be sufficient to discourage market manipulation. Well before the Western electricity crisis I advocated tougher criminal and civil penalties. In my view, the penalties set by Congress in the Federal Power Act are no longer adequate to discourage criminal behavior. They need to be increased.

The Commission has some ability to address market manipulation absent Congressional action. In my opinion, the Commission has legal authority to proscribe certain market manipulation practices by jurisdictional utilities. The Commission also has discretion to revoke authorization of a public utility to sell power at market-based rates as a remedy for market manipulation. I would support exercise of this authority.

In the past, you discussed the relationship between spot markets and long-term markets. As you know, in its "Final Report on Price Manipulation in Western Markets" the Commission staff concluded spot prices influenced forward prices. As a general matter, I acknowledge there is a relationship between spot markets and forward markets.

There is no question the Commission has legal authority to reform contracts. In the right circumstances, contract reform is appropriate. If it can be demonstrated that any Pacific Northwest contracts impose an excessive burden on consumers or are unduly discriminatory, or that fraud or duress were present at the time of contract formation, then I believe contract reform would be appropriate. You have expressed your strongly-held view that the just and reasonable standard should govern in contract reform cases. I respect your view, and note there is legal precedent supporting your position. I have not prejudged which legal standard should govern in contract reform cases, and Federal courts have applied both the public interest standard and the just and reasonable standard. As you know, the Commission applied the public interest standard in recent contract reform cases. I have not prejudged whether these cases were correctly decided.

I appreciate the opportunity to share my views with you on these matters.

Sincerely,



Joseph T. Kelliher