

Comments on Cost Allocation/Recovery for Reliability Upgrades

The following are some comments from KeySpan-Ravenswood, LLC.

1. When a reliability upgrade is i) Regulated, ii) ISO ordered, or iii) procured out-of-market, it is an indication that market or signals are incorrect. Specifically, it is an indication that the market is not providing the correct price signal to induce entry of required resources or maintain existing resources. Therefore, at the first indication that required resources are not entering the market as required to meet reliability needs, market changes must be implemented in a timely manner to correct the market signals. If for some reason the reliability resource is required before a market change can be made and have the necessary effect, changes to the market should be made in parallel with the reliability resource implementation. Considering the time to conceive, design and install a reliability upgrade, it should be possible to do so. In other words, the reliability upgrade would be accompanied by market revisions that would prevent further market deterioration and assure the market is providing the price signal that was required to induce entry of the out-of-market resource. Essentially, if a reliability resource is ordered into the market at a cost of \$X, the market needs to reflect that same cost.

2. When a reliability upgrade is i) regulated and assured cost recovery, ii) ordered by the ISO, or iii) procured by some other out-of-market mechanism and the underlying market flaw is not corrected, it will further depress already flawed market prices. The reliability resource will increase supply but not have to compete for cost recovery and accordingly it will be a price taker at the bottom of the supply curve even though it may be more expensive than other existing resources. Again, the already depressed market signals will be further depressed.

3. Uncorrected, these further depressed market prices will place additional pressure on marginal units and subject them to possible retirement. These retirements would occur at the same time additional resources are being ordered and required for reliability. This will lead to additional resources being required for reliability and the cycle will continue until the market signals are corrected or until all resources are subject to reliability contracts. This would essentially be the end to market based rates and a return to cost/rate based regulation.

4. Therefore, KeySpan views the correction of market signals to be a requirement that must either precede or accompany any reliability resource procurement. Correct and uniform market signals must be provided to all resources to ensure entry of new resources and maintenance of existing resources. Resources providing the same service should receive the same market signal. As stated above, if a reliability resource is ordered into the market at a cost of \$X, the market needs to reflect that cost.

5. Notwithstanding the above, KeySpan recognizes that it may be inefficient to develop a market to signal the need for certain reliability equipment. Cost based recovery for these types of reliability equipment would be appropriate. However, generation or transmission capacity additions are not the type of reliability equipment upgrades that are not able to have appropriate market signals developed. Any generation or transmission capacity reliability additions must therefore be accompanied by corrections to market signals or the only resource additions will be in response to a reliability crisis.

6. With respect to cost recovery, KeySpan would prefer the TO seek recovery directly from the Federal Energy Regulatory Commission ("FERC") and or the New York Public Service

Commission regardless of type of upgrade. KeySpan thinks this may simplify the allocation issues and avoid the need to determine who the beneficiaries are. Customers obtaining service within the TO's service territory will pay a proportional share of the cost and wholesale transmission users will pay in accordance with the rate design approved by FERC. Incentives over and above existing cost based rate recovery tariffs should not be required because cost recovery is assured so there is no more risk than what exists for the TO's other assets.

7. By taking these issues into consideration in the context of reliability upgrades, KeySpan thinks it will aid the discussions related to projects intended to relieve congestion. Economic considerations, characterized by the existence of congestion, should not be transformed into reliability upgrades. Moreover, it must be clearly stated that generation or transmission capacity increases that are the subject of regulated recovery do not eliminate congestion. These rate regulated projects merely shift the current "cost" of congestion to a firm capacity payment regardless of market conditions. The firm capacity payment could turn out to be greater than or less than what the market based cost would have been but it will be customers that will be at risk not the developer. Accordingly, all efforts should be toward developing a market that has the appropriate signals to ensure reliability and cost efficient congestion.

8. While KeySpan thinks the NYISO should view the ISO-NE cost allocation order for some guidance on FERC's perspective, the NYISO should nevertheless continue to work with its stakeholders to reach a greater consensus than the disagreement that accompanied ISO-NE's proposals and takes into account the other market design elements that exist in New York.