

June 26, 2000

VIA FEDERAL EXPRESS

Hon. Richard J. Grossi
Chairman, New York Independent System
Operator Board of Directors
C/O William J. Museler
President and CEO
New York Independent System Operator, Inc.
3890 Carman Road
Schenectady, NY 12303

Re: Motion in Opposition of the Transmission Owners, LIPA and the Power
Authority of the State of New York to the Appeals to the NYISO Board
Regarding the Decision of the Management Committee to Adopt a Limited
and Temporary Bid Cap Measure

Dear Chairman Grossi:

Pursuant to the "Procedural Rules for Appeals to the ISO Board," the Transmission
Owners,¹ LIPA and the Power Authority of the State of New York² respectfully submit three copies
of a Motion in Opposition to the Appeals to the NYISO Board filed by: (1) Orion Power New York,
L.P.; (2) Hydro Quebec Energy Services (US) Inc.; and (3) Citizens Power Sales,

East Coast Power, LLC, Indeck Energy Services, Inc., KeySpan Ravenswood, Inc., Natural
Resources Defense Council, PG&E National Energy Group and Sithe Energies, Inc.

A copy of the Motion in Opposition has been transmitted by e-mail to Kristen Kranz, of the
NYISO's staff, who has agreed to serve it on each member of the Management Committee
today.

Sincerely,

Paul L. Gioia

Enclosures

cc: Kristen Kranz, via e-mail
DC 179412

¹ The Transmission Owners constitute all of the Members of the Transmission Owners Sector
of the NYISO Management Committee, which includes Central Hudson Gas & Electric
Corporation, Consolidated Edison Company of New York, Inc., New York State Electric & Gas
Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and
Rochester Gas and Electric Corporation.

² LIPA and the Power Authority of the State of New York are Members of the Public
Power/Environmental Sector of the NYISO Management Committee.

**MOTION IN OPPOSITION OF THE TRANSMISSION OWNERS,
LIPA AND THE POWER AUTHORITY OF THE STATE OF NEW YORK TO
THE APPEALS TO THE NYISO BOARD REGARDING THE DECISION OF THE
MANAGEMENT COMMITTEE TO ADOPT A LIMITED AND TEMPORARY
BID CAP MEASURE**

In accordance with Article 5 of the ISO Agreement and Sections 1.03 and 4.01 of the NYISO's Procedural Rules of Appeal, the Transmission Owners,¹ LIPA and the Power Authority of the State of New York² ("Electric Systems of New York State" or "Member Systems") file this motion in opposition to appeals to the New York Independent System Operator, Inc. ("NYISO") Board concerning the June 5, 2000 decision of the Management Committee to institute temporary bid caps on the NYISO energy and ancillary services markets. The Member Systems are comprised of the eight electric systems in the State of New York, which recently transferred operational control over significant portions of their transmission facilities to the NYISO and are the largest load serving entities ("LSE"s) in the New York control area. The Member Systems urge the NYISO Board to reject the requests to overturn the decision of the Management Committee.

I. Background

On June 5, 2000, the NYISO Management Committee approved, by a vote of 63%, a motion that the NYISO file as soon as possible with the Federal Energy Regulatory Commission ("Commission") for authority to impose temporary bid caps on the NYISO's energy and ancillary services markets until October 31, 2000.³ On June 15-16, 2000, notices of appeals of

¹ The Transmission Owners constitute all of the Members of the Transmission Owners Sector of the NYISO Management Committee. They include: Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., and Rochester Gas and Electric Corporation.

² LIPA and the Power Authority of the State of New York are Members of the Public Power/Environmental Sector of the NYISO Management Committee.

³ The bid caps approved by the Management Committee cap: 1) generator bids in the Day-Ahead and Real Time Energy markets at \$1,000 per MWh; 2) combined payments for availability and lost opportunity costs for 10-Minute and 30-Minute Reserves at \$1,000 per

this decision were filed with the NYISO Board of Directors, by: 1) Orion Power New York, L.P.; 2) Citizens Power Sales, East Coast Power, LLC, Indeck Energy Services, Inc., KeySpan Ravenswood, Inc., Natural Resources Defense Council, PG&E National Energy Group and Sithe Energies, Inc.; and 3) Hydro Quebec Energy Services (US) Inc. ("HQ"). These entities (collectively referred to as "Appellants") are among the parties that voted against the temporary bid caps.

In support of their filings, Appellants claim that concurrence by the ISO Board in the Management Committee's bid cap decision would be inconsistent with the NYISO's response to the Complaint filed by New York State Electric & Gas Corporation ("NYSEG"). Appellants also claim that the bid caps will harm the developing NYISO markets and will reduce system reliability. Appellants also request that, if the NYISO Board concurs in the Management Committee's bid cap proposal, the bid caps not be effective until approved by the Commission. Finally, Appellants oppose the suspension of the Bid Production Cost Guarantee ("BPCG") when the average LBMP exceeds \$200 per MWh or more per day.

The requested relief of the Appellants should be denied on several grounds. First, The bid caps were adopted by a significant majority of the Management Committee after a full discussion by the market participants of all relevant issues, and the Appellants have not provided sufficient justification for overturning that decision. Second, Appellants mischaracterize and improperly rely upon the NYISO's response to the NYSEG Complaint in opposing the limited bid cap measure adopted by the Management Committee. Third, the bid caps provide consumers with needed protection during the current summer capability period in light of the significant problems that have been experienced in the NYISO markets. Fourth, the lack of any

MWh; and 3) combined payments for availability and lost opportunity costs for regulation service at \$1,100 per MWh. BPCGs also are suspended for a supplier that bids minimum generation levels, start-up costs, or minimum run times when the Locational Based Marginal Price ("LBMP") at the supplier's bus averages \$200 per MWh or more per day. The total payments, including BPCGs may not exceed \$24,000 per MWh per day. Emergency External Payments are not subject to the caps.

significant price-sensitive load in New York State is further justification for the limited bid caps. Fifth, the bid caps are a reasonable response to current conditions in the NYISO markets. Finally, Appellants have not provided any reasonable basis for their contention that the bid caps will adversely affect reliability, either in the short-term or the long-term.

Contrary to the claims of the Appellants, the bid caps approved by the Management Committee are a limited and reasonable response by market participants, acting through the NYISO's Management Committee, to legitimate concerns with respect to significant problems that have affected the NYISO markets, and provides needed protection against unjustified prices that could be devastating both to consumers and load serving entities during the summer peak load period. Furthermore, it is vital that the Board reject Appellants' request to delay implementation of bid caps and act to implement bid caps immediately, as requested by the Management Committee.

II. Appellants Have Not Provided Adequate Justification For Overturning The Decision Of The Management Committee To Adopt A Limited And Temporary Bid Cap Measure

The Management Committee extensively debated, over several meetings, the adoption of bid caps. The proposal also was considered by the Bid Cap Task Force appointed by the Management Committee. All views for and against the bid cap proposal were articulated and carefully considered by the Management Committee. After full discussion, the Management Committee voted by a 63% majority to approve a limited and temporary bid cap measure. The bid caps received support from each of the five industry sectors represented on the Management Committee, and the overwhelming support of three sectors. The strong support of the market participants represented on the Management Committee should be given great weight by the NYISO Board. At a recent Liaison Committee Meeting, the NYISO Board advised the representatives of the Management Committee that it looked to the Management Committee to develop a plan to address problems in the NYISO markets during the summer capability period, and that it viewed the Management Committee's ability to address the difficult issues raised in that regard as a test of the NYISO governance process. The Management Committee has successfully met that test with its adoption of a limited bid cap measure, and the NYISO Board should not overturn that decision.

III. The NYISO's Response To The NYSEG Complaint Is Not Relevant To Its Consideration Of The Management Committee's Adoption Of A Limited And Temporary Bid Cap Measure.

The primary justification provided by the Appellants for the overturning of the Management Committee's adoption of bid caps is the NYISO Answer to the NYSEG Complaint, filed on April 24, 2000, which initiated the Commission's proceeding in Docket No. EL00-70-000 ("NYSEG Complaint"). However, such reliance is misplaced. The NYISO Answer was submitted in response to a vastly different proposal. In that case, NYSEG's primary proposal, subsequently withdrawn by NYSEG, was to suspend market-based prices and to impose pervasive cost-based bid caps. In contrast, the Management Committee action is much more

limited and would not interfere with market-based prices unless prices in the energy and ancillary services markets reach an extremely high level, i.e., \$1,000 per MWh. The NYISO's response to the NYSEG proposal, which it described as "drastic," is not relevant to the much more limited bid cap measure adopted by the Management Committee, and the Appellant's use of statements made by the NYISO in that proceeding are misleading and inapposite.

In addition, the NYISO criticized the NYSEG filing because there had been no collaborative stakeholder process to develop a reasoned and equitable proposal and the governance procedures had not been followed. According to the NYISO:

[A]lthough the NYISO's standard committee procedures require time for differing views to be fully aired and discussed, and thus may not move as quickly as NYSEG would like, that is not sufficient justification for the April 24th Complaint's proposal to bypass those procedures entirely. The NYISO's committees are well aware of the problems that have been encountered thus far. They have been, and will continue to be, heavily involved in developing solutions and may propose additional remedies if they believe them to be necessary.⁴

The Management Committee's action, therefore, is precisely what the NYISO contemplated in its Answer. The bid cap measure adopted by the Management Committee was developed in accordance with the governance procedures in the ISO Agreement and was approved by a vote of 63% of the NYISO's market participants after a full discussion and consideration of differing views. The NYISO Answer to the NYSEG Complaint expresses a clear preference for measures developed among market participants pursuant to NYISO governance procedures. The Management Committee's bid cap decision is just such a measure.

IV. The Limited Bid Cap Measure Adopted By The Management Committee Provides Consumers Needed Protection For The Summer Capability Period.

Notwithstanding efforts by the NYISO, concerns about the operation of the NYISO

⁴ NYISO Corrected Answer, Docket Nos. EL-00-70-000 and EL00-67-000 (May 31, 2000) ("NYISO Corrected Answer") at 11 (emphasis added).

markets have not been dispelled. The Board of Directors of the NYISO recently approved the refiling of the TEPs, with the strong support of the Management Committee.⁵ In justifying the continued need for this authority, the NYISO explained that:

Since the start-up of the ISO administered markets, additional software flaws and anomalies have been identified and remedied. Other problems have been identified and are being analyzed and remedied, as necessary....Other anomalies are likely to surface which will require investigation and potential remediation.⁶

The NYISO has confirmed that it continues "to experience a number of anomalies" and has "recognized design flaws," requiring the use and continuation of its TEP authority.⁷

The Commission recognized that market design flaws and implementation errors had a major impact on prices and imposed a prospective bid cap and other prospective changes with respect to the NYISO operating reserve market for 10-minute non-spinning reserves.⁸

As the NYISO stated in its Answer, "it is impossible for the NYISO to guarantee that its markets will be completely free of market flaws or market power abuses."⁹ The Management Committee's action will provide limited but reasonable protection for consumers against extremely high prices that may result from existing or potential problems in the NYISO markets during the summer peak period.

The NYISO's authority to impose prospective market power mitigation measures will not

⁵ New York Independent System Operator, Inc., Extension of Temporary Extraordinary Procedures, Docket No. ER00-2624-000 (May 26, 2000), transmittal letter at 7.

⁶ New York Independent System Operator, Inc., Extension of Temporary Extraordinary Procedures, Docket No. ER00-2624-000, transmittal letter at 3.

⁷ New York Independent System Operator, Inc., Extension of Temporary Extraordinary Procedures, Docket No. ER00-2624-000, transmittal letter at 1.

⁸ New York Independent System Operator, Inc., et al., Order on Tariff Filing and Complaints at 19 (May 31, 2000) ("May 31 Order").

⁹ NYISO Corrected Answer at 26.

provide adequate protection to consumers this summer. While market power mitigation is important, it is an extremely limited tool that can be used only in limited circumstances (i.e. when the exercise of market power can be demonstrated) and any remedy imposed is prospective. The NYISO's TEP authority, while helpful, also does not provide adequate protection. Recent experience has demonstrated that the TEP authority is not effective in protecting against a large number of unjustified prices that arise from a series of market design flaws, which the NYISO is still in the process of identifying and addressing.

Furthermore, and contrary to the contentions of the Appellants, market participants can not adequately protect themselves against unwarranted high prices through hedging. Given the current nature of the electricity market (i.e., no significant ability to store electricity or change demand in response to prices) load can never be hedged completely. There always will be volume uncertainty and price risk at the margin. When prices rise to extraordinary levels, this risk can be very substantial and LSE's have not been able to secure hedges for balancing market transactions. In addition, the current NYISO markets have experienced the unjustified curtailment of export and import transactions, forcing parties to purchase electricity in the real time market at very high prices.

Appellants' contention, therefore, that the Management Committee's action does not protect prudent LSE's who hedged their transactions and subsidizes LSE's who have failed to take advantage of available hedges, is unfounded. The best proof of this is the universal support by LSE's and end use consumers for the limited bid cap measure.

V. The Lack Of Price Sensitive Load In New York State Provides Added Justification For The Bid Cap Measure Adopted By The Management Committee.

The Appellants, while discussing the importance of correct price signals, fail to mention that the NYISO market structure assumes that load will be able to respond to price signals. Given current metering limitations, very few consumers "see" real time prices and, thus, cannot reduce their consumption in response to high prices. This inability to react to high prices is not present in other competitive markets for commodities. In the absence of the price sensitive load, the

ability of the NYISO markets to establish reasonable prices is severely hindered and prices can rise to excessive levels, especially during the summer peak load period. Without price sensitive load, the only way to bring supply and demand into proper balance is by adding supply, which takes years. The absence of price sensitive load in New York State creates an imminent risk of harm to consumers from unjustified and excessive prices that would provide windfalls to suppliers. These excessively high prices may increase supplier profits in the short-run, but will cause significant economic harm to consumers. They also will undermine confidence in the NYISO markets and may invite political and regulatory responses that could be very damaging in the long-term to the competitive markets that have been developed in New York State. While the NYISO staff and the NYISO committees are attempting to advance the development of price sensitive load, it is clear that New York consumers will be vulnerable to extremely high and unjustified prices this summer, and are entitled to the limited protection afforded by the bid caps adopted by the Management Committee.

VI. The Bid Cap Measure Adopted By The Management Committee Is A Reasonable Response To Current Conditions In The NYISO Markets.

The Management Committee's bid cap decision was based on its conviction that limited and reasonable protection of consumers is needed given the current state of the NYISO administered markets, as evidenced, in part, by the pending complaint proceedings concerning the operating reserves, energy and ancillary services markets, as well as the current lack of any significant price sensitive load in New York State. The bid caps will not interfere with market prices below the \$1,000/MWh level, which is very far above normal market clearing prices and the same level of bid cap that has been in effect in the PJM markets.

It also is important to note that the bid caps adopted by the Management Committees are temporary, with a specific expiration date of October 31, 2000. In addition, given the high level of the bid cap, relatively few hours of the capability period will be affected.

The limited and temporary bid cap measure adopted by the Management Committee balances the importance of continuing to allow the NYISO markets to operate on the basis of

competitive prices, with the clear need to provide minimal protection to consumers against unjustified and excessive prices that may result from uncorrected market design flaws or the inability of load to respond to, and protect itself against, high prices. The Appellants have not provided sufficient justification for upsetting the balance achieved by the Management Committee.

VII. The Bid Caps Will Not Adversely Affect The NYISO Markets Or System Reliability.

Appellants assert that the bid caps adopted by the Management Committee will harm NYISO markets and impair reliability. Under the limited bid cap mechanism, however, market prices will remain in effect below the bid cap level.¹⁰ The bid cap level is sufficiently high so that generators will not be discouraged from selling into the NYISO markets. In addition, if generation resources are needed, the NYISO can recall sales from ICAP providers,¹¹ and can make emergency purchases above the bid cap limitation. This flexibility, inherent in the limited Management Committee bid cap plan, provides additional protections to consumers in the event that unanticipated supply shortages arise.

Furthermore, it is unreasonable to suggest that the bid cap measure will adversely affect the construction of new generation in New York State. As noted above, the bid caps are a temporary measure, and a limited and reasonable response to problems that have occurred in the newly established NYISO markets. Parties interested in constructing generation in New York State are well aware of these circumstances. In addition, the level of the bid caps is far above the prices needed for generation to operate profitably in New York State. It is interesting that the

¹⁰ Prices below the bid cap will be subject to reservation and correction, as appropriate under the TEPs, and the NYISO's market power monitoring and mitigation authority. As noted above, however, erroneous prices produced by market flaws and a lack of demand response render those tools alone inadequate to protect against erroneous prices.

¹¹ The statewide ICAP requirement, which is set at 18 % above peak load, ensures that sufficient capacity is committed for the NYISO.

Appellants do not suggest that the \$1,000 bid cap in PJM has resulted in a lack of interest in the construction of new generation in that market. There is no reasonable basis, therefore, for concluding that the limited and temporary bid cap measure adopted by the Management Committee will have an adverse effect on long-term decisions to construct generation in New York State.

Appellants also complain that when they sold ICAP or purchased TCCs in the NYISO markets they were not aware that bid caps would be adopted. They speculate that, had they known bid caps would be adopted, this might have affected some of their decisions in their ICAP sales and TCC purchases. This contention fails to acknowledge that there are risks in participating in any market. There were no assurances that the imposition of bid caps might not be necessary in the NYISO markets, as had been done in other markets including PJM, especially during the NYISO's initial operating period. Furthermore, it is not reasonable to assume that participants in the ICAP and TCC markets reasonably relied upon energy prices in excess of \$1,000 per MWh.

Similarly, Appellants have not demonstrated that the limited suspension of BPCG payments will have adverse consequences in the NYISO markets. The measure adopted by the Management Committee limits total payments, including BPCGs, to \$24,000/MW per day. It further provides that BPCGs will be suspended for a supplier which bids minimum generation levels, start-up costs, or minimum run times when LBMP at the supplier's bus averages \$200/MWh or more per day. These provisions were included in the bid cap measure so that generators, needed for reliability purposes, would not be able to evade the bid cap by submitting bids with very high minimum generation, start-up costs or minimum run time requirements.

Orion Power contends that the BPCG suspension provision may penalize a gas turbine generator with high operating costs. Orion, however, has failed to support this contention. The BPCG would be suspended only when the suppliers' LBMP averages \$200/MWh or more per day. This is an extraordinarily high average LBMP for a full day and would require extremely high prices during the peak load hours. Orion has not provided adequate support for its

contention that it would be adversely affected by the suspension of the BPCG under such circumstances and with such high prices over a 24 hour period. Furthermore, published data suggests that gas turbine generators will be able to operate without sustaining losses under the limited BPCG suspension provision.¹² If the Appellants have additional information to support their contention that the limited BPCG should be modified, that information should be provided to the Management Committee for its consideration.

VIII. The Bid Caps Approved By The Management Committee Should Be Implemented As Soon As Possible.

Appellants argue that the Management Committee's bid cap decision should not be implemented until approved by the Commission. The Management Committee, however, clearly intended that the bid caps would go into place as quickly as possible and would be in effect during the current summer capability period. Failure to take all steps necessary for the immediate implementation of bid caps would constitute, as a practical matter, a veto by the NYISO Board of the Management Committee decision. In order to effectuate the intent of the Management Committee, the NYISO Board must make an immediate filing with the Commission requesting waiver of the Commission's prior notice requirements, and implement the price caps effective no later than June 5, 2000.

IX. Conclusion

The Member Systems respectfully urge the NYISO Board to take action consistent with the comments provided herein. Specifically, the Member Systems request: 1) that the NYISO Board approve the decision of the Management Committee to adopt temporary bid caps in the NYISO energy and ancillary services markets through the NYISO's first summer capability

¹² For example, the New York Power Pool's "Yellow Book" as well as filings with the New York PSC and FERC indicate that the annual production costs for the Gowanus and Narrows gas turbine generations averaged from \$126 to \$180/MWh and \$59 and \$116/MWh, respectively, from 1993 through 1999. Despite recent increases in oil prices, these numbers indicate that gas turbine generators could operate under the limited BPCG suspension provision without incurring losses.

period; and 2) that the NYISO Board file with Commission and immediately implement the bid caps approved by the Management Committee in order to provide consumers with needed protection during the current summer capability period.