Hon. Richard J. Grossi
Chairman, Board of Directors
New York Independent System Operator, Inc.
C/o William J. Museler
President & CEO
New York Independent System Operator, Inc.
3890 Carman Road
Schenectady, NY 12303

Re: Motion of New York State Electric & Gas, and Rochester Gas and Electric Corporation In Opposition To LIPA's and Consolidated Edison of New York, Inc., The City Of New York, and Consumer Power Associates' Appeals Of The Management Committee's February 7, 2002 Decision To Approve The Congestion Reduction Proposal

Dear Chairman Grossi:

Pursuant to Section 5.07 of the ISO Agreement and Article IV of the Procedural Rules for Appeals to the ISO Board, New York State Electric & Gas Corporation ("NYSEG"), and Rochester Gas and Electric Corporation ("RG&E) (hereinafter, the "Companies") hereby submit their Notice of and Motion in Opposition to the Appeals submitted by LIPA and Consolidated Edison Company of New York, Inc., The City of New York, and Consumer Power Associates ("ConEd") regarding the Management Committee's February 7th decision to approve the Congestion Management Proposal. The Companies respectfully request that the Board reject LIPA's and ConEd's requests for appeal and support the Management Committee's decision, which was arrived at following months of discussion and enjoyed overwhelming market participant support.

The Companies also oppose LIPA's request for a hearing before the Governance Committee because it is unnecessary. ConEd and LIPA participated extensively during development of the Congestion Reduction Proposal in the Market Structures Working Group, the Business Issues Committee ("BIC"), and in the Management Committee. Market Participants considered the concerns raised by LIPA and ConEd and, in the aggregate, concluded that the benefits to be gained by customers of the NYISO strongly outweighed the concerns raised by LIPA and ConEd. The Congestion Reduction Proposal was approved by a vast majority of the participants in the BIC on two separate occasions and by the Management Committee on February 7th. A hearing is unlikely to lead to the discovery of any additional relevant information, and LIPA and ConEd have already stated their positions in motions to the various committees and in the instant appeals. The record is complete. However, to the extent that the Governance Committee finds it necessary to grant LIPA's request for a hearing, the Companies request an opportunity to respond during that hearing to LIPA's comments.

Sincerely,

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Consulting Engineer
Transmission Services
New York State Electric & Gas
Corporation

Clifton B. Olson
Vice President
Rochester Gas and Electric
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cc: NYISO Board of Directors
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Motion of New York State Electric & Gas, and Rochester Gas and Electric Corporation (the "Companies") In Opposition To LIPA's and Consolidated Edison of New York, Inc.'s Appeals Of The Management Committee's February 7, 2002 Decision To Approve The Congestion Reduction Proposal

Summary

The Companies offer the following rebuttal to each of the arguments raised by LIPA and Consolidated Edison Of New York, Inc., The City of New York, and Consumer Power Associates ("ConEd"). The Companies also offer the background and explanation necessary to aid the Board in its understanding of the complex and sometimes confusing concepts of congestion rent shortfalls, congestion rent surpluses, and congestion rent revenues. Once the origin of each of thee revenue streams is understood, the Board will recognize LIPA's and ConEd's attempts to confuse these different revenue streams to make it appear as though they, and not all other market participants, are being economically disadvantaged.

In summary, ConEd and LIPA ask that they continue to be rewarded financially for transmission service that they do not provide over transmission facilities that they do not promptly restore to service. This financial reward comes in the form of congestion rents for Transmission Congestion Contracts ("TCCs") that do not exist when facilities are in an outage because they are not simultaneously feasible with the TCCs that do exist. The Congestion Reduction Proposal (the "Proposal") was developed to provide a financial incentive to all Transmission Owners to reduce transmission system congestion by scheduling their system outages at times of low congestion, and to complete those outages quickly and safely. Of all the New York Transmission Owners, only ConEd and LIPA oppose this improvement, notwithstanding that the Proposal will facilitate the reduction of energy prices for their customers through reduced congestion costs.

The Companies respectfully request that Board support the Management Committee's approval of the Proposal. In the interest of addressing the concerns raised by LIPA and ConEd, the Companies also request that Board consider, without delaying the implementation of the Proposal, directing the NYISO staff to expeditiously complete:

- Development of methodologies to reduce TCCs offered in the NYISO's TCC auction to ensure simultaneous feasibility as required by the NYISO OATT.

- Studies of the current allocation methods for congestion rent shortfalls and excesses, and to the extent necessary and feasible develop alternative methods to ensure equitable distribution of the excesses and surpluses in accordance with the principle that shortfalls and surpluses be allocated to the owners of the facilities on which the shortfalls and surpluses occur.

Rebuttals To Specific Arguments

1. LIPA's Argument - that Transmission Owners that Conduct Their Outages in Accordance with Good Utility Practice Should be Exempt from Financial Accountability for those Outages in the Form of a Counter-Flow TCC - is Without Merit and Would Eviscerate The Proposal

All outages are presumed to be conducted in accordance with Good Utility Practice. LIPA's proposed change would not merely modify the proposal – it would negate it. No transmission owner should ever conduct an outage inconsistent with regionally-accepted utility practices. LIPA clearly misunderstands the reason for the Counter-flow TCC. The Counter-flow TCC is not a punishment imposed on a Transmission Owner for failing to follow standard facility maintenance procedures. The Counter-flow TCC is a financial incentive intended to motivate all Transmission Owners to schedule their outages during periods of lower congestion and to return those facilities to service quickly, and safely, and in a manner consistent with the NYISO approved outage schedule. Reducing outage length will necessarily reduce congestion costs.

LIPA argues that it will now have to bear the cost of maintaining its facilities as well as the cost associated with the Counter-flow TCC. Of course it will – it owns the facilities, and, like every other Transmission Owner, it is responsible for facility maintenance and operation. By scheduling outages during periods of lower congestion (e.g., during shoulder months and off-peak hours), LIPA can reduce its financial exposure and benefit from reduced locational energy prices as congestion is reduced. To the extent LIPA passes through its energy cost savings, LIPA's customers will benefit. Further, to the extent that LIPA, or any other Transmission Owner, can return its facilities to service before the return-to-service date scheduled with the NYISO, that owner may receive additional revenue as excess congestion rents.

Contrary to LIPA's argument, there is nothing antithetical about requiring a Transmission Owner to plan its transmission outages in a manner that reduces congestion in an area where congestion reduction is sorely needed. Optimizing transmission outage performance is good for the system and beneficial for transmission customers. In no way does such a process negatively affect grandfathered rights or violate the ISO-TO Agreement, as LIPA and ConEd suggest.

2. Con Ed and LIPA's Arguments that the Proposal Discriminates Against Underground and Underwater Transmission Line Outages is Incorrect.

First, LIPA argues that underground and underwater cables are harder to maintain and that the outages for these facilities are longer than for overhead lines. Surely a sophisticated owner and operator of transmission lines such as LIPA recognized that underwater and underground cables would be more difficult to maintain. In choosing these types of facilities, LIPA must have also weighed the added benefits associated with their use. No one is in a better position to bear the risks inherent in the choice of technology than the entity that carefully assesses the risk and benefits and ultimately chooses a particular technology. This is precisely the reason why LIPA and ConEd should have a direct financial incentive for improving their maintenance techniques and restoring their transmission assets to operation as quickly as technology permits. As it stands now, there is no incentive because LIPA and ConEd pay a disproportionately small share of the congestion rent shortfalls that occur when their facilities are out of service. The Proposal does not discriminate between above ground and below ground/water facilities. All facilities are treated the same.

Second, LIPA complains that its underwater cables (and associated TCCs) connect two regions with large-differential LBMPs, which will impose significant costs if LIPA is assigned a Counter-flow TCC associated with its outages. LIPA fails to mention that it is the large-differential in LBMPs that makes its TCCs so valuable. In essence, LIPA argues that it is entitled to receive all the revenue associated with these valuable TCCs, and that it should continue to receive this revenue even when its facilities are in outage and not providing transmission service. According to LIPA, its should not be responsible for the outage congestion costs because those costs (which are based on the same high LBMP differential) would be greater than the congestion costs that would be paid by other Transmission Owners who own less valuable transmission facilities. LIPA's complaint evidences how unbalanced and inequitable the current process is and how important it is to make Transmission Owners directly responsible for the congestion costs that their outage management practices impose on others.

ConEd goes so far as to say that the proposal discriminates against companies like LIPA and ConEd that rely on forced outages to maintain their facilities (i.e., fixing the facilities after they break) and in favor of companies that rely on planned outages (i.e., maintaining facilities so that they will not break). Con Ed Motion at 3-4. It is safe to say that most market participants, most Transmission Owners, and the Public Service Commission would prefer that transmission facilities be maintained on planned and consistent prospective basis rather than fixing facilities after they break. The Proposal provides an incentive to all Transmission Owners to take a practical approach to efficiently scheduling transmission line outages when they will have the least effect on congestion, and to quickly and safely restore facilities that are in outage back to service.

3. LIPA's and Con Ed's assertion - that the sole purpose of the congestion reduction proposal is to reallocate congestion rent shortfalls while maintaining the existing allocation of congestion rent surpluses, and that such a result is inequitable - is inaccurate and disingenuous.

First, a clearly stated purpose of the proposal is to reduce congestion costs by minimizing outage duration and providing an incentive for transmission owners to perform outages during periods of reduced congestion. It is completely appropriate that the Transmission Owner that controls the maintenance of its facilities should be responsible for the costs that are a direct result of how and when its facilities are maintained. No other entity, other than possibly the NYISO (and then only to a limited extent) can direct the facility owner's maintenance activities. Any financial incentive directed at improving the way outages are conducted can only be effective when directed at the party that has control.

Second, Objective 4 of the proposal that commits the NYISO, as an objective and disinterested body, to consider and study more equitable allocation processes is intended to address any potential inequities in the way that congestion rent surpluses and shortfalls are allocated. Many market participants, including the Companies, support this objective and have asked the NYISO to study and propose alternate allocation processes to the extent that current processes are inequitable. Of course, if the process that ultimately results in congestion rent surpluses being allocated to owners of the facilities on which those surpluses are generated, LIPA stands to receive nothing. Surpluses can only be generated on facilities that are not fully subscribed (i.e., facilities with capacity that has not been sold in the TCC auction or grandfathered under a pre-existing transmission agreement in place prior to the start of the NYISO). As LIPA has continuously pointed out, the Y-49 and Y-50 cables are fully subscribed and, therefore, cannot generate congestion rent surpluses. The Companies support evaluation of alternative allocation methods but stress that evaluation of these alternatives should not in any way delay implementation of the Proposal.

Third, arguments that equity requires congestion rent surpluses be allocated in the same manner as congestion rent shortfalls are wrong. These arguments presume that congestion rent shortfalls and surpluses are equally likely to occur on the same transmission facilities. This presumption is, however, false. Congestion rent surpluses are generated on transmission facilities that are not fully subscribed by TCCs, that is more transmission capability is available in the NYISO's day-ahead market than was sold as TCCs. This excess capacity will generate surpluses. Shortfalls on the other hand are generated on transmission facilities that are fully subscribed by TCCs but have their capability reduced prior to scheduling of transactions in the NYISO's day-ahead market. For examplethe Y-49 and Y-50 transmission cables are unlikely to generate congestion rent surpluses because they are fully subscribed with TCCs, but they most assuredly have resulted in congestion rent shortfalls. Under the current allocation methodologies when the applicable Transmission Owner removes the fully subscribed Y-49 or Y-50 lines from service for an outage, the entity that holds the grandfathered TCCs continues to receive the associated congestion rents on facilities that are not providing transmission service. Since the lines, are out of service a congestion rent shortfall occurs which is currently funded by all of the New York Transmission Owners. This is inequitable because only the actual owners of those lines have any ability to return the lines to service and minimize the congestion rent shortfall.

The rationale behind allocating on a similar basis congestion rent surpluses and shortfalls was premised on providing a simple means of allocating small revenues without performing complex evaluations to determine which facilities actually generated surpluses and shortfalls. But the NYISO Open Access Transmission Tariff ("Tariff") also provided that the NYISO would reduce the number of TCCs when needed (e.g., for outages) to ensure that all TCCs were simultaneously feasible and funded – an underlying tenet of the business solution to which Con Ed and LIPA refer. By ensuring that only an amount of simultaneously feasible TCCs were sold, the congestion rent shortfalls and surpluses were anticipated to be small. Attachment M of the NYISO OATT provides that the NYISO will reduce the amount of grandfathered rights (including Grandfathered TCCs and residual TCCs) to ensure simultaneous feasibility. See Attachment M, Original Sheet Nos. 565-66.

4. LIPA's characterization of the Business Solution is Incorrect

LIPA mischaracterizes the purpose behind the business solution. LIPA Motion at 5. The business solution was not designed to ensure that Transmission Owners like LIPA and Con Edison would not have to bear the economic consequences when their transmission lines were in outage or that sharing these cost with other Transmission Owners was a tradeoff for other provisions that were less favorable to LIPA and ConEd. The business solution was intended to prevent cost shifting between transmission owners in connection with certain grandfathered transmission agreements. The discussions that led to the development of the Congestion Reduction Proposal and the ultimate Management Committee approval demonstrate that the current allocation methodology is not equitable.

5. The Congestion Reduction Proposal Does Not Diminish Grandfathered Rights or TCCs

LIPA and ConEd claim that the congestion reduction proposal will diminish their rights under Existing Transmission Agreements, which were in effect at the commencement of the ISO, and that such action violates the terms of the ISO/TO Agreement. This claim is incorrect. The holders of TCCs that are derived from grandfather transmission agreements, indeed all TCC holders, will continue to receive full funding of their TCCs. The Congestion Reduction proposal only changes the responsibility for funding the congestion rent shortfalls, which has no impact on TCC holders.

Additionally these arguments ignore the simple fact that LIPA's and ConEd's grandfathered arrangements relating to the use of those facilities did not purport to hold either LIPA or ConEd harmless in the event of an outage of their facilities. Instead, prior to the formation of the NYISO, LIPA and ConEd received the benefits of those transmission facilities only when they were operational. As a result of the substantial differences in market prices between Long Island and the rest of New York State, LIPA in particular had powerful economic incentives to maximize the availability of these transmission facilities.

Inexplicably, provisions that would have made the grandfathered rights and TCCs consistent with the Existing Transmission Agreements, namely adjustments related to outage conditions were not carried over into the NYISO operation. The Congestion Reduction Proposal proposes only to restore LIPA and Con Edison to the situation in which they found themselves prior to the formation of the NYISO. This result cannot be regarded as depriving LIPA or ConEd of any of their "grandfathered" rights under their pre-existing transmission arrangements. Simply stated, LIPA and ConEd cannot be allowed to use the grandfathering provisions of the NYISO OATT and the NYISO/TO Agreement to achieve any greater protection from the costs of outages of these transmission facilities than they had under the arrangements in effect immediately prior to NYISO startup.

6. ConEd's Argument that the Proposal will Chill Downstate Transmission - Line Construction is Unsubstantiated and Illogical

ConEd argues that new transmission-lines to Long Island will have to be located underground or underwater but that developers will no longer build these facilities because they will be responsible for the congestion rent shortfalls. ConEd offers no proof of this assertion. The Companies believe that so long as a high LBMP differential exists between Long Island and the rest of New York and New England, developers will continue to propose projects to serve Long Island. Recognizing that there are financial incentives in place to simplify and optimize outage scheduling and performance procedures, developers will have an incentive to select technologies that are reliable and more easily maintained. Recognizing this demand, manufacturers of underground and underwater facilities will have an incentive to improve their equipment to provide for ease of maintenance. On the other hand, if underground or underwater facilities are more costly and less reliable, then developers will choose alternative facility designs. The last thing the market should do is provide an incentive to continue constructing costly and unreliable facilities by offering developers that use these facilities a free-ride.

7. ConEd's Argument that the Proposal Fails to Address the Cause of Congestion Rent Shortfalls is Wrong.

ConEd argues that the proposal does not address the reason behind congestion rent shortfalls – that the NYISO offers for sale TCCs that do not really exist because of facility outages. ConEd complains that the NYISO should reduce the TCCs that are auctioned based upon historic outage data and that such a process would be similar to the NYISO's unforced capacity process.

The Companies support developing a methodology that would allow a reduction in TCCs to accommodate outages and, in fact, the NYISO Tariff requires that staff consider outages in assuring simultaneous feasibility of TCCs. NYISO staff is already considering a method to forecast scheduled and planned outages, and to use those forecasts in calculating TCCs that will be available and feasible. But the method that ConEd proposed – the use of an historical database – is impractical because such a database does not exist. The NYISO could begin to develop such a database as it gains more experience. ConEd's proposal - that each Transmission Owner could generate its own historical outage experience for use by the NYISO to reserve for each transmission owner TCCs that would otherwise be sold in the auction – was met with great market participant skepticism. The idea was not fully thought-out when presented and many participants thought that the ConEd's database proposal provided too great an opportunity for gaming and cost shifting. The data that each Transmission Owner would provide could simply not be verified by market participants.

The Companies would support a NYISO Board-issued directive to NYISO staff to develop an objective, reliable and accurate methodology to predict future outages and their duration and incorporate such predictions into the calculation of feasible TCC sets. But such directive must not delay implementation of the congestion reduction proposal.

ConEd's assertion that the congestion reduction proposal does not address the underlying problem is not true. The Companies believe the proposal addresses a significant share of the problem for all the reasons described above – principally, that Transmission Owners that cause these costs will have a clear incentive to reduce them and, in doing so, will schedule outages and restore equipment to service in a manner that will ultimately reduce the energy prices their customers pay.

Conclusion

WHEREFORE, for the above stated reasons, New York State Electric & Gas Corporation, and Rochester Gas and Electric Corporation respectfully request that the NYISO Board reject the appeals of the Management Committee's approval of the Congestion Reduction Proposal submitted by the Consolidated Edison Company of New York, Inc. the City of New York, and Consumers Power Associates, and by the Long Island Power Authority, and that the Board instead support the Management Committee's approval of the Congestion Reduction Proposal and direct NYISO Staff to work with the Market Participants to develop the necessary tariff amendments and join with the Management Committee in the filing of those amendments with the Federal Energy Regulatory Commission under Section 205 of the Federal Power Act, 16 U.S.C. § 824d.

Additionally we ask the Board to direct the NYISO staff to work expeditiously with Market Participants to complete additional studies on congestion rent surplus allocation, and TCC reduction methodologies associated with TCC feasibility under outage conditions. However, it is imperative that these efforts do not delay providing the incentives, and rectifying the inequities of the current processes, that will occur with the implementation of the Congestion Reduction Proposal.