112 FERC ¶61,004
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

New York Independent System Operator, Inc. Docket No. ER05-941-000

ORDER ACCEPTING IN PART AND REJECTING IN PART TARIFF SHEETS

(Issued July 1, 2005)

1. On May 5, 2005, the New York Independent System Operator, Inc. (NYISO) filed to revise its Open Access Transmission Tariff (OATT) and Market Administration and Control Area Services Tariff (Services Tariff) to allow an additional form of collateral and to reduce the amount of collateral required in the Virtual Transactions market. For the reasons discussed below, we will conditionally accept in part and reject in part NYISO's proposed revisions, to become effective July 5, 2005. This order benefits customers by reducing undue barriers to participation in the virtual market while also balancing the need to adequately protect the market from loss.

Background

2. On September 4, 2001, NYISO filed tariff revisions in Docket No. ER01-3009-000 to implement bidding of non-physical, *i.e.*, financial-only, supply and demand (Virtual Transactions). Virtual Transactions allow market participants to bid non-physical generation and load into the Day-Ahead Market and settle those bids in the Real-Time Market. NYISO states that its original Virtual Transactions filing included credit policies, which provided that cash and letters of credit were the only acceptable forms of collateral for Virtual Transactions. Additionally, those credit policies proposed that fourteen days of collateral be posted as a condition to engaging in Virtual Transactions.

3. On October 25, 2001, the Commission conditionally accepted NYISO's original Virtual Transactions proposal, approving the two forms of acceptable collateral (cash and letters of credit), but ordering that the amount of collateral be reduced from fourteen days to seven days.[1]

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[1] *New York Independent System Operator, Inc.*, 97 FERC ¶ 61,091 at 61,474 (2001), *reh'g denied*, 98 FERC ¶ 61,077 (2002) (approving NYISO's proposed credit

(continued)

4. In the instant filing, submitted on May 5, 2005, NYISO filed to revise its OATT and Services Tariff to allow an additional form of collateral and to reduce the amount of collateral required. Specifically, NYISO proposes to (i) allow netting of amounts receivable as an additional acceptable form of collateral, and (ii) reduce the collateral requirement necessary to participate in Virtual Transactions from seven days to four days.

5. NYISO states that the proposed tariff revisions were approved by unanimous vote at the February 2, 2005 Management Committee meeting, and that NYISO's Board of Directors approved the amendments on April 18, 2005.

Notice, Interventions, and Protest

6. Notice of NYISO's filing was published in the *Federal Register*, 70 Fed. Reg. 28,933 (2005), with interventions or protests due on or before May 26, 2005. The New York Transmission Owners filed a timely motion to intervene.[2] Edison Mission Energy and Edison Mission Marketing & Trading, Inc., Dynegy Power Marketing, Inc. and Dynegy Northeast Generation, Inc., and the New York State Public Service Commission filed timely motions to intervene and a notice of intervention, respectively, and comments in support of NYISO's filing.

7. On May 26, 2005 EPIC Merchant Energy LP (EPIC) filed a motion to intervene and protest. EPIC argues that consistent with recent Commission precedent[3] and policies in neighboring independent system operators (ISO) and regional transmission organizations (RTO) (*e.g.*, PJM Interconnection L.L.C. (PJM) and Midwest Independent Transmission System Operator, Inc. (Midwest ISO)), NYISO should be directed to either establish a one-day collateral requirement, or establish a two-day requirement with a directive that a one-day requirement be studied. EPIC also argues that NYISO should be

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policies, subject to conditions, "as an interim measure until operation of the virtual market produces sufficient information to judge the appropriateness of these policies").

[2] The New York Transmission Owners consist of Central Hudson Gas & Electric Corp., Consolidated Edison Company of New York, Inc., LIPA, New York Power Authority, New York State Electric & Gas Corp., Rochester Gas and Electric Corp., Orange and Rockland Utilities, Inc., and Niagara Mohawk Power Corp., a National Grid Company.

[3] *PJM Interconnection L.L.C.*, 104 FERC ¶ 61,309 at P 24 (2003) (*PJM*); *Midwest Independent Transmission System Operator, Inc.*, 108 FERC ¶ 61,163 at P 257 (2004) (*Midwest ISO*).

directed to either change its reliance on a reference price based on the 97th percentile of the highest price experienced in the market over a three-month period or to study such a change.[4]

Discussion

A. Procedural Matters

8. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2004), the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

B. Analysis

9. NYISO's proposed tariff change includes allowing "any amount receivable to the Customer …" as an additional appropriate form of collateral (commonly referred to as "netting") for Virtual Transactions. Thus, amounts that the NYISO owes to a market participant now can be used to satisfy the market participant's collateral requirements. NYISO argues that this is an acceptable form of collateral because it represents money already in NYISO's possession to be paid to a market participant. As such, NYISO would withhold payment from the market participant in the event a market participant is in default and NYISO needs to "draw" on that collateral. NYISO states that it currently allows netting as a form of collateral in other markets it administers, and market participants have expressed their support with a unanimous vote approving this proposal.

10. We find that allowing amounts receivable to be used as collateral is appropriate here for the reasons noted above and is consistent with prior Commission policy on netting current obligations across the NYISO markets.[5] The Commission thus accepts NYISO's proposal to allow amounts receivable as an acceptable form of collateral for Virtual Transactions.

11. NYISO's tariffs currently require seven days collateral be posted as a requirement to participate in Virtual Transactions. The proposed change will reduce that requirement to four days. NYISO states that it currently has over three years of experience with administration of Virtual Transactions during which the NYISO has not had to terminate a Virtual Transactions Customer. Based on this experience, NYISO supports the

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[4] EPIC's Protest at 8 n.9.

[5] *See New York Independent System Operator, Inc.*, 104 FERC ¶ 61,311 at P 51-52 (2003), *clarification granted*, 105 FERC ¶ 61,340 at P 17 (2003). In those orders the Commission determined that although FTRs may bring in future revenues, those future monies were not guaranteed, and therefore could not be netted.

proposed reduction as a reasonable compromise that balances the need to adequately protect the market from loss with reducing undue barriers to participation. NYISO states that market participants' unanimous vote approving the proposal expresses their support for the collateral reduction.

12. EPIC argues that NYISO's proposed reduction to a four-day collateral requirement contradicts Commission precedent, does not go far enough in that four days still far exceed what is needed to protect against realistic market risk, and does not go far enough in that four days still far exceed the credit requirements imposed on virtual transactions in other ISOs and RTOs.

13. We agree with EPIC that NYISO has not justified its proposal to reduce the collateral requirement to four days, rather than two days or even one day, for Virtual Transactions. In general, virtual trading provides benefits to the market by increasing liquidity and price convergence between the Day-Ahead and Real-Time Markets. Although the NYISO markets currently use a seven-day collateral window for Virtual Transactions, we note that this provision was granted as an "interim measure" only, and it was expected that the collateral requirements would decrease over time.[6] We find, as we did similarly for PJM and Midwest ISO,[7] that NYISO's requirement for collateral equal to the total bid (in MWh times the 97 percentile price differential) times four (for four days) is excessive. NYISO will know at the close of the day ahead bidding which of the virtual bids has cleared and must remain collateralized and which bids are no longer valid and do not present further credit risk. At the end of the second day, NYISO will know the actual settlement amount of the previous days' cleared bids. Thus, NYISO's exposure for uncleared bids is a single day and for cleared bids a second day.

14. To facilitate Virtual Transactions, we direct NYISO to adopt a two-day Virtual Transactions collateral window, through a compliance filing, consistent with our directions to PJM and Midwest ISO.

15. Furthermore, after each operating day, the NYISO should know which bids were accepted and which were not. Therefore, we direct the NYISO to study, with stakeholder

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[6] *New York Independent System Operator, Inc.*, 97 FERC ¶ 61,091 at 61,474 (2001), *reh'g denied*, 98 FERC ¶ 61,077 (2002).

[7] *PJM*, 104 FERC ¶ 61,309 at P 23-24 (rejecting a proposed four-day collateral requirement); *Midwest ISO*, 108 FERC ¶ 61,163 at P 447-48 (rejecting a proposed six-day collateral requirement).

involvement, the feasibility of moving to a one-day Virtual Transactions collateral window and report the results of this analysis to the Commission within 180 days.[8]

16. EPIC further argues that NYISO uses a reference price that is artificially high. EPIC states that, under the existing and proposed NYISO tariffs, the assumed market clearing price from financial trading is presumed to be the 97th percentile of the highest actual price experienced in the market, over a three month period. EPIC argues that this is an extreme, unrealistic, and unjustified market clearing price. Accordingly, EPIC argues that, as the Commission required for Midwest ISO, NYISO should be directed to reconsider, or change, its reliance on a reference price based on a 97th percentile calculation.

17. We share EPIC's concerns regarding the use of a reference price based on a 97th percentile calculation for Virtual Transactions. Therefore, we direct the NYISO to submit a compliance filing, within 30 days of the date of issuance of this order, justifying an assumed market clearing price of 97 percent of the highest actual price experienced in the market for Virtual Transactions, consistent with our directions to the Midwest ISO.[9]

<u>The Commission orders</u>:

(A) The proposed tariff revisions of NYISO are hereby conditionally accepted in part and rejected in part, as discussed in the body of this order, to become effective July 5, 2005.

(B) NYISO is hereby required to make a compliance filing as described in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

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[8] *See supra* note 7.

[9] *Midwest Independent Transmission System Operator, Inc.*, 109 FERC ¶ 61,285 at P 377 (2004) (requiring justification of a 97th percentile calculation).