

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

New York Independent System Operator, Inc.) Docket No. ER02-____-000

**MOTION OF THE
NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.
FOR PERMISSION TO WAIVE PERFORMANCE CHARGES
THAT COULD NOT ACCURATELY OR FAIRLY BE ASSESSED,
OR THAT WERE DEFERRED ON AN INTERIM BASIS**

Pursuant to Rule 212 of the Commission's Rules of Practice and Procedure,¹ the New York Independent System Operator, Inc. ("NYISO") hereby respectfully requests that the Commission grant it permission to waive: (i) performance charges applicable to certain categories of Generators² that were previously deferred on an interim basis by the NYISO; and (ii) performance charges applicable to suppliers of Regulation and Frequency Response Service ("Regulation") that could not be accurately or fairly assessed. The requested waivers will avoid the imposition of charges in a manner that would be arbitrary and inconsistent with efficient market design principles. Imposing the charges at this time would also have a disruptive market effect and would unreasonably upset the expectations of parties to contracts that were executed before the NYISO commenced operations.

I. Copies of Correspondence

Communications regarding this proceeding should be addressed to:

Robert E. Fernandez, General Counsel and Secretary Arnold H. Quint

¹ 18 C.F.R. § 385.212 (2002).

² Capitalized terms that are not otherwise defined herein shall have the meaning specified in Article 2 of the NYISO's Market Administration and Control Area Services Tariff ("Services Tariff").

Belinda R. Thornton, Director of Regulatory Affairs
New York Independent System Operator, Inc.
3890 Carman Road
Schenectady, NY 12303
Tel: (518) 356-7661
Fax: (518) 356-4702
rfernandez@nyiso.com
bthornton@nyiso.com

Ted J. Murphy
Hunton & Williams
1900 K Street, N.W.
Washington, D.C. 20006
Tel: (202) 955-1588
Fax: (202) 778-2201
aquint@hunton.com
tmurphy@hunton.com

II. Background

A. Performance Charges Included in the NYISO's Original Market Design

When the NYISO commenced operation, its market rules included performance charges applicable to Regulation Suppliers as well as to Suppliers that did not provide Regulation. Specifically, under the NYISO's original market rules, Regulation Suppliers that deviated from the Automatic Generation Control ("AGC") Base Point Signals sent every six seconds by the NYISO were required to pay a charge equal to the deviation in MWh multiplied by the applicable market clearing availability price for Regulation.³ Non-Regulation Suppliers that deviated from the Security Constrained Dispatch ("SCD")⁴ Base Point Signals sent every five minutes by the NYISO, were required to pay a similar charge. These charges were intended to encourage Suppliers to follow their schedules and thereby to help the NYISO improve the level of Control Performance achieved by its predecessor, the New York Power Pool ("NYPP").⁵

³ See Schedule 3, Section 4.1 of the currently effective Services Tariff.

⁴ SCD is a computerized algorithm that performs the NYISO's real time dispatch by evaluating the New York Control Area contingency set against the system conditions expected for the next 5 minutes, or a shorter period under certain circumstances. SCD's results are a key input in the calculation of real-time market-clearing prices. See also Services Tariff § 2.166.

⁵ These market rules were accepted in *Central Hudson Gas & Electric Corp., et al.*, 86 FERC ¶ 61,062 at 61,227 (1999); *order denying reh'g*, 88 FERC ¶ 61,138 at 61,386 (1999).

On November 12, 1999, the NYISO and the then Member Systems of the NYPP (“Member Systems”)⁶ jointly submitted a proposal to the Commission that would have exempted the following categories of Generators from performance charges otherwise applicable to non-Regulation Suppliers: (i) Qualifying Facilities (“QFs”) selling Energy within the New York Control Area under existing Public Utility Regulatory Policies Act of 1978 (“PURPA”) contracts; (ii) existing topping or extraction turbine Generators, or Generators replacing or re-powering such facilities, that produce electric Energy as a result of supplying steam to New York City’s district steam system (up to a 365 MW maximum); and (iii) any Generator that is a non-schedulable renewable resource and that was either operating or attempting to commence construction as of November 18, 1999, or among the first 500 MW of renewable resources to begin development after November 18, 1999.⁷ The Commission rejected this proposal without prejudice to its being refiled with more “appropriate justification.”⁸

B. Post Start-Up Issues Affecting the NYISO’s Ability to Assess Performance Charges Accurately or Fairly

As the NYISO approached its start-up date in November 1999, it became apparent that the legacy equipment used to regulate the bulk power transmission system was inadequate to support a market-based Regulation model. The NYISO and the Member Systems, who had used their own systems to regulate generation in their service territories prior to NYISO start-up

⁶ The “Member Systems” were the eight Transmission Owners that comprised the membership of the New York Power Pool. The group formerly known as Member Systems of the New York Power Pool are currently known as Members of the Transmission Owners Committee of the Energy Association of New York State.

⁷ See *Joint Filing of the New York Independent System Operator, Inc. and Member Systems of the New York Power Pool*, Docket No. ER00-556-000 (November 12, 1999).

⁸ See *New York Independent System Operator, Inc., et al*, 90 FERC ¶ 61,015 (2000); *order on reh’g*, 91 FERC ¶ 61,012 (2000).

consequently agreed to utilize an interim AGC process. Under the interim process, the NYISO would calculate a statewide Control Error, separate it into eight different Satellite Control Error (“SCE”) signals and electronically forward them to the Member Systems. For some Member Systems, the SCE from the NYISO triggered their own AGC programs to calculate and send out six-second base point signals to the regulating units in their territory. Others took the NYISO-provided Base Point Signals and converted them into raise/lower pulses depending on the Generator’s output at a given moment. The base point value itself was sent to the Generator via the Internet.

Many, if not all, of the Member Systems were also using their AGC systems to send five-minute base point signals to non-regulating Generators located in their Transmission Districts that were providing On-Dispatch service. This interim AGC system allowed the NYISO and the Member Systems to continue to rely on existing technology to operate New York’s bulk power transmission system reliably while phasing in the new technology required to operate a Regulation market.

However, directing the output of Regulation Suppliers using the Member Systems’ existing AGC systems, or via raise/lower pulses based on the NYISO Base Point Signals, made it impossible for the NYISO to measure Generators’ performance accurately. Although, the NYISO’s Performance Tracking System (“PTS”) measured actual output against the Base Point Signals created by the NYISO’s AGC system Generators were actually responding to base points calculated by the Member Systems’ AGC software. Since the NYISO had no reason to believe that the base points calculated by its AGC system were identical to those calculated by the Member Systems’ AGC software, it was impossible for the NYISO to assess accurately the extent to which Regulation and non-Regulation Suppliers were following the base points they

received. Without an accurate assessment of Generators' performance it was impossible to assess performance charges against them accurately or fairly.⁹

By January 2000, the Member Systems had stopped using their AGC systems to create and send five minute base point signals from the NYISO to non-regulating Generators and were, instead able to relay SCD Base Point Signals from the NYISO directly to non-regulating Generators. Because the NYISO was now assured that that non-regulating Generators were receiving, through the Member Systems, five-minute SCD Base Point Signals calculated by the NYISO it began to assess performance charges against non-Regulation Suppliers, with the exception noted in Section II.C below.

Most regulating units, on the other hand, continued to receive either six-second base point signals from the Member Systems' AGC software or raise/lower pulses translated by the Member Systems from the NYISO's six-second Base Point Signals.¹⁰ Technology was not yet in place to allow for the central calculation of six-second base points or for the communication of them to all Regulation Suppliers statewide. Given these circumstances, the NYISO concluded that it would be arbitrary, unreasonable and affirmatively harmful to impose charges on Regulation Suppliers for failure to follow Base Point Signals that they were not receiving. It would also have been discriminatory to impose charges only on a small subset of Regulation Suppliers based on solely on the availability of certain equipment in their local Transmission

⁹ During the month of November 1999, communications and control problems between the NYISO and the Member Systems required the NYISO to put all Suppliers out of merit for settlement purposes. Pursuant to the then-effective NYISO tariffs, performance charges were not imposed.

¹⁰ The NYISO learned in late 2000 that some Member Systems were sending NYISO Base Point Signals directly to Generators but it was not clear when the requisite communications technology went into service.

Owner's control room. Moreover, because very few Suppliers were then providing Regulation, the NYISO was concerned that the imposition of arbitrary charges would result in dangerous Regulation shortages by causing Suppliers to stop providing Regulation.¹¹

At the same time, the absence of performance charges applicable to Regulation Suppliers did not seem to undermine the NYISO's ability to reliably operate the New York State Transmission System. Notably, after falling off sharply at the commencement of NYISO operations, the NYISO's CPS-2 performance improved dramatically.¹² Indeed, its performance was much better than it was under NYPP operations. Although the use of the interim AGC process prevented the NYISO from directly monitoring the performance of individual Generators, the NYISO was able to monitor Regulation performance on an aggregate, area-by-area basis. This permitted the NYISO to monitor and assure the stability of the New York State Transmission System.

During 2000, the NYISO completed development and installation of its new statewide AGC package that was capable of calculating Base Point Signals for regulating units and non-regulating units alike and of communicating those Base Point Signals to all Suppliers. This system was fully functional at the NYISO by December 2000.

However, the NYISO was not able to verify that all of the Member Systems had made the technological adjustments necessary to utilize NYISO-calculated Base Point Signals rather than their own for regulating generation. An informal survey conducted in the fall of 2000 yielded

¹¹ At the time, there were often as few as ten units meeting New York State's total Regulation needs. *See also* Attachment I at 3-5 (describing disincentives to provide Regulation under the NYISO's previously effective market rules.)

¹² *See* Attachment II, a report of NYPP and NYISO CPS1 and CPS2 performance for 1999, 2000 and 2001.

incomplete information. Some Member Systems reported that they continued to rely on raise/lower pulses, others reported they were passing through the NYISO six second signal and still others were using a variety of control mechanisms depending on generation and communication configurations. During a discussion of Regulation performance charges and Control Performance at the October 19, 2000 meeting of the NYISO's Business Issues Committee ("BIC"), Market Participants asked the NYISO not to begin imposing Regulation performance charges until it had obtained confirmation from the Member Systems that they could relay AGC Base Point Signals directly to Regulation Suppliers, bypassing the Member Systems' AGC software. In a December, 2000 report, the Chairman of the NYISO's Billing and Accounting Working Group informed the BIC that the NYISO had not received the requested confirmation from most of the Member Systems. The NYISO was reluctant to begin assessing performance charges against Regulation Suppliers given the lack of certainty that Generators would receive AGC Base Point Signals, the possibility that Suppliers would stop providing Regulation if they were subject to penalties for not following signals they did not receive, and the NYISO's exceptionally good Control Performance. Consequently, the NYISO postponed the implementation of performance charges for Regulation Suppliers pending the receipt of confirmations from all of the Member Systems.¹³

During the winter of 2000 - 2001, the NYISO also began discussions with Market Participants regarding possible improvements to its Regulation market rules. The NYISO and a substantial majority of Market Participants ultimately concluded that the Regulation rules should be re-designed so that Generators had economic incentives to follow Base Point Signals, instead of depending on penalties to compel Generators' performance.

¹³ See also Attachment III hereto, the Affidavit of John E. Hickey.

In June, 2001, the NYISO filed proposed revisions to its Services Tariff to institute a more efficient system for incentivizing generator performance that eliminated Regulation performance charges and established a new charge to discourage persistent undergeneration. With the Commission's acceptance of the filing, the NYISO's original Regulation performance charges ceased to be effective on July 25, 2001.¹⁴

C. Interim Deferral of Billing of Performance Charges Assessed Against Certain Special Categories of Generators

As noted above, the NYISO and Member Systems previously sought an exemption from the performance charges applicable to certain categories of non-Regulation Suppliers, *i.e.*, PURPA contract parties, New York City steam/electric generating stations, and certain intermittent resources. The Commission rejected this request without prejudice because it concluded that the request was not adequately justified.¹⁵ Subsequently, the NYISO provided an extensive explanation of why it was appropriate to prospectively exempt these types of Generators from persistent undergeneration charges,¹⁶ which supplanted Regulation performance charges as a mechanism for incentivizing Generators to follow their schedules after July 25, 2001. The Commission accepted this explanation in a October 3, 2001 letter order.¹⁷ Because

¹⁴ *New York Independent System Operator, Inc., Letter Order*, 96 FERC ¶ 61,112 (2001).

¹⁵ *See New York Independent System Operator, Inc., et al.*, 90 FERC ¶ 61,015 at 61,037 (2000) (Rejecting proposed exemption without prejudice because the applicants had "provided no rationale for exempting any class of participants from regulation charges."); *order on reh'g*, 91 FERC ¶ 61,012 at 61,051-52 (2000) (Rejecting proffered rationale for the proposed exemption because it was offered for the first time in a request for rehearing).

¹⁶ *See New York Independent System Operator, Inc., Request to Submit Compliance Filing One Day Out of Time and Compliance Filing on Regulation Penalty Exemptions*, Docket No. ER01-2251-001 (August 28, 2001).

¹⁷ *See New York Independent System Operator, Inc.*, Docket No. ER01-2251-001 (October 3, 2001).

the NYISO believed that performance charges should not have been imposed on these Generators for the exact same reasons that persistent generation charges will not be imposed on them prospectively, it deferred imposing the charges on an interim basis pending the issuance of an order addressing this Motion.

As a general matter, it is appropriate to waive performance charges applicable to the specified categories of Generators because they are either technically incapable of following NYISO Base Point Signals, are operating under grandfathered contracts that preclude the assessment of performance charges against them, or have obligations to meet steam host requirements that would subject them to significant economic hardship if they were required to follow SCD Base Point Signals.¹⁸ More specific explanations of why it is appropriate to waive performance charges for each of the special categories of Generators are set forth below.

First, it is reasonable to waive such charges for Generators that are QFs and that are selling Energy under contracts, entered into prior to November 18, 1999.¹⁹ PURPA permits QFs to sell directly to their host utilities or to wheel across their host utilities to sell to third parties. Prior to the start of NYISO operations, QFs had not been required to purchase Commission-jurisdictional transmission services when selling directly to their host utilities. Such transactions had generally been regarded as complete upon delivery of the QF power into the utilities' systems. The contracts underlying these transactions did not require the QF plants to be capable of following base point signals. Moreover, many QFs are required to meet the steam needs of

¹⁸ See Attachment I at 6-7, which endorses the NYISO's reasons for seeking a waiver of performance charges that would otherwise be applicable to these Generators.

¹⁹ The NYISO started operations on November 18, 1999. Facilities with Commission-approved settlement agreements may qualify for exemptions, pursuant to such agreements, with regard to contracts entered into subsequent to November 18, 1999. This filing is not intended to abrogate agreements reached in any such Commission-approved Settlement Agreement.

their thermal hosts or are powered by intermittent renewable resources and are therefore unable to follow five-minute Base Point Signals. Finally many of the QF contracts make the power purchaser responsible for paying operational penalties, such as NYISO performance charges, despite the fact that purchasers do not control the operation of the facility. It would not be appropriate to impose performance charges on purchasers that had no way of controlling facilities which were themselves not capable of following Base Point Signals.²⁰

The second category of Generators for which it is appropriate to waive performance charges are the steam/electric generating stations that are operated principally to meet the requirements of the New York City steam system. There are two basic configurations for these stations. The first configuration includes those electric turbine Generators in which the electric output is a by-product of the steam flow required to meet steam system demand and to maintain pressure on the steam system within acceptable limits. The second configuration relates to a Generator which, in the winter, is typically operated as a steam system unit with its full steam output going to the steam distribution system, bypassing the electric turbine.

These units, which serve the steam system demands and produce electric output reflecting them, cannot follow NYISO schedules or SCD Base Point Signals accurately. Following SCD Base Point Signals would require these units to produce too much or too little steam, thereby jeopardizing the reliability of service to the steam customers. These units are required to maintain the existing performance level for existing steam customers into the future. Because of the inherent limitations imposed on electric output by priority response to the steam

²⁰ It was presumed that contracts for the output of QF units, entered into after November 18, 1999, would be entered into with full knowledge of their parties' potential exposure to NYISO performance charges and would make adequate provisions to address them.

system requirements, it was necessary and appropriate to waive performance charges for steam/electric units.

The final category of Generators for which the NYISO is seeking a waiver are intermittent (i.e., non-schedulable) renewable resources. These are Generators, the electric output of which is dictated by, among other things, environmental elements, like water stream flow, wind velocity, sunlight, and actions taken by public authorities such as the New York State Thruway Authority, which operates the New York barge canal system, and the United States Army Corps of Engineers. These renewable resources lack the ability to control the circumstances affecting their output with the certainty required to maintain electric output schedules or to follow Base Point Signals, and thus could not avoid NYISO performance charges if they were subject to them. Moreover, subjecting such Generators to performance charges would have provided a disincentive for future investments in renewable resources.²¹

III. Motion

The NYISO respectfully requests that the Commission authorize it to waive, for the period from December 1999 to January 2000, all performance charges applicable to both Regulation and non-Regulation Suppliers during that period since it was impossible for the NYISO to accurately assess them. The NYISO also respectfully requests that the Commission authorize it to waive, for the period from January 2000 to July 24, 2001: (i) performance charges applicable to the special categories of Generators that were previously deferred on an interim basis by the NYISO for the reasons set forth above in Section II.C.; and (ii) performance charges applicable to Regulation Suppliers which, again, could not be accurately assessed due to

²¹ The NYISO believed that exempting existing intermittent generators, plus as much as 500 MW of additional intermittent resources would have been operationally manageable.

technical considerations.²² Granting these requests will be in the public interest for the following reasons.

The requested waiver will avoid the imposition of performance charges that were very likely to be arbitrary given the impossibility of accurately conveying Base Point Signals and tracking Generators' responsiveness to them during the relevant period. Because it was not possible for the NYISO to accurately calculate the charges contemporaneously, it would be impossible for the NYISO to calculate them now. Furthermore, even if it were possible to accurately approximate the charges at this point, it would disrupt the markets to impose them after so much time has passed. Second, with respect to the special categories of Generators described in Section II.C., waiving performance charges will avoid unfairly penalizing units that are physically or economically incapable of following SCD Base Point Signals. Third, with respect to Suppliers with grandfathered contracts that exempt them from performance charges, granting the requested waiver will avoid upsetting settled contractual expectations. Fourth, as the NYISO's Control Performance demonstrates, the absence of performance charges caused no harm. Finally, the NYISO and Commission have both recognized that a Regulation market based on incentivizing appropriate behavior, rather than penalizing Generators that did not comply with Base Point Signals, can achieve very good Control Performance and induce Regulation Suppliers to remain in the market.²³

²² The NYISO is not seeking permission to waive performance charges for November 1999 because its then-effective market rules did not require such charges to be assessed against Out-of-Merit units. *See supra* n. 9.

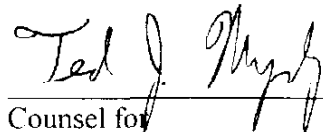
²³ *See* Attachment I at 3-5.

IV. Service List

The NYISO has mailed a copy of this filing to all persons that have executed Service Agreements under the NYISO's Services Tariff or its Open Access Transmission Tariff, to the New York State Public Service Commission, and to the electric utility regulatory agencies in New Jersey and Pennsylvania.

V. Conclusion

WHEREFORE, the New York Independent System Operator, Inc., respectfully requests that the Commission grant the waivers requested herein.


Counsel for
New York Independent System
Operator, Inc.

Arnold H. Quint
Ted J. Murphy
Gloria J. Halstead
Hunton & Williams
1900 K Street, N.W.
Washington, D.C. 20006-1109
Of Counsel

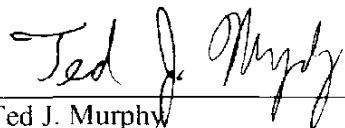
July 12, 2002

cc: Mr. Daniel L. Larcamp, Director Office of Markets, Tariffs and Rates, Room 8A-01,
Tel. (202) 208-2088
Ms. Alice M. Fernandez, Director Office of Markets, Tariffs and Rates—East Division,
Room 82-15, Tel. (202) 208-0089
Ms. Andrea Wolfman, Lead Counsel, Market Oversight and Enforcement, Office of the
General Counsel, Room 9E-01, Tel. (202) 208-2097
Mr. Stanley Wolf, Office of the General Counsel, Room 101-03, Tel. (202) 208-0891
Mr. Michael Bardee, Lead Counsel, Markets Tariffs and Rates, Office of the General
Counsel, Room 101-09, Tel. (202) 208-2068

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all persons that have executed Service Agreements under the NYISO's Services Tariff or its Open Access Transmission Tariff, to the New York State Public Service Commission, and to the electric utility regulatory agencies in New Jersey and Pennsylvania in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.2010 (2002).

Dated at Washington, DC this 12th day of July, 2002.



Ted J. Murphy
Hunton & Williams
1900 K Street, N.W.
Washington, DC 20006-1109
(202) 955-1500