

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

**New York Independent System Operator, Inc.     )     Docket No. ER05-428-000**

**MOTION OF  
THE NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.  
FOR LEAVE TO SUBMIT A RESPONSE AND RESPONSE TO PROTESTS**

Pursuant to Rules 212 and 213 of the Commission’s Rules of Practice and Procedure,<sup>1</sup> the New York Independent System Operator, Inc., (“NYISO”) hereby respectfully requests leave to respond, and responds to the comments and protests (collectively the “Protests”), filed in response to the NYISO’s proposed modifications to its Market Administration and Control Area Services Tariff (“Services Tariff”) to implement installed capacity (“ICAP”) demand curves (“Demand Curves”) for the ICAP market for capability years 2005/2006, 2006/2007, and 2007/2008.<sup>2</sup> The NYISO seeks leave to respond to the Protests submitted by: (1) AES Eastern Energy, L.P.<sup>3</sup>; Dynegy Power Marketing, Inc. and Dynegy Northeast Generation, Inc.<sup>4</sup>;

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<sup>1</sup> 18 C.F.R. §§ 212, 213 (2004).

<sup>2</sup> *New York Independent System Operator, Inc.*, New York Independent System Operator, Inc.’s Tariff Revisions to Implement Revised ICAP Demand Curves, Docket No. ER05-428-000 (Jan. 7, 2005) (“NYISO Filing”).

<sup>3</sup> *New York Independent System Operator, Inc.*, Motion to Intervene and Comments of AES Eastern Energy L.P., Docket No. ER05-428-000 (Jan. 28, 2005) (“AES Comments”).

<sup>4</sup> *New York Independent System Operator, Inc.*, Motion to Intervene and Protest of Dynegy Power Marketing, Inc. and Dynegy Northeast Generation, Inc. in Support of the Protest of the Independent Power Producers of New York, Inc., Docket No. ER05-428-000 (Jan. 28, 2005) (“Dynegy Protest”).

KeySpan-Ravenswood, LLC<sup>5</sup>; the Mirant Companies<sup>6</sup>; the NRG Companies<sup>7</sup>; and the Independent Power Producers of New York, Inc.<sup>8</sup> (together, the “Generator Intervenors”); (2) New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, Multiple Intervenors, and Municipal Electric Utilities Association of New York<sup>9</sup>; and (3) the City of New York<sup>10</sup> (all the foregoing referred to collectively as the “Protesting Parties”).

### **REQUEST FOR LEAVE TO SUBMIT RESPONSE**

The NYISO recognizes that the Commission generally discourages responses to protests. The Commission has, however, allowed such responses when they help to clarify complex issues, provide additional information that will assist the Commission, correct inaccurate

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<sup>5</sup> *New York Independent System Operator, Inc.*, Motion to Intervene, Protest, and Comments of KeySpan-Ravenswood, LLC, Docket No. ER05-428-000 (Jan. 28, 2005) (“KeySpan Protest”).

<sup>6</sup> *New York Independent System Operator, Inc.*, Motion to Intervene, Supporting Comments and Limited Protest of the Mirant Companies, Docket No. ER05-428-000 (Jan. 28, 2005) (“Mirant Comments”).

<sup>7</sup> *New York Independent System Operator, Inc.*, Motion to Intervene and Protest of the NRG Companies, Docket No. ER05-428-000 (Jan. 28, 2005) (“NRG Protest”).

<sup>8</sup> *New York Independent System Operators, Inc.*, Motion to Intervene, Supporting Comments and Limited Protest of Independent Power Producers of New York, Inc., Docket No. ER05-428-000 (Jan. 28, 2005) (“IPPNY Limited Protest”).

<sup>9</sup> *New York Independent System Operator, Inc.*, Motion to Intervene and Protest of New York State Electric & Gas Corporation, Rochester Gas and Electric Corporation, Multiple Intervenors and Municipal Electric Utilities Association of New York, Docket No. ER05-428-000 (Jan. 28, 2005) (“NYSEG Protest”).

<sup>10</sup> *New York Independent System Operator, Inc.*, Motion to Intervene and Protest of the City of New York, Docket No. ER05-428-000 (Jan. 28, 2005) (“City of New York Protest”).

statements, or are otherwise helpful in developing the record in a proceeding.<sup>11</sup> The NYISO's response meets this standard. The NYISO's response does not introduce new arguments, but instead is submitted for the limited purpose of clarifying certain factual matters and correcting inaccurate or misleading statements in the Protests, thereby assisting the Commission in its review and consideration of the complex issues presented in this proceeding. The NYISO therefore respectfully requests that the Commission exercise its discretion and accept the NYISO's response.

## RESPONSE

### A. *The Generator Intervenors' Efforts to Turn This Docket Into a GT Rate Case Are Misplaced*

The Generator Intervenors, either individually or by joining in the IPPNY Limited Protest, or both, make a series of detailed arguments about the specific cost, operating or other characteristics of a particular model gas turbine (GT) generator, and assert that those facts require significant increases in the Demand Curves.<sup>12</sup> In effect, the Generator Intervenors are trying to turn this proceeding into a GT rate case, claiming that the Demand Curves must be based on data and methodologies that are "in accordance with rate making principles in order for

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<sup>11</sup> See, e.g., *Morgan Stanley Capital Group, Inc. v. New York Independent System Operator, Inc.*, 93 FERC ¶ 61,017 at 61,036 (2000) (accepting an answer that was "helpful in the development of the record . . ."); *New York Independent System Operator, Inc.*, 91 FERC ¶ 61,218 at 61,797 (2000) (allowing "the NYISO's Answer of April 27, 2000, [because it was deemed] useful in addressing the issues arising in these proceedings . . ."); *Central Hudson Gas & Electric Corp.*, 88 FERC ¶ 61,138 at 61,381 (1999) (accepting prohibited pleadings because they helped to clarify the issues and because of the complex nature of the proceeding).

<sup>12</sup> See, e.g., NRG Protest and KeySpan Protest.

rates to be just and reasonable.”<sup>13</sup> ICAP payments, however, are not statutory entitlements akin to classic just and reasonable rates. In *Sithe New England Holdings, LLC v. FERC*,<sup>14</sup> the First Circuit correctly recognized that characterizing ICAP as a statutory entitlement is “fatally wrong.”<sup>15</sup> Just and reasonable rates are “revenues that compensate carriers for their investment and expenses . . . [such as] the rates that [generators] charge when they sell their surplus power or sell standby rights assuring access to that power.”<sup>16</sup> But the “ICAP charge, by contrast, is not of this ilk. Rather it is a payment to suppliers *over and above* the amount they charge for power sold to or reserved for buyers.”<sup>17</sup> Indeed, as the Court noted: “If ICAP charges were abolished by FERC tomorrow, the sellers could object that FERC was behaving unreasonably in its ‘on and off’ regulatory policies but not that they were deprived of a just and reasonable rate.”<sup>18</sup> Consequently, Generator Intervenors’ claim of entitlement to a “just and reasonable ICAP rate” determined through traditional ratemaking methodologies is, in the words of the court, nothing more than an abused slogan.<sup>19</sup>

Even if the precise cost of a particular GT built in a particular place at a particular time could be determined with a precision that would satisfy the Generator Intervenors, that is not the goal of the analysis. As stated in the August 16, 2004, report of Levitan & Associates, the

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<sup>13</sup> KeySpan Protest at 4, 9, 27.

<sup>14</sup> 308 F.3d 71 (1st Cir. 2002).

<sup>15</sup> *Id.* at 77.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* (emphasis in original).

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

“ICAP reference values are based on the capital and operating costs of *hypothetical* gas turbine peaker additions located in the three regions in the 2005, 2006, and 2007 capacity years.”<sup>20</sup>

Thus, establishing reference values for the Demand Curves requires a series of judgments and trade offs, as done by the NYISO, and the exercise of the Commission’s expertise and discretion, and not simply the performance of a rate-case calculation that “reflect[s] the cost of entry of a marginal resource into the NYC capacity market” or the other New York capacity markets.<sup>21</sup> As stated in the NYISO’s September 22, 2004, Demand Curve proposal, “the new Demand Curve parameters proposed in the attachments hereto by the NYISO are intended to reflect a reasonable determination of typical costs and revenues that balances the objectives of providing appropriate compensation to generators while providing reliable service to energy consumers at a reasonable cost.”<sup>22</sup>

*B. All of the Protests Seek to Cherry-Pick Individual Demand Curve Factors, or Urge Result-Oriented Arguments, in an Effort to Skew the Result in Their Favor*

As noted in the NYISO’s Filing, throughout the Demand Curve stakeholder and Board review processes, “[d]ifferent interested parties have advocated higher or lower curves that would favor their interests,”<sup>23</sup> and this continues to be the case, with generators pushing in one direction and loads pushing in the other. The Protesting Parties each single out one analytic factor or another, without taking a balanced or consistent approach. For example, generators have repeatedly characterized supply conditions in New York as tight, as a predicate for

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<sup>20</sup> NYISO Filing, Attachment III at (i) (emphasis added).

<sup>21</sup> NRG Protest at 12-13.

<sup>22</sup> NYISO Filing, Attachment IV at 4.

<sup>23</sup> NYISO Filing at 9.

advocating measures that will increase supply while increasing their returns.<sup>24</sup> Yet, at the same time the Generator Intervenors complain that the determination of the Net Revenue (“NR”) Offset<sup>25</sup> should not have considered prices in 2002, on the grounds that warm temperatures led to relatively high loads and high prices—that is, supply and demand conditions that were relatively tight.<sup>26</sup> Similarly, IPPNY claims that “forecasts of scarcity-related price spikes are inherently uncertain and cannot be relied upon to any meaningful degree by those making investment decisions.”<sup>27</sup> Elsewhere, however, generators have repeatedly extolled the necessity of their reaping the benefit of price spikes. Needless to say, IPPNY does not claim that its members would forego price spike revenues as a trade-off for what it considers appropriate Demand Curves.

None of the Protesting Parties takes a truly balanced approach that not only recognizes the competing interests at stake, but also evaluates all of the factors together to derive an overall result that seeks to best achieve the objectives of the Demand Curves. It is simply not the case, as NRG claims, that: “In each instance where NYISO could be said to have exercised its judgment in determining the Annual Revenue Requirement or level of NR Offsets, NYISO accepted assumptions and parameters that resulted in lower Demand Curve reference values that

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<sup>24</sup> *See, e.g.*, NRG Protest at 11 (asserting that “NYC faces supply shortages, and the market is already failing to send the needed price signals to spur the investment needed to prevent those shortages.”).

<sup>25</sup> Unless otherwise specified, capitalized terms used herein have the meanings specified in the NYISO Filing, or in the NYISO’s Market Administration and Control Area Services Tariff.

<sup>26</sup> *See, e.g.*, NRG Protest at 16; KeySpan Protest at 3.

<sup>27</sup> IPPNY Limited Protest at 10.

do not realistically reflect the true cost of entry into NYC.”<sup>28</sup> Indeed, contemporaneous studies for ISO-NE and PJM produced lower revenue requirements, indicating that the NYISO’s “GT revenue requirement for New York may be in the upper area of the range of revenue requirement estimates.”<sup>29</sup> Similarly:

The NYISO had data points available to it that indicated that the expected NR offset could range from \$12 to \$18 for a reasonably ‘tight’ NYCA market and could increase under circumstances where total capacity supply just equals the minimum NYCA capacity requirement. It was the NYISO’s judgment that the median point in this range would provide a reasonable result and elected, therefore, to adopt an expected value for NRs of \$15.<sup>30</sup>

As shown in the NYISO’s Filing, and “as the Board found, the proposed curves generally are set at a middle ground between these competing interests, and seek a reasonable accommodation between the offsetting considerations implicated in establishing ICAP Demand Curves.”<sup>31</sup>

*C. None of the Protesting Parties Claims that It Did Not Have a Full Opportunity to Express Its Views in the Stakeholder Process and to the Board*

Both NRG and KeySpan include a number of attachments in support of their protests.

These attachments, however, are materials that date back to the stakeholder process,<sup>32</sup> or were available at the time of the stakeholder process.<sup>33</sup> Neither NRG nor KeySpan, nor any other of

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<sup>28</sup> NRG Protest at 5.

<sup>29</sup> NYISO Filing, Attachment IV (September 30, 2004 NYISO Clarification of Proposed ICAP Demand Curves) at 2.

<sup>30</sup> *Id.* at 3.

<sup>31</sup> NYISO Filing at 9-10.

<sup>32</sup> *See, e.g.* NRG Protest, Attachment F (PA Consulting Group letter dated August 25, 2004).

<sup>33</sup> *See, e.g.*, NRG Protest, Attachment C (NYISO Power Trends report dated May, 2004).

the Protesting Parties, claims that they did not have an adequate opportunity to present any and all information they deemed relevant to the NYISO staff or the NYISO Board of Directors.

Thus, the protests renew arguments previously made in the stakeholder and Board reviews.<sup>34</sup>

The Commission should conclude, as did the Board, that

opinions in one direction were offset by opinions in the opposite direction, and that a persuasive case had not been made for adopting any of the alternate values advocated by any of the entities presenting arguments. The Board also concluded that it had not been presented with persuasive evidence that the proposed values, or that the independent review or stakeholder processes, were significantly biased or skewed against the objectives of the Demand Curve.<sup>35</sup>

IPPNY makes repeated *ad hominem* assertions that the NYISO brought Dr. Patton into the process “at the 11<sup>th</sup> hour.”<sup>36</sup> In fact, as noted in the NYISO’s September 22, 2004, Demand Curves proposal, the NYISO issued the Demand Curves “in consultation with its Independent Market Advisor,” Dr. Patton.<sup>37</sup> The NYISO Board found that “Dr. Patton performed an independent analysis of the historical net revenue levels in the NYISO markets and met with the NYISO and stakeholders on several occasions to discuss the results of his analysis . . . .”<sup>38</sup> Moreover, as IPPNY acknowledges, the issuance of the proposed Demand Curves was followed by “two rounds of comments by stakeholders and oral argument before the Market Performance Committee of the NYISO Board (‘Board’).”<sup>39</sup> IPPNY does not and cannot contend that the

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<sup>34</sup> See NYISO Filing at 4-5.

<sup>35</sup> *Id.* at 9.

<sup>36</sup> IPPNY Limited Protest at 3, 4, 7.

<sup>37</sup> NYISO Filing, Attachment IV at 1.

<sup>38</sup> NYISO Filing, Attachment VI, at 2 (NYISO Board Decision on Review).

<sup>39</sup> IPPNY Limited Protest at 7.



Demand Curves were not adopted in accordance with the approved stakeholder and Board review procedures.

*D. The Zero Crossing Point Should Not be Changed*

NYSEG asserts that the Zero Crossing Point should be set to a significantly lower value and claims that the NYISO cannot cite the Levitan & Associates' report for keeping the Zero Crossing Point at the proposed value, but ignores several critical considerations. First, the Levitan & Associates' report does in fact state that "we do not advocate any alteration in the zero-crossing points used to define the demand curves," and further states that in reaching this conclusion Levitan & Associates "assessed the total cost of ICAP under a range of zero point crossings—the point where the demand curve meets the \$0 value on the X axis."<sup>40</sup> Thus, it is simply not correct to assert that the Levitan & Associates' conclusion was based on a unique slope determined by the proposed Zero Crossing Point and a particular Reference Value. Levitan & Associates considered a range of different possible slopes for the Demand Curves.

In addition, NYSEG overlooks the fact that the Demand Curve proposal includes an annual escalation in the Reference Value, which will have the effect of increasing the slope of the Demand Curves.<sup>41</sup> NYSEG makes no showing that the slope of the Demand Curves should be increased both by lowering the proposed Zero Crossing Point *and* by an escalation of the Reference Value.

Finally, NYSEG overlooks the fact that the proposed Zero Crossing Point is also based on two years of successful experience with Demand Curves based on that same Zero Crossing

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<sup>40</sup> NYISO Filing, Attachment III, at 66, 57.

<sup>41</sup> NYISO Filing, Attachment IV, at 5-6 (September 22, 2004, Demand Curve proposal).

Point. As the KeySpan Protest points out: “The NYISO’s report on the first 18 months of operation of the Demand Curve indicated that it is working well and that the NYISO has observed the beginnings of trends in the ICAP markets, as well as market behaviors and outcomes that were anticipated.”<sup>42</sup> In addition, the proposed Zero Crossing Point provides an opportunity for most existing generation to participate in the capacity markets. In sum, NYSEG’s contention that the Zero Crossing Point should be significantly lower is deficient in several crucial respects.

The City of New York contends that “the zero-crossing point for Zone J for 2005/2006 should be set at 18% above the in-City locational requirement, but for the two succeeding years, the NYISO should conduct the comprehensive analysis recommended by Levitan to determine the appropriate zero-crossing points.”<sup>43</sup> While the NYISO certainly intends to analyze the performance of the Demand Curves on an on-going basis, annual changes in the Zero Crossing Point would undermine the highly valuable predictability associated with resetting the Demand Curves only every three years.

*E. The Proposed \$5 Correction in the Winter/Summer Adjustment is Appropriate*

As pointed out in the NYISO’s Filing:

Since their inception, the ICAP Demand Curves have incorporated an adjustment to account for the greater potential supply of capacity in the winter (and thus lower prices) than in the summer that results from generators being capable of higher output in the winter, primarily because of the lower ambient temperatures. The Demand Curves are adjusted upward so that the resulting summer and winter capacity prices will, on average, equal the Annual Reference Value. As initially implemented, however, this adjustment recognized only changes in the capability

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<sup>42</sup> KeySpan Protest at 6.

<sup>43</sup> City of New York Protest at 8.

of internal generation, and did not consider any seasonal effects related to imports or exports of capacity.<sup>44</sup>

Because the original adjustment considered only differences in the capacity of internal generation, the NYISO determined that a \$5 correction to the adjustment was needed to account for the upward price pressure of lower external capacity availability in the winter compared to the summer period. The City of New York criticizes the NYISO for not applying this differential to the New York City and Long Island Demand Curves. Both the New York City and Long Island load zones, however, have significant locational requirements for ICAP—80% and 99%, respectively. Consequently, external sources of ICAP are largely irrelevant to those locational ICAP markets and, therefore, the \$5 correction is not applicable to the NR Offsets for the NYC and LI constrained load zones.

IPPNY asserts that the NYISO incorrectly relies on experience with capacity imports from Hydro Quebec as a basis for the proposed \$5 NR Offset correction and contends that external ICAP supplies are derived from numerous sources. While IPPNY is correct that external ICAP is available over several interfaces with the NYCA, the NYISO's adjustment reflects the facts that: (i) the decreases in available external capacity have been experienced largely over the Hydro Quebec interface; and (ii) the New England and PJM interfaces are heavily subscribed at all times, so that additional external ICAP cannot flow over these ties during the winter season to compensate for HQ's significantly reduced exports to New York from its winter peaking system.<sup>45</sup> The NYISO's proposed adjustment was reasonably based on the actual decreases in external ICAP supplies experienced from Hydro Quebec in previous

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<sup>44</sup> NYISO Filing at 7.

<sup>45</sup> See <http://www.nyiso.com/markets/icapinfo.html>.

winter periods, which can be expected to continue for the foreseeable future as Hydro Quebec continues to be a winter peaking system.<sup>46</sup>

IPPNY asserts that the Winter/Summer adjustment failed to consider additional winter capacity from three new combined cycle units, and thus should have been based on a 1700 MW differential rather than the 1400 MW Gold Book Winter/Summer differential.<sup>47</sup> Contrary to IPPNY's assertions, the additional capacity from the new units was considered in the analysis. As indicated in the September 30, 2004, NYISO Clarification of Proposed ICAP Demand Curves, in the 2003/2004 Winter Capability Period, the actual excess winter capacity was approximately 600 MW.<sup>48</sup> An additional 300 MW from the new units would mean an excess of approximately 900 MW, for a difference from the 1400 MW Gold Book value of 500 MW. At a revenue difference of approximately \$1/kW year for each decrement of 110 MW from the 1400 MW seasonal performance difference assumption, an adjustment of around \$5 is appropriate and is consistent with consideration of the additional MW from the new combined cycle units.

*F. The Demand Curves Will Not Develop New Seams Issues with PJM or ISO-NE*

NYSEG contends that the Demand Curves will be likely to develop new seams issues with PJM and ISO-NE.<sup>49</sup> The NYSEG Protest provides no specifics, however, on what such a "seam issue" might be. Moreover, the Commission concluded in its initial approval of the use of the Demand Curves that it "is not convinced that the implementation of the ICAP Demand Curve

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<sup>46</sup> See, e.g., [http://www.hydroquebec.com/visit/virtual\\_visit/reservoir.html](http://www.hydroquebec.com/visit/virtual_visit/reservoir.html) and <http://www.hydroquebec.com/transenergie/en/reseau/bref.html>.

<sup>47</sup> IPPNY Limited Protest at 18-19.

<sup>48</sup> NYISO Filing, Attachment IV at 3.

<sup>49</sup> NYSEG Protest at 19-20.

will create seams with neighboring regions. The potential sale of ICAP into New York is a market response, is not an example of a seam, and is something that is made possible or is allowed by the tariffs in PJM and ISO-NE.”<sup>50</sup> In addition, NYSEG ignores “Dr. Patton's conclusion that the assumptions underlying the Levitan study were consistent with the assumptions made in PJM and New England in the development of the capacity market parameters in those markets.”<sup>51</sup> While continued consultation and cooperation on setting and meeting regional capacity requirements between the NYISO, PJM, and ISO-NE is certainly appropriate as the latter continue to develop installed capacity markets with demand curves, delay or redetermination of the Demand Curves on the basis of NYSEG’s at best inchoate “seams” allegations would not be appropriate.

### CONCLUSION

Accordingly, for the reasons set forth above and in the NYISO Filing, the NYISO

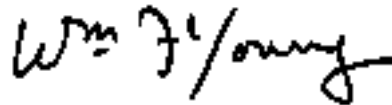
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<sup>50</sup> *New York Independent System Operator, Inc.*, 103 FERC ¶ 61,201 at P87 (2003).

<sup>51</sup> NYISO Filing at 9.

respectfully requests the Commission to deny the Protests of the Protesting Parties, and to approve the Demand Curves as filed.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Wm F. Young". The signature is written in a cursive, somewhat stylized font.

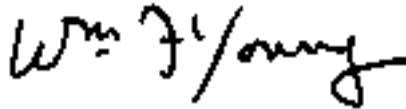
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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon each person designated on the official service lists compiled by the Secretary in this proceeding in accordance with the requirements of Rule 2010 of the Rules of Practice and Procedure, 18 C.F.R. § 385.2010.

Dated at Washington, DC this 14th day of February, 2005.

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Submission Contents

ResponseICAPprotests.doc..... 1-15