

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

**Consolidated Edison Company
of New York, Inc.,
Complainant,**

v.

**Docket No. EL02-23-000
(Phase II)**

**Public Service Electric and Gas
Company,
PJM Interconnection, L.L.C. and
New York Independent System
Operator, Inc.,
Respondents.**

**INITIAL BRIEF OF
THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.**

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**INITIAL BRIEF OF
THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.**

To: The Honorable Isaac D. Benkin
Presiding Administrative Law Judge

The New York Independent System Operator, Inc. (“NYISO”), pursuant to the Chief Administrative Law Judge’s March 17 order,¹ the Presiding Judge’s March 21 order,² and Rule 706 of the Commission’s Rules of Practice and Procedure,³ hereby respectfully presents its initial brief in this proceeding. Because the NYISO is essentially neutral in this proceeding, and because it has no commercial stake in the outcome, it is not taking any position on a number of issues that are included in the Presiding Judge’s official briefing outline. Consistent with the

¹ Order of Chief Judge Extending Procedural Schedule, Docket No. EL02-23-000 (Phase II) (March 17, 2003).

² Presiding Administrative Law Judge’s Order Prescribing Outline for Post-Hearing Briefs, Docket No. EL02-23-000 (March 21, 2003).

³ 18 C.F.R. § 385.706 (2002).

March 21 Order's instructions, the NYISO has followed the official outline and has identified the issues it does not wish to address.

INTRODUCTION AND SUMMARY

There has been little change in the NYISO's position in the year since the Commission originally set this case for hearing. This case continues to be about the "1975 Agreement" and the "1978 Agreement" (together, the "1975 and 1978 Agreements"), two unusual wheeling contracts negotiated at a time of intense regulation, vertically-integrated utilities, and minimal competition.⁴ They must now be implemented in a more complex, market-based environment that is organized around Independent System Operators ("ISOs") that offer open-access transmission service and administer competitive electricity markets based on locational marginal pricing ("LMP").

The NYISO is not a party to either agreement and continues to have no interest in how they are interpreted, or in the commercial implications for their signatories, the Consolidated Edison Company of New York, Inc. ("ConEd") and the Public Service Electric and Gas Company ("PSE&G"). Given its role as a non-profit entity responsible for providing open-access, preserving reliability and administering efficient wholesale electricity markets, the NYISO's interest lies solely in the successful development of a protocol for implementing the two contracts. As the Presiding Judge has observed, the development of such a protocol raises technically difficult issues and will have important consequences for both the NYISO and the PJM Interconnection, L.L.C.. A flawed protocol could have serious adverse market, operational, planning and reliability effects, especially in the sensitive New York City area. Conversely, an

⁴ The NYISO defers to ConEd and PSE&G to provide a detailed factual statement on the history of the 1975 and 1978 Agreements.

effective protocol will ensure that the intended level of contract flows under the 1975 and 1978 Agreements are not disrupted.

From the NYISO's perspective there have been two significant developments during Phase II. First, the NYISO is increasingly optimistic that it and PJM can work together and will ultimately succeed in creating a sound operating protocol. The NYISO has always anticipated that a protocol to implement the 1975 and 1978 Agreements could be established once the preliminary contract interpretation and commercial issues were resolved. There have been times in this proceeding when disagreements between the ISOs may have made this optimism seem unfounded. After filing their Phase II rebuttal testimony, however, the NYISO and PJM experts met to discuss operating protocol issues. The NYISO believes that this meeting eliminated a number of misunderstandings and showed that the ISOs agree on a number of issues, at least on a preliminary basis and at a high level.⁵ The NYISO now believes that the redispatch cost comparison and equalization method introduced in Mr. Michael C. Calimano's Phase II Testimony⁶ can be combined with several of PJM's concepts, as expressed in the Phase II Testimony of Mr. Michael Kormos, and serve as the foundation of an operating protocol. There is not yet agreement between the ISOs on many issues and much work remains to be done. Nevertheless, it is now more clear than ever to the NYISO that success is possible.

The NYISO believes that the Presiding Judge can best facilitate the creation of a successful protocol by encouraging the Commission to resolve the commercial and contractual issues as quickly and with as much finality as possible. The Presiding Judge should also

⁵ See Tr. at 1415-16.

⁶ See Initial Remand Testimony of Michael C. Calimano, ("Calimano Testimony") at 2-3, 7-9; Corrected Phase II Rebuttal Testimony of Michael C. Calimano On Behalf of the New York Independent Transmission System Operator, Inc., ("Calimano Rebuttal Testimony") at 5-8.

recommend that the Commission endorse the NYISO's view that the final operating protocol should be a "hybrid" that reflects the views of both ISOs and balances the interests of their respective stakeholders. Such a protocol would not give either ISO unilateral decision-making authority, which would allow the ISO with that authority to advance the interests of its own region's stakeholders over the other's. Instead, the operating protocol should include very specific rules that would be settled in advance and unambiguously govern each ISO's operations.

There is no need for the Presiding Judge, or the Commission, to go further by seeking to create a protocol for the parties. Once clear guidance on basic principles has been given, the ISOs, which have the requisite technical expertise, should take the lead on protocol development. They should consult with the other parties and with any other interested stakeholders to ensure that all interests are represented. To date, the ISOs have not had a genuine opportunity to work out a protocol because basic contractual issues have been unresolved. When the meaning of the contracts is finally clear it should be possible for the ISOs to proceed reasonably quickly. The NYISO agrees with Mr. Kormos that the ISOs could use the Commission's dispute resolution procedures to settle any intractable technical disagreements once work on a protocol is underway.

The second significant Phase II development from the NYISO's perspective has been PSE&G's misleading attempt to blame the NYISO, in part, for causing alleged "impairments" of service under the 1975 and 1978 Agreements. PSE&G witness Mr. Robert V. Snow has claimed that the lack of a physical deliverability requirement in the NYISO's "System Reliability Impact Study" ("SRIS") criteria is a major design flaw that has made it much more difficult and expensive for PSE&G to fulfill its contractual commitments. PSE&G argued further that the SRIS process should be changed prospectively to include a physical deliverability requirement.

These contentions are without merit and should be rejected. As Mr. Calimano has previously explained, and as the NYISO reiterates below, there are important reasons why the SRIS process does not, and should not, include a deliverability requirement. The Presiding Judge should therefore reject PSE&G's claims and support the NYISO's position that its Commission-approved SRIS rules do not need to be modified.

ARGUMENT

I. THE NYISO HAS DONE NOTHING TO IMPAIR SERVICE TO PSE&G UNDER THE 1975 AND 1978 AGREEMENTS

The NYISO is not taking any position on Issues I.A, I.B, I.C.1, or I.D.

C.2 THE NYISO'S PLANNING PROCESS HAS NOT RESULTED IN IMPAIRMENTS UNDER THE 1975 AND 1978 AGREEMENTS AND NEED NOT BE MODIFIED

PSE&G's witness Mr. Snow has complained that the lack of a physical deliverability requirement in the NYISO's SRIS process has contributed to "impairments" that can make it more difficult or expensive for PSE&G to meet its contractual obligation to deliver up to 1000 MW to ConEd.⁷ Mr. Snow has suggested that the Commission should solve the alleged problem by requiring the NYISO to adopt a physical deliverability standard. PSE&G is correct that the NYISO's interconnection study requirements "analyze the impact of generation and merchant interconnections from the standpoint of reliability" and that "there is no attempt to analyze the deliverability of particular transactions or generation sources." It is mistaken and misleading, however, to suggest that the SRIS process is to blame for any impairments. Furthermore, there is no need to require the NYISO to graft a superfluous deliverability requirement onto its SRIS

⁷ See Testimony of Robert V. Snow ("Snow Testimony") at 3, 12-23; Rebuttal Testimony of Robert V. Snow ("Snow Rebuttal Testimony") at 16-17.

process that is not wanted by the NYISO or a majority of its stakeholders and that has not previously been required by the Commission.

As a preliminary matter, there is no legal basis for PSE&G's to assert an impairment claim against the NYISO in connection with the 1975 and 1978 Agreements. The NYISO is not a party to either contract, and thus cannot be found to have breached, repudiated or impaired them. PSE&G likewise has not even attempted to demonstrate that the SRIS procedures are unjust or unreasonable under Section 206 of the Federal Power Act.⁸ There is thus no basis for PSE&G to seek any kind of relief in this case that would require the NYISO to modify its SRIS procedures.

Mr. Calimano Phase II Rebuttal Testimony highlighted the more substantive flaws in PSE&G's positions.⁹ The NYISO also supports the arguments put forward by ConEd's witness Mr. Charles Ruscowicz, to the extent that they further explain why the SRIS process does not cause impairments of service.¹⁰

The key point is that the SRIS process is not "deficient" by virtue of the fact that it does not employ a physical deliverability requirement because the NYISO's system makes "deliverability" decisions based on economic factors in real-time. The NYISO does not, and does not need to, consider the deliverability of specific units as a long-term reliability planning matter. The purpose of the SRIS process is to identify the system upgrade facilities that are necessary, given the applicable reliability requirements, to interconnect generation or merchant

⁸ 16 U.S.C. 824e.

⁹ See Corrected Phase II Rebuttal Testimony of Michael C. Calimano ("Calimano Rebuttal Testimony") at 9-15.

¹⁰ See Initial Testimony of Charles Ruscowicz ("Ruscowicz Testimony") at 2-7; Rebuttal Remand Testimony of Charles Ruscowicz ("Ruscowicz Rebuttal Testimony") at 2-3, 6-8.

transmission facilities to New York’s transmission grid. The NYISO’s “installed capacity” (“ICAP”) system focuses on ensuring that sufficient capacity will be available to preserve long-term reliability both on a statewide basis and within specific locations, such as New York City, that are known to be vulnerable to capacity deficiencies. The SRIS planning process recognizes these “locational capacity requirements,” which obviates the need to consider the physical deliverability of a particular generator to a particular load. By establishing statewide and localized locational capacity requirements the NYISO ensures that there will be sufficient generation in each area to serve that area’s load after allowing for transmission constraints.

The NYISO’s use of a LMP-based market design makes this approach feasible because it provides the NYISO with accurate pricing information which enables redispatch of the system while accounting for transmission constraints. By contrast, physical deliverability requirements are needed in non-LMP systems. While it would be possible to employ a physical deliverability requirement within a LMP-based framework, the NYISO believes that its own model is best suited for New York’s needs.¹¹ Most New York stakeholders appear to agree, and the Commission has never instructed the NYISO to adopt a different regime.

Under the NYISO’s Commission-approved LMP system, the actual delivery of energy from specific generators to specific loads is determined based on an economic evaluation of the bids and offers submitted into the markets. The NYISO automatically redispatches its system, based upon the economic preferences expressed in the bids and offers, to support all transactions to the greatest extent possible. If there is insufficient capacity to support every transaction, then the NYISO will cut transactions based on their economic priority (which also is determined

¹¹ In particular, the NYISO, unlike PJM, must contend with two locations, New York City and Long Island, that frequently face potential capacity shortages.

through customer bids). The NYISO provides a customer that wants to move power through a constrained area with a number of options. It can compete with other suppliers for transmission capacity and either bear the risk of having to pay congestion costs or obtain sufficient Transmission Congestion Contracts (the NYISO's equivalent of PJM's "FTRs") to hedge this risk. Alternatively, if it wants to improve its ability to make physical deliveries to a specific load location it can apply for a physical transmission system reinforcement by submitting a transmission expansion request. If a customer chooses not to avail itself of any of these options and its transaction is cut, the outcome has nothing to do with the SRIS process or any alleged contract impairment by the NYISO.

PSE&G has repeatedly attempted to blur the distinctions between SRIS and Locational Installed Capacity standards and real-time deliverability by, for example, complaining that various deliverability factors have not been considered in SRIS analyses. This is a fundamentally misleading apples to oranges comparison. As was noted above, the SRIS process is designed to ensure that there is sufficient transmission capacity to ensure that state-wide and locational load needs are met. Actual deliveries are determined in NYISO's markets. It would be highly inefficient to revise the SRIS procedures to instead ensure that all generators are deliverable to load under all conditions, since this would tend to result in overbuilding. The Presiding Judge should therefore reject PSE&G's request that the SRIS procedures be modified.

Finally, apart from the SRIS considerations, PSE&G's impairment theory is inconsistent with the Commission's market-oriented policies. Mr. Calimano previously noted Mr. Ruscowicz's testimony that ConEd would agree to reduce the amount of power transfers it would request under the 1975 and 1978 Agreements if more economical energy supplies were available

from local generation on Staten Island or from other sources.¹² This is entirely consistent with the NYISO's administration of a LMP-based market design, which encourages ConEd to find efficient ways to meet its load. There could only be an impairment if PSE&G were obliged to deliver 1000 MW to ConEd at all times, including when ConEd has no desire to hold PSE&G to its maximum delivery obligation. PSE&G's impairment theory would thus prevent exactly the kind of choices that LMP systems are designed to allow, and that the Commission's December 9 Order and Opinion on Initial Decision ("December 9 Order") has effectively required ConEd to make.¹³ Accepting PSE&G's impairment theory would needlessly prevent ConEd from making efficient choices and thus needlessly reduce market efficiency. It would also make it harder for the ISOs to implement the NYISO's proposed redispatching cost comparison method.

II. THE PRESIDING JUDGE SHOULD ENDORSE THE NYISO'S PROPOSED CONCEPTUAL FRAMEWORK AND RECOMMEND THAT IT BE THE BASIS OF A FINAL OPERATING PROTOCOL

A. The Implementation Concepts Introduced by the NYISO and PJM Experts Can Be the Foundation of a Successful Operating Protocol

Mr. Calimano has proposed a method for resolving the most challenging component that the Commission required the parties to include in the Operating Protocol issue, namely a real-time economic evaluation of the redispatch options available to ConEd against PSE&G's redispatch costs before requiring PSE&G and PJM to redispatch.¹⁴ Mr. Calimano has explained how this can be done in a real world environment where each ISO only has access to its own cost

¹² See Calimano Rebuttal at ___, *Initial Remand Testimony of Charles Ruscowicz* at 3.

¹³ Consolidated Edison Co. of New York, Inc. v. Pub. Serv. Elec. & Gas Co., 101 FERC ¶ 61,282 at P 37-38 and n. 37 (2002).

¹⁴ See December 9 Order at PP 37-38 and n. 37 (2002).

information and the ISOs' respective day ahead markets run sequentially instead of simultaneously.¹⁵

Specifically, when it is necessary to make a redispatching decision, the ISOs would compare their internal redispatch costs that are relevant to the flows under the 1975 and 1978 Agreements. The relevant NYISO redispatch costs would equal the congestion cost difference between the Ramapo and Farragut/Goethals substations, *i.e.*, the difference between the NYISO LMPs at those two points. The relevant PJM redispatch costs would equal the congestion cost difference between the Waldwick and Hudson/Linden substations, *i.e.*, the difference between the PJM LMPs at those two points. After the two ISOs compared their redispatching costs, the ISO that faced lower redispatching costs would support the contract flows by redispatching its system until the point where its redispatching costs were equalized with the other ISO's costs.

For example, if the NYISO was faced with a \$50/MWh redispatch cost between its Ramapo and Farragut/Goethals substations, and PJM was faced with a \$20/MWh redispatch cost, the levels of contract flows (circulation) would be increased incrementally towards the New York City area. This would result in PJM redispatching until PJM's redispatch cost between the Waldwick and Hudson/Linden substations equaled the NYISO redispatch costs.

PJM has indicated that it does not object to Mr. Calimano's methodology.¹⁶ Certain aspects of PSE&G's proposed approach also appear to be generally consistent with it, although the NYISO does not agree with PSE&G that ConEd's needs could reasonably be addressed solely through FTR assignments.

¹⁵ See Calimano Rebuttal Testimony at 5-6.

¹⁶ See Tr. at 1414-1416.

The NYISO's proposed framework has the advantage of being workable regardless of what level of service under the agreements is ultimately found to warrant redispatching by PSE&G and PJM. Under the current terms of the December 9 Order, the proposal would apply to redispatching decisions related to the 600 MW flow under the 1978 Agreement, but not the 1975 Agreement.¹⁷ If ConEd and PSE&G agree to "firm up" the 1975 Agreement, as the NYISO hopes will occur, then the framework would apply to the full 1000 MW flow. Alternatively, if the Commission ultimately revises the December 9 Order so that PSE&G and PJM must always pay redispatching costs under the 1978 Agreement, and the economic cost comparison requirement would apply only to the 1975 Agreement, the NYISO's method could be applied to the 400 MW flow.

The NYISO's redispatching cost comparison and equalization method can also be combined with operating concepts sponsored by Mr. Kormos, such as the use of a desired flow circulation model, or that may be developed by the parties in future negotiations over the Operating Protocol. The Presiding Judge and the Commission should encourage the parties to work together to establish such a hybrid protocol.

B. A "Desired Flow" Calculation Could Be a Workable Component of the Operating Protocol

The NYISO previously expressed reservations about Mr. Kormos',¹⁸ and the Commission's,¹⁹ suggestion that a "desired flow" calculation similar to the one employed under the "5018 Agreement" should be part of the Operating Protocol. Subsequent discussions with Mr. Kormos have dispelled many of the NYISO's misgivings. The NYISO is now open to the

¹⁷ December 9 Order at PP 37-38 and n. 37 (2002).

¹⁸ See Calimano Rebuttal Testimony at 3-5.

¹⁹ See December 9 Order at P 65.

possibility that a desired flow calculation could be included in an Operating Protocol to govern operations during periods when neither ISO would be required to re-dispatch. Many details need to be resolved, however, and it is possible that Mr. Kormos' original concepts will have to be modified somewhat as the Operating Protocol is fleshed out. The Presiding Judge should therefore endorse the use of a desired flow calculation in principle but also allow for any departures from the core concept that are necessary in the final protocol. The Commission's December 9 Order, is sufficiently flexible to permit this approach since it only gives the use of a 5018-type procedure its preliminary endorsement.²⁰

C. The Operating Protocol Should Provide for ISO Control of the Phase Angle Regulators Located on the PSE&G - ConEd Interties

The Operating Protocol should expressly provide that the NYISO and PJM will exercise real-time operating control over the Phase Angle Regulators on the "A," "B", "C", "J" and "K" lines that are used to manage flows under the 1975 and 1978 Agreement. The Operating Protocol should also specify that neither ISO may take unilateral action without the concurrence of the other. To the greatest extent possible, it should define procedures that the ISOs will follow when making PAR moves in order to minimize the risk of real-time disagreements. The NYISO's proposed inter-ISO redispatching cost comparison and equalization procedure is the most important example of such a pre-defined rule, but there are likely be additional, more narrowly drawn, guidelines as well. Working out the rules will take time but there is no reason to expect that the ISOs will be unable to develop them, with the assistance, as necessary, of the Commission's dispute resolution staff.

²⁰ See December 9 Order at P 64 (noting that the Commission's guidance on this issue must be "viewed as preliminary.")

D. Third Party Transactions Should Be Allowed to Flow Across the PSE&G - ConEd Interties to the Extent That They Do Not Interfere with Flows Under the 1975 and 1978 Agreements

The Commission's December 9 Order confirmed that the 1975 and 1978 Agreements are grandfathered transmission contracts, rather than mere "facilities agreements," and are to be treated as providing for "firm" transmission service, except with respect to the parties' redispatching obligations. The NYISO is therefore obliged to treat the 1975 and 1978 Agreements the same as it treats other grandfathered firm transmission arrangements, even though they were not included on the list of grandfathered agreements included in the NYISO's tariff. Under applicable NYISO precedent,²¹ holders of grandfathered physical transmission rights that do not "convert" them to LMP-type financial rights are entitled to flow without being subject to curtailment for economic reasons. This approach is consistent with the Commission's holdings in Order No. 888,²² Order No. 2000,²³ and the recent Notice of Proposed Rulemaking

²¹ See, e.g., Central Hudson Gas & Electric Corp., et al., 88 FERC ¶ 61,138 (1999) (describing the provisions of Attachment K of the NYISO's open-access transmission tariff, which govern the treatment of grandfathered transmission agreements.)

²² See Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996), FERC Stats. & Regs. ¶ 31,036 at (1996), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274 (March 14, 1997), FERC Stats. & Regs. ¶ 31,048 (1997), order on reh'g, Order No. 888-B, 81 FERC ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), aff'd in relevant part, remanded in part on other grounds sub nom. Transmission Access Policy Study Group, et al. v. FERC, 225 F.3d 667 (D.C. Cir. 2000), aff'd sub nom. New York v. FERC, 122 S. Ct. 1012 (2002).

²³ See Regional Transmission Organizations, Order No. 2000, 65 Fed.Reg. 809 (Jan. 6, 2000), FERC Stats. & Regs. ¶ 31,089 at 31,205 (1999), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (Mar. 8, 2000), FERC Stats. & Regs. ¶ 30,092 (2000), aff'd sub nom. Public Utility District. No. 1 of Snohomish County, Washington v. FERC, 272 F.3d 607 (D.C. Cir. 2001).

on standard market design.²⁴ In each of these major issuances the Commission refused to mandate the “abrogation” of existing transmission arrangements and has allow holders of physical transmission rights that choose not to convert them to retain those rights.

Thus, assuming that ConEd does not voluntarily convert its rights, the Operating Protocol should require the NYISO to support “third party” transactions over the A, B, or C lines to the maximum extent possible, provided that they do not interfere with grandfathered flows under the 1975 and 1978 Agreements. Third-party transactions would be scheduled based on the NYISO’s normal bid-based economic evaluation, which essentially assigns a super-priority to grandfathered physical rights that are not subject to being “cut for economics.”

The NYISO has previously operated its system in this way, based on its understanding that the 1975 and 1978 Agreements were to be treated as grandfathered transmission contracts. As Mr. Calimano has testified, the NYISO’s experience has been that its obligation to support flows under the 1975 and 1978 Agreements only rarely results in third party transactions being limited. The NYISO normally schedules up to 2500 MW of third-party energy transactions across the PJM-NYISO interface and has found that this level of transactions does not normally compromise the expected 1000 MW flow under the 1975 and 1978 Agreements.²⁵ The NYISO therefore does not believe that a rule preventing the ConEd – PSE&G interties from being used for service that “interfered” with the contract flows would in any way degrade the total transfer capability between the NYISO and PJM

In short, the Presiding Judge should accept the NYISO’s proposal because it is consistent

²⁴ See Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design at PP 372-374, 67 Fed. Reg. 55,451, FERC Stats. & Regs. ¶ 32,563 (2002)

²⁵ See Calimano Rebuttal Testimony at 8-9 .

with both Commission precedent and the Commission's open-access policy goals.

The NYISO is taking no position on Issue II.D.1.

2. The ISOs Should Not Be Required to Establish New Proxy Buses at this Time

There were extensive discussions at the Phase II hearing about whether each ISO should establish one or more new proxy buses in order to more accurately represent the other's system.. The NYISO generally agrees with ConEd's view that its current practice of having only one proxy bus for PJM is an imperfect oversimplification. At the same time, the NYISO shares Mr. Kormos' concern that having multiple proxy buses will lead to a serious gaming problem, involving sham inter-proxy bus transactions that serve no useful economic purpose and produce inefficient market outcomes.²⁶ This is why the NYISO has always used a single proxy bus to represent the pricing and settlement of PJM transactions and why PJM ultimately switched to a single proxy bus to model the NYISO.

Although both ISOs are aware of this gaming problem it has proven extremely difficult to prevent. It is likely that a solution will be found at some point, but very unlikely that it could be implemented in time to be included in an Operating Protocol. Moreover, it is unnecessary to solve the proxy bus problem in order to have a workable protocol under the 1975 and 1978 Agreements. Under the circumstances, the gaming dangers that having multiple proxy buses would introduce must outweigh the potential market benefits that multiple proxy buses would bring. In addition, many non-party stakeholders are very interested in proxy bus modeling issues but are not represented in this proceeding, and were not on notice that proxy bus issues might arise in it. Indeed, the NYISO currently has a separate stakeholder process underway to consider

²⁶ See Tr. at 1260-63, 1265-66.

the proxy bus issue. The Presiding Judge should therefore not require the ISOs to take any action related to the creation of additional proxy buses at this time.

E. Detailed Procedures for Measuring Flows and Counterflows Should Be Worked Out By the Parties and Included in the Operating Protocol

The NYISO is taking no position on the question of whether flows under the 1975 and 1978 Agreement should be measured on a “net” or “metered” flow basis during periods when neither ISO is required to redispatch to support the flows. Each method can be made to work with the NYISO’s proposed redispatching cost comparison and equalization method and can be part of a “hybrid” protocol. Under either system, there will be a number of technical issues that the parties will have to resolve once the Commission decides which measurement approach they should use. These details should be left for the parties to flesh out as they develop the Operating Protocol.

F. Redispatching Decisions Should Be Governed by the NYISO’s Proposal for Comparing Relevant Redispatch Costs

As was noted above in Section II.A, the redispatching cost comparison and equalization proposal sponsored by Mr. Calimano would satisfy the Commission’s requirement that the Operating Protocol “address a comparison of options available to Con Edison before redispatch by PSE&G and PJM is required.” The NYISO’s redispatching cost comparison and equalization method will work regardless of how the legal issues concerning PSE&G’s redispatching obligations under the 1975 and 1978 Agreement are resolved.

G. The NYISO’s Cost-Comparison Proposal Could Be Used to Determine How Redispatch Costs Under the 1978 Agreement Will Be Recovered

If the December 9 Order’s holding that PSE&G and PJM must redispatch to support the 1978 Agreement only when it is economically appropriate is upheld, the NYISO’s proposed inter-ISO redispatching cost comparison and equalization procedure should be used to determine

whether the NYISO or PJM will redispatch, and thus which ISOs' customers will ultimately bear the redispatch costs. On the other hand, if the Commission ultimately concludes that PSE&G and PJM must always redispatch to support the 600 MW flow then there would be no need for an economic evaluation.

H. The NYISO's Cost-Comparison Proposal Should Be Used to Determine How Redispatch Costs Under the 1975 Agreement Will Be Recovered

If the December 9 Order's holding that PSE&G and PJM need not redispatch to support the 1975 Agreement is upheld, then the NYISO's redispatching cost comparison and equalization proposal would not apply to the 400 MW flow. However, if the 1975 Agreement were voluntarily "firmed up," or if it is later determined that PSE&G and PJM must redispatch to support the 400 MW flow when it is economically appropriate, the NYISO's method should be used to govern the recovery of costs under it.

If the Commission's decisions regarding PSE&G's and PJM's redispatching obligations under the 1975 and 1978 Agreements stand, the NYISO would strongly support efforts to "firm up" the 1975 Agreement. As the December 9 Order notes this would be desirable in light of New York City's supply situation. Accordingly, the NYISO suggests that the Presiding Judge recommend that the Commission direct, instead of merely encouraging, the parties to negotiate a "firming up" of the 1975 Agreement.

I. Service Under the 1975 and the 1978 Agreements Should Be Scheduled In the Day-Ahead Market

The NYISO does not agree that the 1000 MW transaction under the 1975 and 1978 Agreements is so unusual that it cannot be scheduled through normal day-ahead market procedures just like more typical transactions. The NYISO currently schedules the circulation and believes that PJM already does so as well. Each ISO should schedule the circulation day-ahead based on its best estimate of real-time conditions in order to ensure efficient market

outcomes for both ISOs. The NYISO's experience demonstrates that it is possible to do this without creating harmful price divergences between the day-ahead and real-time markets. Conversely, the NYISO is concerned that not scheduling the anticipated level of real-time contract flow could lead to artificial divergences between day-ahead and real-time prices.

J. Service Under the 1975 and the 1978 Agreements Should Have the Same Priority as Other Grandfathered Pre-Locational Marginal Pricing Contracts

For the reasons specified above in Section II.D, the NYISO believes that the flows under the 1975 and 1978 Agreements are entitled to the same transmission priority afforded to other grandfathered transmission arrangements under the NYISO's Commission-approved tariff and LMP market design.

K. Transmission Loading Relief Procedures May Initially Be Part of the Operating Protocol Initially But Should Ultimately Be Replaced with a Mechanism More Compatible With LMP

If the December 9 Order's holdings regarding the firmness of the 1975 and 1978 Agreements are upheld, the NYISO would not object to Mr. Kormos' assessment of the Transmission Loading Relief ("TLR") priorities that should be assigned to them.²⁷ The NYISO does not believe, however, that TLRs should be part of the operating protocol. As Mr. Calimano has explained, TLRs are blunt instruments that the Commission is striving to supplant through the implementation of its standard market design proposal. Both the NYISO and PJM already use LMP-based congest management systems that are much more compatible with efficient markets, and thus greatly preferable to TLRs. Both ISOs are authorized to use the TLR procedures as a back-up to their LMP systems but have almost never had to do so. TLRs should play, at most, the same, minimal, role under the Operating Protocol. The NYISO would support

²⁷ See Kormos Rebuttal Testimony at 5-6.

their inclusion as an initial matter, if necessary, but would favor replacing them over time with a curtailment tool that would be more consistent with LMP.

L. If It Is Ultimately Determined That Service Under the 1975 or 1978 Agreements Has Been, or Will Be, Impaired, The Amount of Service That the ISOs Will Be Required To Support Under the Operating Protocol Can Be Modified

If the Commission's preliminary conclusion that ConEd has impaired service to PSE&G and that the impairments must be considered in the Operating Protocol,²⁸ is not modified it should not be a difficult requirement with which to comply. The number of MWs that PSE&G would be required to wheel to ConEd would be reduced by the required amount. Other elements of the protocol would remain unchanged.

It bears repeating, however, that there is no merit in PSE&G's contention that the lack of a deliverability requirement in the NYISO's SRIS procedures has somehow resulted in, or even contributed to, an impairment of PSE&G's ability to deliver energy to ConEd. The NYISO addressed this issue in detail in Section I.C.2 above.

M. Rules Governing the Distribution of Contract Flows Over the A, B and C Lines Should Be Worked Out By the Parties and Included in the Operating Protocol

The NYISO is not taking any position on this issue with respect to most system operating conditions. During periods when the NYISO or PJM must redispatch in order to support the contract flows, however, the distribution of flows over the A, B and C lines may necessarily be dictated by the NYISO's application cost comparison an equalization procedure. For example, if the ISOs were to determine that NYISO redispatch costs could be reduced or equalized to PJM redispatch costs by simply adjusting the distribution of the contract flows over the A, B, and C

²⁸ See December 9 Order at P 70.

lines, then such an adjustment would be the natural consequence of applying the proposed redispatching cost comparison method.

N. Critical Bulk Facility Outages and Their Implications Should Be Defined In Advance By the Parties and Included in the Operating Protocol

Before finalizing the Operating Protocol the parties should specifically define all of the “critical bulk facility outages” on the northern portion of PSE&G’s system that would justify reductions in flows associated with the 1975 and 1978 Agreements. They should also agree on how much of a reduction each defined outage would warrant. This determination should be revisited periodically to account for changes in system topology, in advance of real-time operations, based on an updated system planning analysis. This analysis should be the joint responsibility of the ISOs, but Con Ed and PSE&G should have a major role in its preparation. If intractable disagreements arise, the parties should be required to resolve them through the Commission’s alternative dispute resolution procedures. Once a list of outages and reductions was agreed upon in they would then be included in the Operating Protocol. This would give the ISOs unambiguous operating rules to apply in real-time.

O. The Presiding Judge Should Favor the Development of a Flexible Operating Protocol That Will Not Require Major Revisions if the December 9 Order Is Modified And That Will Not Give Either ISO Excessive Unilateral Authority

It is clear that neither the Presiding Judge’s Initial Decision, nor the Commission’s eventual order addressing it, is likely to be the final word in this proceeding. ConEd and PSE&G have both sought rehearing of the contract interpretation decisions in the December 9 Order. Both of their rehearing requests are still pending and either party may seek further judicial relief once the Commission finally acts on them. Thus, the December 9 Order’s decisions regarding the relative “firmness” of the 1975 and 1978 Agreements, which were largely taken as givens during the Phase II hearing, will remain potentially subject to change for some time. The

Commission’s issuance of a Phase II order on the issues addressed at the hearing is likely to prompt another wave of rehearing requests, and possible judicial appeals.

Under the circumstances, the NYISO respectfully suggests that the Presiding Judge endorse flexible operating principles capable of accommodating any future changes in the underlying legal framework without requiring massive technical or software adjustments. The NYISO’s proposed redispatching cost comparison and equalization method has this quality. It can easily be adjusted in the event that the parties redispatching obligations under the contracts are revised on rehearing or appeal.

Finally, the Presiding Judge should recommend that the Operating Protocol give each ISO equal dignity. In the past, the Commission has made statements suggesting, perhaps unintentionally, that the Operating Protocol should protect PJM’s interests without mentioning the NYISO.²⁹ This would be inappropriate, as PJM itself has conceded.³⁰ The Presiding Judge should be clear that the Operating Protocol must balance the legitimate interests of each ISO and their stakeholders. Moreover, the Operating Protocol should not give either ISO unilateral decision-making authority, which could be exercised in a way that favored the ISO’s own region. Instead, the Operating Protocol should establish specific rules to unambiguously drive real-time operational decisions in pre-defined situations.

III. TRANSFORMER REPLACEMENT ISSUES

The NYISO is not taking any position on Issues III.A, III.B, or III.C.

IV. MARKET POWER ISSUES

The NYISO is not taking any position on Issues IV.A or IV.B.

²⁹ See, e.g., December 9 Order at P 68.

³⁰ See, e.g., Kormos Rebuttal Testimony at 4.

C. The ISOs Should Be Allowed to Confidentially Share Market Monitoring Information Pursuant to the Operating Protocol

Both the NYISO and PJM currently have effective market power monitoring and mitigation rules that meet their individual needs. Their monitoring systems, however, are focused on their own markets. There is currently no mechanism for coordinated monitoring of transactions that affect both ISOs. Indeed, the ISOs' tariffs both include confidentiality restrictions that hamper their ability to share market monitoring information and thus complicate joint monitoring efforts.

It may be desirable for the Operating Protocol to provide for better coordinated market monitoring of flows associated with the 1975 and 1978 Agreements. The NYISO anticipates that it will not be necessary to institute elaborate new procedures. It would be premature, however, to prescribe any particular monitoring or mitigation rules at this time. The Presiding Judge could best facilitate progress in this area by encouraging the ISOs to determine what monitoring procedures are necessary, and by recommending that the Commission allow them to freely share monitoring information relevant to the contract flows.

The Presiding Judge should also understand that the concern, expressed by PSE&G witness Mr. Rodney Frame,³¹ that inter-ISO monitoring (or mitigation) rules will necessarily be burdensome and intrusive is exaggerated. The NYISO does not believe that it will be necessary to implement aggressive new monitoring and mitigation procedures. Allowing the ISOs to better coordinate their existing activities should suffice. Moreover, if more extensive measures do in fact prove to be necessary, the ISOs will balance the need for effective monitoring and mitigation against the need to avoid disrupting markets as they have successfully done in the past.

³¹ See Tr. at 1218-21.

CONCLUSION

For all of the foregoing reasons, the Presiding Judge should: (i) recommend that the Commission resolve the outstanding contractual issues as expeditiously, and with as much finality, as possible; (ii) endorse an operating protocol built around the NYISO's proposed inter-ISO redispatching cost comparison and equalization methodology; and (iii) allow the ISOs in consultation with the other parties, to develop an operating protocol based on the conceptual framework.

Respectfully submitted.

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Commission in this proceeding.

Dated at Washington, D.C., this 14th day of April, 2003.

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