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To: NYISO Management Committee

From: Chris LaRoe

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Re: IPPNY Comments on the Proposed Changes to the RS 1 Cost Allocation

At the May 18, 2011 Budget & Priorities Working Group (“BPWG”) meeting, the NYISO’s consultants, Black & Veatch (“B&V”), presented its draft Rate Schedule 1 (“RS 1”) study report (“Draft Report”). Many questions and concerns were raised concerning the assumptions used for, and the overall conclusions of, the Draft Report. However, Market Participants agreed to forego further discussions at that time -- including discussions concerning possible amendments to correct deficiencies inherent in the Draft Report -- in the hope that settlement discussions would produce an acceptable outcome. In addition, at the outset of this process, the Independent Power Producers of New York, Inc., (“IPPNY”) along with several of its individual members, requested that B&V be directed to conduct an analysis comparing the proposed cost allocation by service category between the 2011 B&V study and the 2004 Rudden study (“RS 1 Comparison Assessment”). That comparison was not provided to Market Participants until the June 23rd BPWG meeting. While RS 1 was listed as a discussion item for that meeting as a placeholder, settlement discussions were ongoing between parties at that time. Thus, there were no substantive discussions at that meeting concerning either the Draft Report or the RS 1 Comparison Assessment.

Despite the good faith efforts of all involved, no settlement was achieved; impasse was declared on July 15, 2011 and the NYISO was notified accordingly. On July 20, 2011, the NYISO issued the agenda and meeting materials for the July 27, 2011 Management Committee meeting. The July MC agenda includes discussion and action on the RS 1 cost allocation issues. The RS 1 meeting materials includes a final report issued by B&V (“Final Report”).

While we are still reviewing the Final Report, it does not appear to have been changed significantly since the May 18th BPWG meeting notwithstanding the numerous concerns raised at that time. Initially, IPPNY requests that the RS 1 action item be deferred until the August meeting to give parties an opportunity to understand what, if anything, has changed in the report and to provide an opportunity to ask questions of, and get input from, B&V concerning the contents of the Final Report and the RS 1 Comparison Assessment. IPPNY would note that a one month period would not adversely affect a January 1, 2012 implementation of any revised RS 1 cost allocation that is approved by the FERC.

While the Final Report remains under review at this time, IPPNY has identified a number of shortcomings with the Final Report and, specifically, with B&V’s conclusion that, “Ultimately, if bundled rates are to be continued, we recommend a change from the current 80/20 split to a split that is at or around

the midpoint of 72/28. We find that the upper and lower bounds of the studies represent the limits of what would be reasonable, and therefore recommend a split near the midpoint as a reasonable settling point.” (See Final Report at 2.) While not exhaustive, IPPNY hereby provides a preliminary list for illustrative purposes:

- As reflected in the RS 1 Comparison Assessment, B&V has determined that the Rudden Study categories of system reliability, real time operations and energy and ancillary services markets would have produced a 78% load/22% supply split. IPPNY would note that the Rudden Study was never approved; settlement was reached ending further discussions to address the shortcomings inherent in therein. B&V now proposes to assign costs for these very same categories on a 72% load/28% supply basis. B&V, however, fails to provide an adequate justification for such a significant shift in costs, particularly given the fact that there have been very few changes to the market design in the intervening period. These costs account for nearly 70% of the NYISO’s administrative budget, and thus, the proposed change in their allocation substantially affected B&V’s proposed increase of the RS 1 costs to suppliers from 20% to 28%, a 40% increase when, again, there have been no changes in the market design of a sufficient enough magnitude to account for this substantial shift in costs.

- At the time the Rudden Study was conducted, there were no significant “system and resource planning” functions within the NYISO, and thus, no separate category to allocate the costs associated therewith. The NYISO now has a system and resource planning function that accounts for nearly 20% of its budget, making it the NYISO’s second largest cost category. IPPNY would note that ISO-NE also has a system planning category. B&V has reported that these costs are allocated in New England 100% to load. However, B&V inexplicably has assigned the NYISO system and resource planning costs on a 74.2% load/25.8% supply basis. Both system and resource planning focus on the reliability of the system, and thus, the full costs for such service should be allocated 100% to load as ISO-NE correctly has recognized.

- As part of its analysis, B&V reviewed the cost allocation percentages of all other ISOs. Taking out the outliers on both sides, the New England, PJM and MISO markets provide a legitimate basis for comparison. As reflected in the Final Report, the load share in each of these markets is 78%, 79% and 75%, respectively. Importantly, while the specific rules vary from market to market, each of these markets have the same basic categories, and hence, cost centers as the NYISO (e.g., energy and ancillary services markets, FTRs, capacity, resource and system planning). Were the B&V Final Report to be accepted, New York would catapult overnight from the lowest of the four adjacent ISOs to the highest -- and by a significant margin as compared to New England and PJM. Again, this unjustifiably would take place in the absence of any changes to the NYISO market design of such a significant magnitude in the intervening period so as to warrant such a substantial change in the allocation of RS 1 costs.