

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

New York Independent System Operator, Inc.)	
)	
Complainant)	
)	
v.)	Docket No. EL01-____-000
)	
New York State Electric & Gas Corporation)	
)	
Respondent)	

**COMPLAINT OF NEW YORK INDEPENDENT SYSTEM OPERATOR, INC
REQUESTING FAST TRACK PROCESSING
AND DECLARATORY ORDER**

Pursuant to Section 206 of the Federal Power Act (“FPA”)¹ and Rule 206 of the Commission’s Rules of Practice and Procedure (“Rules”),² the New York Independent System Operator, Inc. (“NYISO”) submits this Complaint against the New York State Electric & Gas Corporation (“NYSEG”). For the reasons set forth below, it is imperative that this Complaint be resolved in an expeditious manner. The NYISO therefore respectfully requests that the Commission review this Complaint pursuant to the Fast-Track Processing procedures set forth in Rule 206(h) of the Commission’s Rules.

This Complaint concerns NYSEG’s unlawful withholding of \$6.635 million that it owes the NYISO and is required to pay pursuant to the NYISO’s Open Access Transmission Tariff (“OATT”). The OATT, like the NYISO’s Market Administration and Control Area Services

¹ 16 U.S.C. §§ 791a-825r (1994).

² 18 C.F.R. § 385.206 (2000).

Tariff (“Services Tariff”), requires market participants to pay disputed amounts in full to the NYISO, subject to possible refunds when the underlying dispute is resolved.

NYSEG informed the NYISO that it was withholding the payment in a November 16, 2000 fax which it styled a “Claim for Indemnification.”³ The fax stated that NYSEG believed it was entitled to withhold the payment because it previously filed a lawsuit against the NYISO alleging that the NYISO is liable to pay NYSEG \$6.635 million in connection with the problems in the NYISO’s 10-Minute operating reserves markets last winter.⁴ Despite the fact that the reserves issues all arise under the NYISO’s OATT and Services Tariff, NYSEG claimed a right to “set-off” the \$6.635 million pursuant to the Asset Purchase and Sale Agreement (“APA”) between the NYISO and the former New York Power Pool (“NYPP”).⁵ NYSEG’s APA theory is described in two letters it sent to the NYISO on September 5, 2000 and is discussed below.⁶ The APA, which, to the best of the NYISO’s knowledge, information and belief, was never filed with or approved by the Commission, governs the NYISO’s purchase of certain miscellaneous assets from the NYPP. Although the APA contains indemnification provisions that include a set-off right the APA has absolutely nothing to do with the administration of the NYISO’s 10-minute operating reserves markets or with the payment of reserves charges.

³ NYSEG’s fax is appended to this Complaint as Attachment I.

⁴ Although NYSEG’s civil action involves issues that were previously decided by the Commission, or that are currently pending on rehearing before it, this Complaint does not address the merits of the lawsuit. The NYISO is vigorously defending against NYSEG’s civil action which the NYISO believes is preempted by pending Commission proceedings on reserves market issues.

⁵ The text of the APA, excluding its appendices and schedules, is appended to this Complaint as Attachment II.

⁶ The two September 5 letters are appended to this Complaint as a Attachment III.

Consequently, NYSEG's attempt to invoke the APA's set-off provision in order to override the payment rules established by the NYISO's tariffs is entirely inappropriate, unreasonable and unlawful. Because NYSEG's decision to withhold its payment has already had financial consequences for the NYISO, and may shortly result in financial harm to other New York market participants, the NYISO has been compelled to file this Fast-Track Complaint. The NYISO respectfully requests that the Commission expeditiously issue an order declaring that NYSEG's withholding is an unlawful violation of its obligations as a customer under the NYISO's OATT. The Commission should also direct NYSEG to immediately reverse its set-off and pay the NYISO the full amount that it is owed, plus interest, and all other costs incurred by the NYISO in connection with the set-off from the date of non-payment.

I. Copies of Correspondence

Communications regarding this proceeding should be addressed to:

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II. Background

A. **The NYISO's Commission-Approved Open Access Transmission Tariff Requires that NYSEG Pay All "Amounts in Dispute" to the NYISO Without Delay and Does Not Provide NYSEG with a Superior Right to Set-Off Payments That Other Market Participants Do Not Have**

The NYISO's OATT and Services Tariff establish that customers must pay disputed amounts in full to the NYISO, subject to after-the-fact billing adjustments once the underlying dispute is ultimately resolved. For purposes of this Complaint the OATT's provisions are relevant because NYSEG's set-off represents an attempt to avoid paying operating reserves charges incurred pursuant to Rate Schedule 5 of the OATT.⁷ Prior to NYSEG's November 16th set-off no market participant had tried to challenge the payment-in-full principle during the entire first year of NYISO operations.

Section 7.2A of the NYISO OATT, "Billing Disputes," explicitly states that when a customer "wishes to challenge Settlement information for accuracy" it must "first make payment in full including any amounts in dispute." If the customer is subsequently found to have overpaid, the NYISO is required to repay it with interest, which ensures that the customer will suffer no financial harm. The same policy is incorporated into Section 7.3, "Customer Default" which does not include language from Section 7.3 of the Commission's *Pro Forma* OATT that allows customers to pay disputed amounts into an escrow account pending the resolution of the dispute. The escrow language was eliminated pursuant to a tariff amendment that was jointly

⁷ The Services Tariff, while not relevant to this case because it does not govern reserves payments by customers, contains virtually identical language requiring customers to pay disputed amounts in full.

submitted by the Member Systems of the New York Power Pool (“Member Systems”),⁸ including NYSEG, and the NYISO, on November 12, 1999 in Docket No. ER00-556-000 (“Joint Filing”). In the Joint Filing, the NYISO and the Member Systems, including NYSEG, explained that:

Section 7.3 of the OATT which deals with Customer Default presents a significant risk to the NYISO’s financial strength. The provision currently enables a customer who disputes a bill to pay the amount of the bill under dispute directly into an independent escrow account. The NYISO understands that customers in other ISOs have invoked the escrow provisions and, thereby, created significant cash flow problems for the ISO. From the NYISO’s financial perspective, the inability to use these escrowed funds to pay the market is tantamount to not being paid at all. The provision is being changed to require the payment of disputed amounts during the pendency of the dispute. The Member Systems and the NYISO submit that this change is consistent with or superior to the *Pro Forma* Tariff. In Pennsylvania-New Jersey-Maryland Interconnection, et al., 81 FERC ¶ 61,257 at 62,274 (1997), reh’g granted, the Commission refused to require the use of an escrow account in connection with a disputed charge. There the Commission recognized that “[i]f funds were escrowed during billing disputes, PJM-OI would have no means to pay its obligations during the pendency of the dispute.” This change is necessary to reflect the fact that the NYISO requires these funds to pay its suppliers.⁹

The Commission accepted this argument and approved the amendment, without discussing the reasons for its decision. However, the Commission had previously offered clear policy guidance in the *Pennsylvania-New Jersey-Maryland Interconnection, et al.* (“PJM”) order that was quoted in the Joint Filing. There the Commission reviewed a provision of PJM’s proposed Operating Agreement (“OA”) which required that customers must pay all bills, notwithstanding any disputes, subject to appropriate after-the-fact adjustments. The OA also

⁸ On March 6, 2000, after the New York Power Pool was supplanted by the NYISO, the Member Systems of the New York Power Pool changed their name to the Members of the Transmission Owners Committee of the State of New York.

⁹ Joint Filing at 5.

allowed PJM to assess any billing deficiencies against non-defaulting market participants, who would then be permitted to seek recovery from the non-paying entity. A market participant argued that this provision was inconsistent with the escrow account language set forth in the *Pro Forma* Tariff. The Commission disagreed and stated:

We will not order Supporting Companies to revise PJM-OI's billing and settlement provisions as requested by Clearinghouse. If funds were escrowed during billing disputes, PJM-OI would have no means to pay its obligations during the pendency of dispute. Further, if we were to direct PJM-OI to create reserves for purposes of paying disputed charges, this would unnecessarily increase PJM-OI's operating costs.¹⁰

The relevant Commission precedent thus clearly affirms that customers taking service under the NYISO OATT must pay all disputed amounts in full, subject to after-the-fact adjustments.

B. NYSEG's Set-Off Has Financially Harmed the NYISO and Will Soon Inflict Financial Harm on Innocent Market Participants

The payment rule established by the NYISO OATT is essential to the financial stability of the NYISO. The NYISO is a not for-profit entity without shareholders, retained earnings, or any source of revenue, other than collections from its customers, that it can use to pay its suppliers. The Commission has previously recognized that the NYISO is vulnerable to mismatches between its receipts from customers and the amount it must pay for services.¹¹ Moreover, although the NYISO has secured a modest credit revolver capable of handling its ordinary cash flows the NYISO has no ability to satisfy large mismatches between receipt and

¹⁰ *Pennsylvania-New Jersey-Maryland Interconnection*, 81 FERC ¶ 61,257 at 62,274 (1997), *order on reh'g*, 92 FERC ¶ 61,282 (2000).

payments, such as the \$6.635 million gap created by NYSEG. The NYISO has been forced to resort to this credit line, as an interim measure, to maintain the stability of its markets and to avoid financial harm to innocent market participants. However, this is not a viable long-term solution because the NYISO's revolving credit arrangement is limited in amount and duration and was not designed to compensate for wrongly withheld funds.¹² Beyond this, the NYISO will either have to reduce its payments to innocent suppliers, increase its charges to innocent customers or pursue some combination of the two.¹³ The proper outcome is for NYSEG to be compelled to behave responsibly and to reverse its unilateral withholding of amounts properly billed to it under the tariff. If NYSEG were to engage in future set-offs, or if other Member Systems were to follow its example, the NYISO's credit might be cut off, or severely restricted, and the NYISO would be forced to impose harsh financial reserve requirements on innocent market participants, or face possible insolvency. Under these circumstances, the NYISO tariff provisions requiring that disputed amounts be paid in full should be rigorously enforced.

¹¹ See *New York Independent System Operator, Inc., et al.*, 89 FERC ¶ 61,223 (1999) (approving a revised billing rule that helped the NYISO avoid mismatches between its receipts and payments.)

¹² In addition, the NYISO is exercising its right under Section 7.1(iii) of the OATT, which requires the NYISO to pay "net monies" due to customers, to defer its own payments to NYSEG until such time as NYSEG reverses its unlawful set-off. This remedy may help to mitigate, but will not neutralize, the adverse financial effects of NYSEG's set-off.

¹³ In the event that the Commission rejects this Complaint the NYISO respectfully requests that it provide guidance as to how the NYISO market participants should bear the cost of NYSEG's withholding.

B. The Asset Purchase and Sale Agreement Set-Off Provision Cannot Legitimately Be Invoked In Connection With a Dispute Over Operating Reserves Issues Arising Under the NYISO Tariffs

In its November 16th fax, NYSEG stated that NYSEG has “incurred damages totaling \$6.635 million as a consequence of NYISO’s operation of the market for Operating Reserves.” Ignoring the provisions of the NYISO’s OATT, NYSEG proceeded to invoke Section 7.5 of the APA in an attempt to justify its “setting off the October 2000 invoice from NYISO to NYSEG in the amount of \$6.635 million.”

NYSEG provided somewhat more detail concerning its reasoning in its September 5th letters to the NYISO. Referring to Sections 7.2 and 7.3 of the APA, NYSEG stated that it was making a claim for indemnification by the NYISO. Specifically:

This claim is for indemnification by the NYISO for claims, including liabilities (as defined in the APA) incurred by NYSEG as a consequence of the operation of the market for Operating Reserves. These damages, totaling \$6.635 million, are subject to indemnification under Section 7.2 because they arise out of, and result from, the NYISO’s post-closing ownership of the Purchased Assets identified in Section 1.1 of the APA and the NYISO’s use of ISO Software, as defined in Section 1.1(c) of the APA.

The NYISO respectfully submits that NYSEG’s expansive interpretation of the APA is, at best, strained. Although it is true that the APA includes indemnification and set-off provisions the APA has nothing to do with the NYISO’s administration of its 10-minute operating reserves markets. The APA governs the NYISO’s purchase from the former NYPP of miscellaneous “Purchased Assets” and its assumption of certain contractual and permit rights and liabilities. The Purchased Assets do not include New York’s bulk power transmission system, which the NYISO operates but does not own. Instead, they consist largely of control room equipment and personal property located at the NYISO’s headquarters, the NYISO’s software, other intellectual

property and the NYPP's files.¹⁴ Moreover, although Section 7.2 of the APA permits a Member System to seek indemnification and set-off in connection with claims "arising out of or resulting from" the NYISO's ownership of miscellaneous NYPP assets, or "arising out of or related to" the ISO software, this language cannot reasonably be read as applying to disputes concerning the NYISO's administration of its 10-minute operating reserves market. Indeed, if the APA were read in this way it would give the Member Systems a special privilege, *i.e.*, the right to set-off disputed payments, that other entities taking service under the NYISO tariffs do not possess.

The reasons NYSEG offers as justification for withholding payment bear no reasonable relationship to the NYISO's ownership of former NYPP assets or the ISO software. Specifically, NYSEG's set-off claim is based on its allegations that the NYISO: (i) failed to consider bids to supply reserves from western suppliers; (ii) did not consider the Blenheim-Gilboa pumped storage facility as a source of reserves; (iii) failed to reserve transmission capacity for reserves across the Central-East interface; (iv) refused to use its Temporary Extraordinary Procedures as aggressively as NYSEG would have preferred; (v) supposedly encouraged a supplier to submit higher bids; (vi) charged NYSEG a price higher than the clearing price for 10-Minute Spinning Reserves when that price was lower than the clearing price for 10-Minute Non-Spinning Reserves; and (vii) supposedly did not base its purchases of reserves on its actual contingency requirements.¹⁵ All of these allegations have to do with the NYISO's tariff provisions and market rules, which have been, and continue to be, the subject of litigation before the Commission, and nothing to do with the subject matter of the APA. It is therefore at best

¹⁴ See Attachment II at 4-5.

¹⁵ See Attachment III at 1.

disingenuous for NYSEG to invoke the APA's set-off provisions in connection with a dispute over the NYISO's administration of the reserves market.

III. Argument

The NYISO respectfully submits that the dispute underlying NYSEG's decision to "set off" the money it owes the NYISO obviously arises under the NYISO's OATT and Services Tariff, not the APA. The two tariffs establish the NYISO's reserve requirements, explain how the NYISO is to administer the reserves markets they create and governs payments to reserve suppliers and by reserve buyers. NYSEG's own pleadings in the Commission's reserves-related proceedings¹⁶ confirm this insofar as they invoke numerous tariff provisions in connection with the same issues that are at the heart of the current payment dispute. The first of NYSEG's two September 5 letters likewise effectively concedes that the issues associated with the disputed payment are tariff issues by calling for the use of alternative dispute resolution procedures under Section 11.1 of the Services Tariff and Section 12.1 of the OATT to address them.¹⁷

By contrast, the APA has absolutely nothing to do with NYSEG's 10-minute operating reserves market dispute, just as disputes concerning the NYISO's administration of the reserve market do not have anything to do with its ownership of former NYPP assets or its operation of the ISO software. Moreover, even if the APA were relevant, its set-off provision could not be invoked here because it is entirely inconsistent with the NYISO OATT's requirement that all disputed amounts must be paid in full. Obviously, the provisions of the Commission-approved NYISO OATT must prevail over the language of a private agreement that has, to the best of the

¹⁶ See NYSEG's pleadings in Docket Nos. EL00-63-000, EL00-70-000 and ER00-3591-000 which discuss a number of reserves related issues.

NYISO's knowledge, information and belief, never been filed with, or approved by the Commission. NYSEG's position that the problems encountered in the NYISO's 10-minute operating reserves markets have arisen under the APA because the NYISO owned the Purchased Assets and was using the ISO software at the time might be literally true. However, NYSEG's reading of the APA is so broad that it would render Sections 7.2A and 7.3 of the OATT a nullity, with respect to the Member Systems, since the NYISO will always own the Purchased Assets and is constantly operating the ISO software. NYSEG's interpretation would favor the Member Systems, by giving them power to invoke the APA's set-off provision in connection with any dispute, permitting them to disregard an important tariff policy, which all other market participants must follow. This is an absurd, and patently discriminatory outcome. Given the financial harm that unauthorized set-offs inflict on the NYISO and other market participants, the Commission should reject NYSEG's interpretation and require it to immediately pay the disputed amount in full, with interest and all other costs incurred by the NYISO in connection with NYSEG's unlawful withholding of funds.¹⁸

¹⁷ See Attachment III.

¹⁸ The NYISO believes that it is perfectly clear that the APA's set-off provisions do not apply to reserves disputes. However, to the extent that the Commission concludes that the APA's provisions are ambiguous the NYISO submits that the Commission should consider the fact that the APA was executed just a few weeks after the Joint Filing. It is clearly unreasonable to conclude that the Member Systems and the NYISO would have intended for the APA to undermine their just-filed amendment to Section 7.3 of the NYISO OATT. See, e.g., *Mid-Continent Area Power Pool*, 92 FERC ¶ 61,229 (2000) (reiterating that the Commission may consider extrinsic evidence "to ascertain the intent of the parties when that intent has been imperfectly expressed in ambiguous contract language, but is not admissible either to contradict or alter express terms.")

IV. Request for Relief

In order to protect the NYISO and innocent New York market participants from serious financial harm, the Commission should issue an order declaring that NYSEG is required to immediately pay the disputed amount, in full, to the NYISO. This order should also direct NYSEG to make the required payment without delay.

The NYISO believes that this request for relief is consistent with Section 7.3 of the NYISO OATT, which identifies two possible remedies that the NYISO may pursue in the event of a customer default, but does not preclude the NYISO from filing this Complaint. In addition, the NYISO's request for relief is consistent with Commission policy insofar as it will minimize the financial harm to the NYISO, and to innocent market participants, by compelling NYSEG to immediately reverse its unlawful behavior, which only serves to undermine the NYISO-administered markets.

V. Compliance with the Other Requirements of 18 C.F.R § 385.206

In compliance with Rule 206(b)(6) of the Commission's Rules,¹⁹ the NYISO states that the issues presented in this Complaint, *i.e.*, the unlawfulness of NYSEG's set-off and the NYISO's request for relief from the financial harm resulting from it, are not pending in any other Commission proceeding. NYSEG recently asked the federal district court hearing its civil action to determine whether it was permitted to set-off its payment but, surprisingly, did not wait for that court to act before going ahead and making the unlawful set off. Commission action is therefore needed to address NYSEG's withholding. Moreover, although NYSEG's stated

¹⁹ 18 C.F.R. § 385.206(b)(6) (2000).

rationale for withholding its payment relates to substantive reserves market issues that are currently pending on rehearing before the Commission in Docket No. ER00-1969-002, the NYISO does not believe that it would be appropriate to consolidate this Complaint, which requires urgent Commission action, with that proceeding.

In compliance with Rule 206(b)(9) of the Commission's Rules,²⁰ the NYISO states that it has previously attempted, and is still attempting, to resolve the issues raised by Complaint through informal means. Most recently, after several attempts to schedule a meeting or a phone call, the NYISO was finally able to schedule a telephone conversation between NYSEG's Chief Operating Officer and the President of the NYISO on November 30th to address NYSEG's set-off. The NYISO hopes that this high-level meeting will lead to a satisfactory agreement that will permit it to withdraw this Complaint. However, because the NYISO's need for relief is so urgent the NYISO has concluded that it can not wait until after the November 30th meeting to seek the Commission's assistance. Similarly, because the NYISO needs immediate relief it has not used the Commission's Enforcement Hotline, Dispute Resolution Service or other tariff-based dispute resolution mechanisms to address the issues raised by this Complaint. The NYISO likewise believes that there is insufficient time for it to obtain relief pursuant to alternative dispute resolution under the Commission's supervision.

Finally, in compliance with Rules 206(b)(11) and 206(h) of the Commission's Rules,²¹ the NYISO emphasizes that Fast-Track Processing is appropriate in this instance because the Commission's standard processes "will not be adequate for expeditiously resolving the

²⁰ 18 C.F.R. § 385.206(b)(9) (2000).

²¹ 18 C.F.R. § 206(b)(6) and 206(h) (2000).

complaint.” Time is of the essence in this proceeding. NYSEG’s unlawful set-off has already put substantial financial pressure on the NYISO and the NYISO needs immediate relief. Moreover, as was explained above in Section III.C, the NYISO may shortly be forced to either reduce the payments it makes to suppliers, or increase the charges it assesses to other customers in order to make up for NYSEG’s deficiency. This will unfairly cause financial harm to innocent market participants and all but certainly result in additional litigation. Such litigation would benefit no one and could have serious adverse effects insofar as it would distract the NYISO staff from more important market correction efforts. Thus, under the circumstances, it would be inappropriate to employ the Commission’s standard complaint review procedures. Because this complaint raises a small number of relatively straightforward issues, the NYISO believes that NYSEG’s procedural rights will not be prejudiced if the Commission were to employ Fast-Track Processing in this case.

VI. Service

Consistent with Rule 206(c) of the Commission’s Rules, the NYISO has served copies of this Complaint on NYSEG, NYSEG’s counsel and the New York State Public Service Commission. In addition, the NYISO will post a copy of this Complaint on the “What’s New” section of its web-site²² and has notified all market participants that subscribe to its “Technical Information Exchange” that it is filing this Complaint, which will ensure that virtually all New York market participants are aware of it.

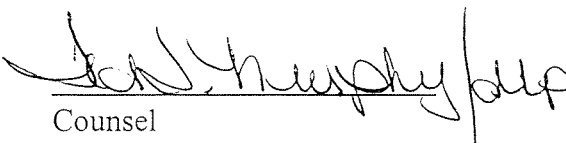
²² <http://www.nyiso.com/topics/whats_new/whatsnew.html>.

VII. Conclusion

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc. respectfully requests that the Commission: (i) grant its request for fast-track processing; (ii) declare that NYSEG's set-off is a violation of the NYISO's OATT and that NYSEG must immediately pay the full amount it has wrongly withheld; and (iii) order NYSEG to make the payment in full, including interest and all other associated costs, immediately.

Respectfully submitted,

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November 24, 2000

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