NEW CAPACITY ZONES MARKET MITIGATION MEASURES

Comments of the Indicated New York Transmission Owners[1]

May 7, 2012

Introduction

On April 16, 2012, the New York Independent System Operator ("NYISO") outlined its planned approach to market mitigation measures in new capacity zones. A related compliance filing is due to be submitted to the Commission no later than June 30, 2012.

In general, the NYISO stated that all new capacity zones would be subject to both supply-side and buy-side mitigation procedures comparable to those currently in effect in New York City. The NYISO also sought input on whether an ICAP Supplier subject to an Offer Floor in two Mitigated Capacity Zones should be subject to the higher of the Offer Floors. The Indicated New York Transmission Owners offer comments on this issue and comments on additional aspects of the NYISO's proposed mitigation measures for new capacity zones.

Pivotal Supplier Definition

In New York City, the NYISO currently applies supply-side mitigation measures only to suppliers that are pivotal – i.e., suppliers that control at least 500 MW of capacity. We do not believe that this threshold should be carried over to new capacity zones in its current form.

A supplier's incentive to economically or physically withhold capacity depends upon the structure of the relevant capacity market and projected market conditions. Depending upon the slope of the demand curve, a supplier may gain large amounts of revenue, modest amounts of revenue, or no revenue at all by withholding capacity. Additionally, if there is a surplus of generation in the market, the supplier may have a greater incentive to withhold capacity, because the revenue the supplier that it would otherwise earn from its withheld capacity is relatively small. By contrast, if supplies are relatively scarce, the revenues lost on withheld capacity are higher.

For this reason, the Indicated NYTOs recommend that the NYISO periodically review the appropriate exemption threshold for supply-side mitigation in new capacity zones, to ensure that entities that have a financial incentive to withhold capacity are not exempted from mitigation, rather than applying the 500 MW threshold in all new zones and under all market conditions. A detailed proposal accompanies these comments.

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[1] Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Long Island Power Authority, New York Power Authority, Niagara Mohawk Power Corporation d/b/a National Grid, and Orange and Rockland Utilities, Inc. (referred to herein as the "Indicated New York Transmission Owners" or "Indicated NYTOs").

The NYISO proposal would also exempt suppliers bidding in a new capacity zone from mitigation whenever some portion of their capacity is not needed to meet the minimum capacity requirement for that new capacity zone. Depending the slope of the applicable demand curve and current market conditions, such suppliers may have an incentive to withhold capacity, regardless of whether all of their capacity is needed to meet requirements. The NYISO should not apply this exemption to new capacity zones.

Buy-side Mitigation Minimum Size

In New York City, suppliers are exempt from supply-side mitigation if they control less than 500 MW of capacity, but no comparable minimum size must be exceeded to trigger the application of buy-side mitigation measures. The NYTOs believe that such an exemption should be provided.

Like existing suppliers, Load-serving Entities ("LSEs") and new entrants with a small market presence do not necessarily have a meaningful incentive to bid their capacity at a level different from their marginal costs. Moreover, any such incentive likely varies depending on the slope of the applicable demand curve(s) and market conditions.

The Indicated NYTOs believe that the NYISO should apply the same minimum size threshold to the application of buy-side mitigation in new capacity zones as it does for supply-side mitigation. If the NYISO periodically reviews and updates the minimum size threshold applicable to supply-side mitigation, as discussed above, it should also periodically determine appropriate minimum size thresholds for buy-side mitigation, based on the applicable demand curve and current market conditions.

If the NYISO opts to exempt all suppliers controlling less than 500 MW of capacity from supply-side mitigation, it should also exempt new entrants with less than 500 MW of supply from buy-side mitigation. This would assure that the rules governing buy-side mitigation are comparable to those governing supply-side mitigation.

The Indicated NYTOs also urge the NYISO to exempt renewable generation and demand response from buy-side mitigation in new capacity zones. Renewable generation development is not driven by the same economic considerations as other forms of new entry. With respect to demand response, the NYISO has contended that new entry costs cannot be estimated with a reasonable degree of accuracy. PJM exempts renewables and demand response from buy-side mitigation.

Buy-side Mitigation for Suppliers Located in Multiple Zones

When a new entrant is located in two capacity zones (i.e., a supplier located in both a larger capacity zone and a smaller capacity zone contained within the larger capacity zone) and is not exempt from buy-side mitigation, the NYISO proposes to apply the higher of the two potential default offer floors that would be calculated for the two capacity zones to the supplier's bids. We are concerned that this proposal will result in inefficient market outcomes and may, in some cases, endanger reliability. As an alternative, the NYISO should consider applying a separate default offer floor in each market.

If the default offer floor calculated by the NYISO is lower within the smaller capacity zone than in the remainder of the larger zone, the NYISO's proposal would effectively increase the default offer floor for new entrants located in the smaller zone, potentially to levels higher than the cost of new entry for the smaller zone.[2] As a result, new supplies could be prevented from clearing the market for the smaller zone even when the smaller zone is at or below its minimum requirement. This result would conflict with one goal of the NYISO's buy-side mitigation procedure, which is to ensure that when a capacity zone is at or near its minimum requirement, new entrants will not be precluded from selling their capacity in that capacity zone.[3] Accordingly, the default offer floor for resources in a smaller capacity zone contained within a larger capacity zone should be based on the default offer floor for the smaller capacity zone, even if it is below the default offer floor for the larger capacity zone.

In cases where the default offer floor is higher within the smaller zone than in the remainder of the larger zone, the NYISO should allow suppliers in the smaller capacity zone that are unable to sell their capacity in the smaller capacity zone as a result of an offer floor to bid their capacity within the larger capacity zone, subject to the default offer floor for the larger capacity zone. Allowing such bids will not depress market prices significantly below net CONE, because the capacity will not clear if prices are higher than 75% of the Mitigation Net CONE for the larger capacity zone, a level which the Commission has found is not significantly below net CONE. Moreover, applying the lower default offer floor for the larger capacity zone would recognize that capacity located within the smaller zone provides the same reliability benefit to the larger zone as capacity located elsewhere in the larger zone.

[2] Based on the estimated cost of new entry included in the NYISO's December 13, 2010 presentation to the ICAPWG entitled "LHV Sensitivity Scenarios," the Mitigation Net CONE for a Southeast New York capacity zone could be approximately $15.52 per kw (slide 8), while the cost of new entry for Long Island is approximately $9.71 per kw (slide 7). The default offer floor for Long Island would effectively be 75% of the former figure or $11.64 per kw, which exceeds the cost of new entry for Long Island.

[3] See, e.g., 122 FERC ¶ 61,211, p. 107: "While commenters raise an issue with the floor being set at seventy-five percent of net CONE rather than at a higher level, such as one hundred percent of net CONE, as Astoria suggests, the Commission agrees with NYISO that its proposed seventy-five percent level of mitigation serves two purposes. It deters uneconomic entry but is not so high as to deter economic entry."