

# **NYISO Market Monitoring Review of Market Power Concerns in the In-City Capacity Market**

**ICAP Working Group  
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# Agenda

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## 1. *Our Analysis*

1. What issues have we been asked to consider?
2. What is our responsibility and authority to consider these issues?
3. What was the scope of our analysis?

## 2. *Analysis and Conclusions*

1. Market Power in the NY Capacity Markets
2. The adequacy of the market power mitigation measures.
3. Conclusions

# Our Analysis

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## What issues have we been asked to consider?

- ◆ Potential economic withholding in the context of the in-city capacity auctions;
- ◆ Demand-side market power concerns specific to out-of-market transactions;
- ◆ The adequacy of current market power mitigation measures relevant to the in-city capacity auctions;
- ◆ The adequacy of proposed market power mitigation measures from 9/29/06 (MC) relevant to the in-city capacity auctions.

# Our Analysis

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## What is our Responsibility and Authority?

*MMP is provided authority and is guided in its responsibilities by:*

- 1. The Market Monitoring Plan &*
- 2. Attachment H of the Services Tariff*

# Our Analysis

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## What was the scope of our analysis?

### *We considered:*

- 1 Market power in the NYC capacity markets
  1. *Supply-side concerns*
  2. *Demand-side concerns*
2. The adequacy of Market Power Mitigation Measures
  1. *Current Mitigation Measures*
  2. *Proposed Mitigation Measures*

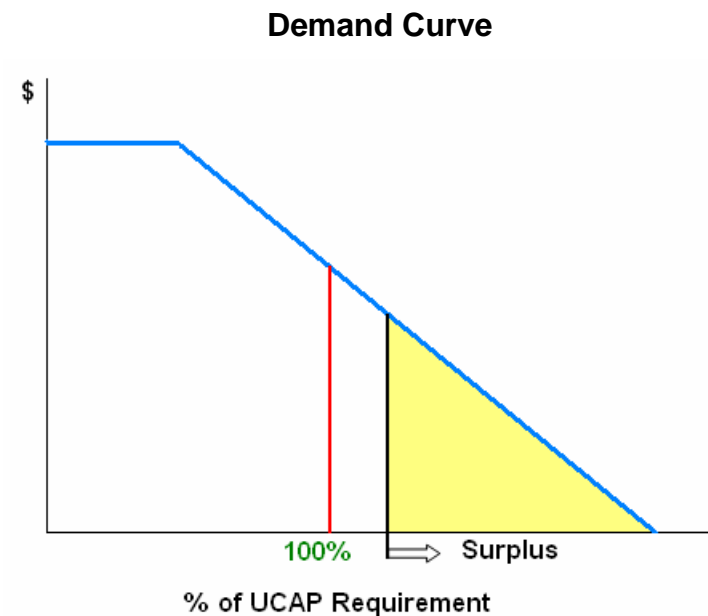
***We constrained our analysis to the boundaries of current market rules, recognizing that other processes are considering longer-run enhancements to the demand curve and to the capacity markets in general.***

# Analysis and Conclusions

- 1 Market power in the NYC capacity markets
  1. *Supply-side concerns*

## Discussion:

1. *Current measures that manage market power include the existing bid/revenue caps and the sloped demand curve.*
2. *Current measures may be deficient in a capacity surplus scenario.*



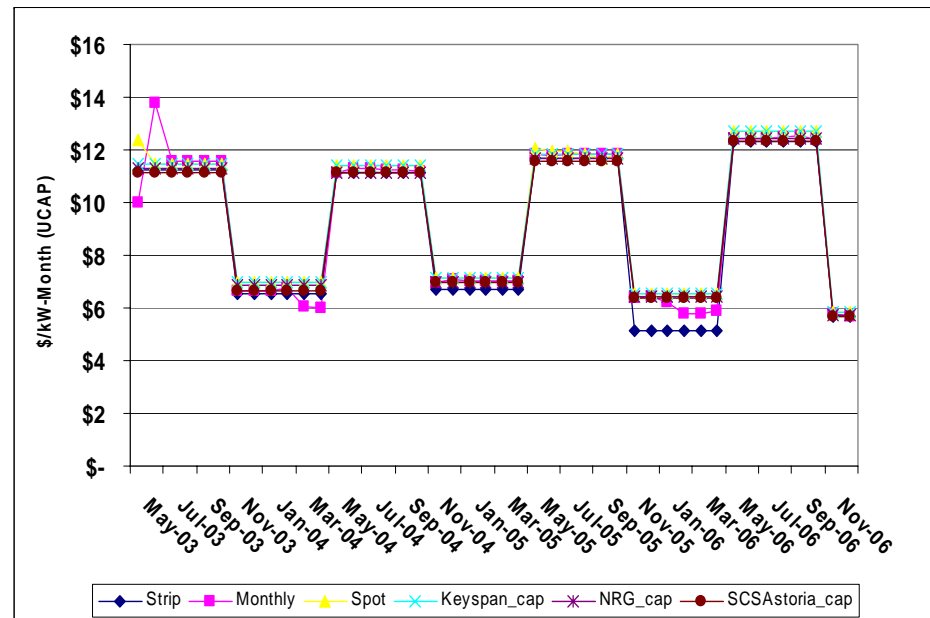
# Analysis and Conclusions

## 1 Market power in the NYC capacity markets

### 1. Supply-side concerns

#### Discussion:

3. *DGOs remain pivotal and have maintained a consistent offering strategy (all capacity at bid-cap) – as anticipated by FERC in '98 - since advent of the Demand Curve.*
4. *Market clearing prices have also followed a predictable path over the last 3 years.*

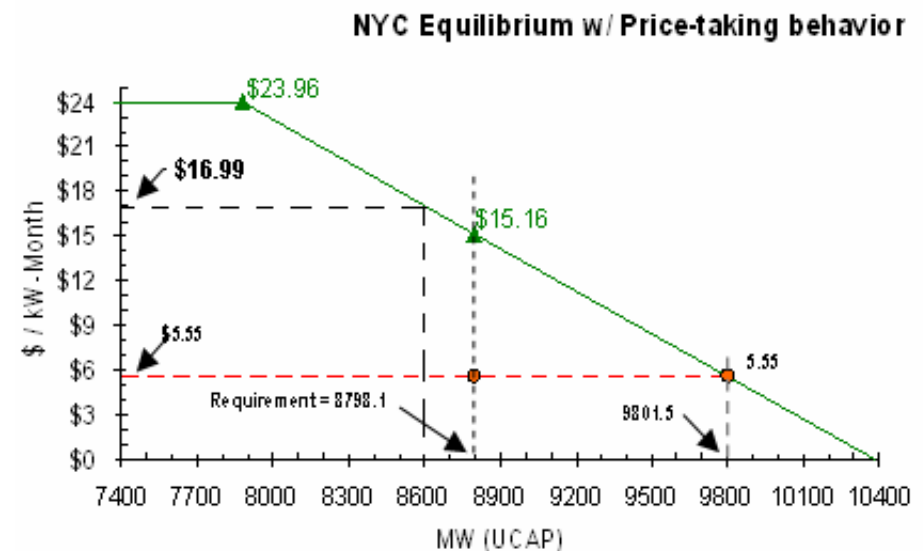


# Analysis and Conclusions

## 1 Market power in the NYC capacity markets 1. Supply-side concerns

### Discussion:

- 5. In a competitive market will set the price at the prevailing level of physical surplus/deficit.
- 6. Given price takers and the current Demand Curve, Summer 2006 capacity prices for NYC would have been \$5.55/kW-Month.



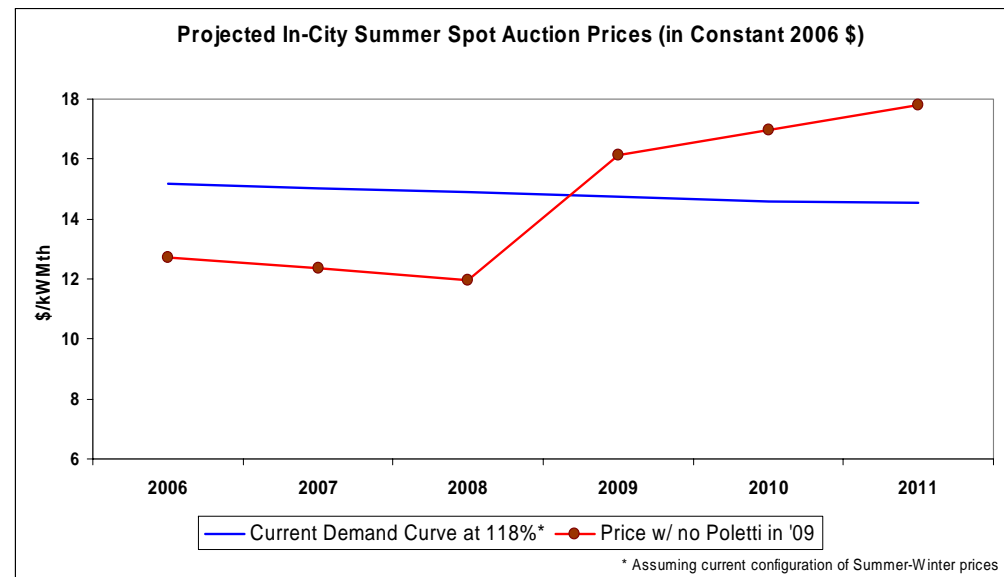


# Analysis and Conclusions

## 1 Market power in the NYC capacity markets 1. *Supply-side concerns*

*Discussion:*

1. *NYISO expects the NYCA to be in an ICAP deficit within two or three years. This will lead to higher spot auction prices.*



# Analysis and Conclusions

- 1 Market power in the NYC capacity markets
  1. *Supply-side concerns*

## Conclusions:

- ◆ *MMP confirmed that supply-side market power is an issue in the NYC capacity market that is imperfectly managed by current mitigation measures.*
- ◆ *This market power has been present within the boundaries of the FERC-approved mitigation measures and is expected to be sustained while the market is in a surplus capacity situation.*
- ◆ *For this reason MMP finds that the current measures could be revised to better manage market power when capacity levels substantial exceed minimum requirements.*
- ◆ *MMP is committed to be part of the demand curve reset process which will consider, among other issues,*
  - ◆ *The cost of new entry,*
  - ◆ *Revenue sufficiency, and*
  - ◆ *The Demand Curve slope and cutoff.*

# Analysis and Conclusions

- 1 Market power in the NYC capacity markets
  2. *Demand-side concerns*

Discussion:

1. *Current and proposed measures do not address potential demand-side market-power abuse.*
2. *This form of market power is mitigated in the short-term by the demand curve, but not in the long-term (i.e., related to out-of-market investment). Such monopsony market power abuse related to recent investments has been alleged.*
3. *It has been suggested that the NYISO impose price-floors for new capacity to prevent demand side market power abuse – this needs study.*
4. *Evaluating the demand-side concerns requires a consideration of market design, the interactions of the ICAP markets with the bilateral market, and a full understanding of the regulatory obligations and incentives facing large load-serving entities.*
5. *While beyond the scope of the current mitigation measures, MMP is committed to study and work with Market Participants to address this issue.*

# Analysis and Conclusions

- 1 Market power in the NYC capacity markets
  2. *Demand-side concerns*

## Conclusion:

- *MMP has concerns about demand-side market power in NY capacity markets. We note, however, that our market power concerns are focused on linkages between the NYISO capacity markets, the bilateral market, and regulatory support for new investment.*
- *Therefore, evaluating the demand-side concerns requires a consideration of market design, the interactions of the ICAP markets with the bilateral market, and a full understanding of the regulatory obligations and incentives facing large LSEs.*
- *MMP is continuing to investigate this and expect that a solution, if required, will be similarly complex and beyond what could be achieved through the narrow and short-run domain of existing and proposed In-City capacity market mitigation measures.*

# Analysis and Conclusions

## 2 The adequacy of Market Power Mitigation Measures

### 1. *Current Mitigation Measures*

#### Discussion:

1. *The real value of the nominally fixed price-cap has eroded since 1998.*
2. *The financial and reference information underlying the Demand Curve eventually becomes outdated, diluting its ability to mitigate market power effectively.*
3. *Current arrangements may be deficient in managing supply side market power especially in situations where the available capacity is substantially in excess of requirements.*
4. *The current situation of surplus capacity is expected to be short-lived, suggesting that current market power concerns will not be sustained as load continues to grow.*
5. *Currently there are no mitigation measures for demand side market power.*

For Discussion Only

# Analysis and Conclusions

## 2 The adequacy of Market Power Mitigation Measures

### 2. *Proposed Mitigation Measures*

#### Discussion:

1. *The proposed measures appear to be an outcome of negotiations and do not have a basis in economic theory.*
  - ◆ We find no basis for taking 75% of the 2005 CONE.
2. *The proposed measures (and the current measures) do not address demand-side market power concerns.*
3. *The proposed bid-cap of \$82/kW-Year based on 75% of the 2005 CONE translates into a UCAP equivalent of \$9.43/kW-Month in summer and \$6.12/kW-Month in winter. This places stronger curbs on what DGO's can offer for their capacity.*
4. *The 3% Conduct threshold and 3% Impact test place a very stringent control on the DGOs' ability to influence prices.*

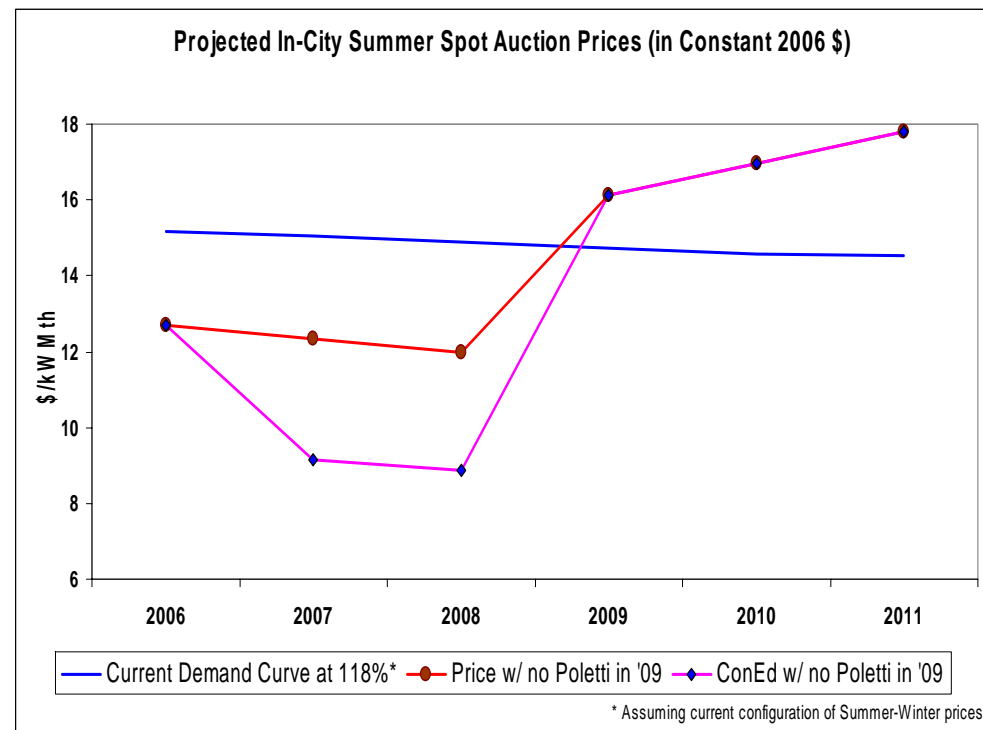
# Analysis and Conclusions

## 2 The adequacy of Market Power Mitigation Measures

### 2. Proposed Mitigation Measures

#### Discussion:

- 5. *The proposal only addresses short-term market power situations under capacity excess.*
- 6. *The mitigation measures do not affect expected capacity prices when the market is close to or in shortage. These prices are only affected by the reset of the demand curve.*



For Discussion Only

# Analysis and Conclusions

## 2 The adequacy of Market Power Mitigation Measures

### 2. Proposed Measures

*Although MMP has concerns about the design of the proposed measures, recognizing a number of imperfections and industry concerns, there is no economic case to reject them.*

- ◆ We note that the proposed measures received almost 70% of the vote in the committee decision process
- ◆ While the proposed measures are imperfect, so too are the current measures.
- ◆ The proposed measures, although lacking theoretical rigor, have the effect of promoting a more competitive outcome in the limited scenario of surplus capacity; they will have no effect when capacity is less than the reliability requirement.
- ◆ MMP will continue to work with Market Participants in the demand curve reset process and ICAP-WG agenda items to address longer run concerns.



# Analysis and Conclusions

## 3 Conclusion

- ◆ MMP confirms that demand side market power is an issue in the NYC capacity market that is imperfectly managed by the current mitigation measures.
- ◆ The proposed mitigation methods will lead to outcomes that are closer to the competitive outcomes under surplus conditions.
- ◆ Under scarcity conditions prices will be set by the Demand Curve and MMP expects there to be scarcity two to three years from now.
- ◆ MMP has equity and regulatory uncertainty concerns but these are best addressed by the FERC.
- ◆ Market Monitoring will continue to work with market participants and the appropriate NYISO committees on
  - *Demand side market power,*
  - *Rest-of-state issues,*
  - *Forward capacity markets; and*
  - *The reset of the Demand Curve.*

**For Discussion Only**