

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

<b>Remedying Undue Discrimination</b>	)	
<b>through Open Access Transmission Service</b>	)	<b>Docket No. RM01-12-000</b>
<b>and Standard Electricity Market Design</b>	)	

**REPLY COMMENTS OF THE  
NEW YORK INDEPENDENT SYSTEM OPERATOR, INC.**

The New York Independent System Operator, Inc. (“NYISO”), hereby respectfully submits its reply comments in this proceeding.<sup>1</sup> They address governance, the role to be played by state regulators, the structure of market monitoring units and a handful of narrower technical issues.

**I. GOVERNANCE**

The NYISO’s *Initial Comments* on Independent Transmission Provider (“ITP”) governance supported the *Joint Petition for Declaratory Order Regarding the Creation of a Northeastern Regional Transmission Organization* (“Joint Petition”) filed by the NYISO and ISO-NE. Since that time, the Joint Petition has been withdrawn and the NYISO has begun considering, including through discussions with stakeholders, its compliance with the Commission’s ITP and Regional Transmission Organization (“RTO”) standards. The NYISO has also reviewed the governance comments submitted by other parties in this proceeding, as well as the Joint Petition docket. As a result, the NYISO is reconsidering some aspects of the position it took in the *Initial Comments*.

---

<sup>1</sup> Reply comments in this proceeding were due on February 18. The NYISO respectfully requests that these comments be treated as timely because the Commission was closed on February 18 due to weather conditions in the Washington, D.C. area.

The NYISO continues to believe that the highly detailed governance rules set forth in the Notice of Proposed Rulemaking (“NOPR”) are unnecessarily prescriptive and inflexible. The Commission would better serve the industry if it confined itself to establishing key independence principles and allowed each ITP region to work out the details of its own governance. The NYISO is also still concerned that the NOPR would give stakeholders so much authority to choose and remove directors that ITPs’ independence would be compromised. Well-qualified candidates are unlikely to serve on ITP Boards if the selection process is overly intrusive and effectively forces them to engage in electioneering.

Nevertheless, the NYISO now believes that it is possible to develop governance rules that will both safeguard an ITP Board’s independence and address the issues raised by the Joint Petition’s opponents. The NYISO needs additional time to explore this possibility. The Commission should not take any action in the final rule that would preempt this reconsideration and force New York into a generic governance model.

More generally, the Commission should give considerable deference to governance proposals that existing ISOs (or RTOs) and their stakeholders submit in response to the final rule in this proceeding. The same deference should apply even if a region determines that the balance between ITP independence and accountability would be struck best by a system that gives stakeholder committees more filing authority, but less power to choose directors, than the NOPR contemplates.

Finally, the Commission should not require ITP Boards to have open meetings or allow stakeholders to bring issues directly to the Board. Although ITP Boards should have regular meetings with stakeholder representatives, as the NYISO Board currently does, opening all regular meetings to stakeholders would overwhelm Boards and reduce their efficiency.

Similarly, ITP staffs perform important functions for ITPs Boards and would be undermined if stakeholders were free to bypass them. ITP staffs have every incentive to keep their Boards well-informed, especially on disputed matters, since they are answerable for the consequences of failing to do so. There is thus no reason to preclude Boards from relying on ITP staff briefings and recommendations.

## **II. STATE PARTICIPATION**

The NYISO's *Initial Comments* explained that the Commission should not share its regulatory responsibilities with state Commissions but did not focus on the distinction between Multi-State Entities ("MSEs") and Regional State Advisory Councils ("RSACs"). The Commission has subsequently clarified its vision that states will form MSEs to coordinate their activities in state-jurisdictional areas, such as regional planning and adequacy, and that RSACs will perform Commission-jurisdictional functions using Commission-delegated authority.<sup>2</sup> In response, the NYISO wishes to clarify its own position.

State regulators are certainly entitled to coordinate their jurisdictional activities by voluntarily forming MSEs. Similarly, there is no reason why states should not form RSACs to provide advice on Commission-jurisdictional matters. Because state regulators play an important consumer protection role, and because Commission policies will necessarily affect state-jurisdictional policies, it is appropriate for the Commission to pay close attention to their views. States should, however, be limited to an advisory role in Commission-jurisdictional matters, such as overseeing ITPs. They should not be permitted to wield federal regulatory authority.

---

<sup>2</sup> See, e.g., *Letter from Chairman Pat Wood III to the Hon. Tom DeLay*, Appendix A at 14-15 (January 6, 2003).

Allowing states to exercise authority over an ITP's management and budget, market monitoring activities or allocation of congestion revenue rights would be bad policy because it would undermine ITP independence. State regulators generally have an explicit consumer protection mandate that can conflict with an ITP's mandate to administer efficient electricity markets. ITPs must balance the interests of all stakeholder sectors. States can have different agendas. States are also, appropriately, responsive to political forces that ITPs are expected to resist. If state regulators have power over ITPs or market monitoring units they will have every incentive to use it to influence them to favor state interests over the wholesale market's, or the Commission's policy objectives. The Commission is well aware of the harm that can result when market participants perceive that a market operator's independence is compromised by state regulators or politicians. It should not open the door to similar problems nation-wide. Furthermore, if neighboring RSACs were to require ITPs to adopt inconsistent policies, the result could be worsened seams and new impediments to interstate commerce.

In addition, the Commission cannot lawfully delegate its authority to state regulators. Commission precedent clearly establishes that decisions pertaining to wholesale electricity markets and transactions are subject to the Commission's "exclusive, nondelegable jurisdiction" and may not be shared with states. The Commission has stated that this doctrine:

[D]oes not mean that we are not sensitive to the concerns of state commissions. These concerns, if brought to our attention in a timely fashion, will be fully considered. However, while we are sensitive to state commission concerns, that does not mean that our role is simply that of automatic approval of state commission positions.<sup>3</sup>

---

<sup>3</sup> *TECO Power Services Corp. and Tampa Electric Co.*, 53 FERC ¶ 61,202 at 61,811 (1990) (refusing to share a Commission jurisdictional decision with the Florida Public Service Commission.) See also *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972); *Florida Power & Light Co., et al.*, 29 FERC ¶ 61,140 (1984); *Florida Power & Light Co.*, 40 FERC ¶ 61,045; *reh'g denied*, 41 FERC ¶ 61,153 (1987).

ITPs will be exclusively Commission-jurisdictional entities engaged in exclusively Commission-jurisdictional activities. The Commission must follow its precedent and may not delegate regulatory authority over them to RSACs. Compliance with the Federal Power Act requires that RSACs play a purely advisory role.

### **III. MARKET MONITORING UNIT STRUCTURE**

The NYISO urges the Commission to reject proposals that would require market monitoring units (“MMUs”) to have independent Boards of Directors distinct from an ITP Board.<sup>4</sup> Having two Boards charged with ensuring the efficiency of wholesale electricity markets in the same region would be redundant, inefficient and likely to lead to distracting conflicts over priorities and turf. There is nothing wrong with MMUs being independent of ITP management and they should always be “autonomous” from market participants. The ITP Board should, however, be the sole arbiter of market policy for its region, subject to the Commission’s ultimate review.

The Commission should also reject proposals that it directly assume responsibility for hiring and working with MMUs.<sup>5</sup> The Commission has already decided to supplement its own market monitoring staff with regional MMUs that will serve as its “eyes and ears” and “first line of defense” against market power abuses.<sup>6</sup> It has also determined that there is nothing inappropriate about independent MMUs having a close, and even contractual, relationship with

---

<sup>4</sup> See, e.g., *Comments of Mirant Americas, Inc. and Mirant Americas Energy Marketing, L.P.*, Docket No. RM01-12-000 at 53-54 (November 15, 2002).

<sup>5</sup> See, e.g., *Comments of the New York State Public Service Commission on the Standard Market Design Proposed Rulemaking*, Docket No. RM01-12-000 at 24 (November 15, 2002).

<sup>6</sup> See, e.g., *Communications with Commission-Approved Market Monitors*, 102 FERC ¶ 61,041 at P 10 (2003).

an ITP or RTO Board.<sup>7</sup> There is no reason to require that the market monitoring function be totally segregated from ITPs. Similarly, there is no reason why ITPs should not be allowed to have internal, non-autonomous, market monitoring staffs as well as an external MMUs, as was described in the NYISO's *Initial Comments*.<sup>8</sup>

#### **IV. OTHER ISSUES**

##### **A. Optimizing Transmission for Energy and Reserves and Self-Supply**

The New York Transmission Owners ("TOs") and the Long Island Power Authority ("LIPA") argue that the NYISO's current market design is inconsistent with the NOPR because it simultaneously "co-optimizes" transmission for energy and reserves instead of "optimizing" for them.<sup>9</sup> In LIPA's words, co-optimization "assumes that the transmission system is best used for the provision of energy and then optimizes the selection of energy and reserve resources using this assumption."<sup>10</sup> By contrast, under "full" optimization, "transmission can be loaded to move energy or can be backed down below maximum loading to allow energy from operating reserves to reach load when needed."<sup>11</sup>

The NYISO disagrees with LIPA's and the TOs' suggestion that P 234 of the NOPR should be read as requiring a full optimization of transmission for energy and reserves. Regardless of how the NOPR is to be construed, however, the final rule should not adopt an optimization requirement. Any potential benefits of enabling ITPs to set aside transmission for

---

<sup>7</sup> See *Midwest Independent Transmission System Operator, Inc.*, 101 FERC ¶ 61,228 at PP 10-12, 29 (2002).

<sup>8</sup> See *Initial Comments* at 78-80.

<sup>9</sup> See LIPA at 16-19; NY TOs at 17-20.

<sup>10</sup> LIPA at 17.

<sup>11</sup> *Id.*

reserves in abnormal situations when reserves are more valuable than energy, would be small and the development costs would be great. It is more practical to design ITP systems on the premise that energy will be more valuable than reserves, as economic theory dictates, and not build an optimization capability that would only be needed in extraordinary circumstances, if ever. The market power concerns that the TOs and LIPA fear will arise under co-optimization regimes can be more efficiently addressed through existing market power mitigation measures.

Finally, the Commission should not be concerned that the use of simultaneous co-optimization will make it more difficult to physically self-supply operating reserves across constraints. As the NYISO noted in its *Initial Comments*,<sup>12</sup> the sort of physical self-supply arrangements contemplated by Order No. 888, and discussed by the TOs and LIPA, are generally a poor fit for financially-based market designs like SMD. Financial self-supply arrangements are better suited to more advanced financially-based market designs and should meet market participants' needs once multi-settlement ancillary services markets are in place.

#### **B. Allocating Congestion Revenue Rights (“CRRs”)**

It appears that a majority of commenters share the NYISO's view that CRRs should not physically “follow” shifting loads. It also appears that a substantial minority, comprised mostly of commenters from regions unfamiliar with CRRs, disagrees. They believe that customers will suffer frequent curtailments, and the economic harm that results, if the NOPR's load-following proposal is not adopted. The Commission should nonetheless accept the arguments against physical load following that the NYISO and others have put forward. Stakeholders should be reassured that the absence of physical load following has not injured customers in the Northeast. Customers can be protected within the framework of a financially-based electricity market

---

<sup>12</sup> See *Initial Comments* at 49.

design if CRR auction revenues are credited to them through a local transmission-owning utility, as is currently done in New York. In no event should the Commission impose the “CRRs follow the load” rule in regions that have retail access. Doing so would force ITPs to solve a number of difficult implementation problems and would not bring any offsetting benefits.

Similarly, commenters appear to be evenly split between those that believe CRRs should never be auctioned and those, including the NYISO, that favor moving to auctions after a transition period. The Commission should not lose sight of the advantages that CRR auctions have over administrative allocation schemes. In addition, as with the physical load following proposal, it should remember that auctions have been successful in New York and should work in other regions.

### **C. Regional Transmission Planning Areas**

Several commenters argue that the New York – New England transmission planning area proposed in the NOPR should be expanded to include PJM and/or portions of the Upper Midwest.<sup>13</sup> They generally claim that the New York – New England area should be dropped because it is a vestige of the Joint Petition. The NYISO disagrees. New York and New England are a natural planning area for the reasons specified in the NYISO’s *Additional Comments*,<sup>14</sup> which were submitted after the Joint Petition was withdrawn. It also seems likely to be unfeasible to have a single planning process for a huge super-region spanning New York, New England the traditional PJM area, and regions like PJM West, PJM South and the Midwest ISO that are mostly electrically remote from New York – New England. It would be more

---

<sup>13</sup> See, e.g., *Additional Comments of the New York State Public Service Commission on the Standard Market Design Proposed Rulemaking*, Docket No. RM01-12-000 at 9-10 (January 31, 2003) (“NYPSC”).

<sup>14</sup> *Additional Comments of the New York Independent System Operator, Inc.*, Docket No. RM01-12-000 at 7 (January 10, 2003).



efficient to coordinate an integrated New York – New England planning process with the PJM process. This is particularly true given the NOPR’s ambitious timeframe for the commencement of regional planning.

#### **D. Allocating Energy Uplift Charges**

National Grid, U.S.A. (“Grid”) has argued that the Commission should clarify the proposed SMD tariff so that that energy uplift charges will be allocated to market participants based solely on their purchases in the energy market without reference to the load that they serve through bilateral transactions “outside” of spot markets.<sup>15</sup> For the reasons specified in the NYISO’s *Initial Comments*, the Commission should reject this suggestion and modify the NOPR’s proposal so that uplift charges are shared among participants that schedule bilateral transactions as well as both day-ahead and real-time spot market transactions. Bilateral transactions rely on the smooth functioning of the ITP’s market and scheduling systems just as much as spot market transactions. Moreover, even “self-scheduled” bilateral transactions impose uplift costs on the rest of the system because other generators have to be committed to manage congestion in order to allow them to flow. Finally, Grid’s proposal would give market participants an artificial incentive to engage in bilateral transactions. Although forward contracting is desirable, the Commission should rely on market forces to ensure that it occurs at efficient levels instead of adopting policies that would over-stimulate it.

#### **E. Long-Term Resource Adequacy**

The NYISO is encouraged that so many parties appear to share its concerns with various elements of the NOPR’s long-term resource adequacy proposal and to support the Northeastern

---

<sup>15</sup> See *Comments of National Grid, U.S.A.*, Docket No. RM01-12-000 at 57-59 (November 15, 2002).

ISOs' Resource Adequacy Model ("RAM") Group's efforts to create a regional alternative. The Commission should allow the RAM Group to design a resource adequacy system for the Northeast instead of imposing a less well-developed solution invented by any single stakeholder.

A number of commenters have asked the Commission to push the RAM Group in their own preferred policy direction. Some have submitted complete and highly detailed resource adequacy proposals. For example, Reliant Resources, Inc. generally supports the RAM Group but calls on FERC to allow LSEs to "self-arrange" their adequacy requirement without bidding into a centralized capacity auction and advocates a specific capacity market design.<sup>16</sup> Similarly, the New York State Public Service Commission ("NYPSC") backs many aspects of the RAM Group proposal but also backs a number of particular changes.<sup>17</sup> While many of the ideas advanced by these and other parties may be meritorious, it would be premature for the Commission to formally adopt any of them at this time. The better alternative would be to trust the RAM Group to consider all of these concepts and to let it formulate a consensus proposal for submission to the Commission. The Commission should give the RAM Group the time it needs to complete this work.

Finally, the NYPSC has argued that states have extremely broad jurisdiction over resource adequacy matters while the Commission has very little.<sup>18</sup> This goes too far. It is true that states have authority over the retail aspects of resource adequacy but this does not deprive the Commission of its exclusive jurisdiction over wholesale electricity markets. To the extent that centralized resource adequacy auctions or wholesale spot markets are established, it appears

---

<sup>16</sup> See *Comments of Reliant Resources, Inc.*, Docket No. RM01-12-000 at 7-11, 35-55 (January 10, 2003).

<sup>17</sup> See NYPSC at 14, n. 23, 26-37.

<sup>18</sup> *Id.* at 15-21.

that bids and other activities by LSEs within them would be Commission-jurisdictional even though other resource adequacy issues may be subject to state control. Similar reasoning led the Commission to assert jurisdiction over demand reduction bidding and other demand-side response programs administered by Independent System Operators, despite the arguable overlap with state jurisdiction.<sup>19</sup> The Commission also appears to have authority to condition participation in Commission-jurisdictional electricity markets on market participants' acceptance of resource adequacy rules that are necessary to ensure just and reasonable prices. In short, the Commission should be respectful of state concerns, and state authority, but it should still play a central role in resource adequacy matters.

---

<sup>19</sup> See, e.g., *Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States*, 95 FERC ¶ 61,225 at 61,771 (2001) (“to the extent the load reductions will be sold at wholesale, they fall under the Commission's jurisdiction.”); *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service into Markets Operated by the California Independent System Operator and the California Power Exchange*, 95 FERC ¶ 61,115 at 61,358 (2001) (asserting authority to require market participants to submit demand bids in wholesale markets and distinguishing state jurisdiction.)

**V. CONCLUSION**

WHEREFORE, for the foregoing reasons, the New York Independent System Operator, Inc., respectfully requests that the Commission adopt the recommendations set forth in these reply comments.

Respectfully submitted,

/s/ Ted J. Murphy

Counsel for

New York Independent System Operator, Inc.

Robert E. Fernandez, General Counsel and Secretary  
Mollie Lampi, Assistant General Counsel  
New York Independent System Operator, Inc.  
3890 Carman Road  
Schenectady, NY 12303

Arnold H. Quint  
Ted J. Murphy  
Hunton & Williams  
1900 K Street, NW, Suite 1200  
Washington, DC 20006

February 19, 2003

cc: Daniel L. Larcamp, Director Office of Markets, Tariffs and Rates, Room 8A-01,  
Tel. (202) 502-6700  
Alice M. Fernandez, Director Office of Markets, Tariffs and Rates -- East  
Division, Room 71-31, Tel. (202) 502-8284  
Robert E. Pease, Acting Director of Division of Enforcement, Office of Market  
Oversight and Enforcement, Room 52-41, Tel. (202) 502-8131  
Michael A. Bardee, Lead Counsel for Markets, Tariffs and Rates, Room 101-09,  
Tel. (202) 502-8068  
Stanley P. Wolf, Office of the General Counsel, Room 101-03,  
Tel. (202) 502-8891

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon each party designated on the official service list compiled by the Secretary in the above referenced docket, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 2010 (2002).

Dated at Washington, D.C. this 19<sup>h</sup> day of February, 2003.

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