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March 7, 2003

VIA HAND DELIVERY

Richard J. Grossi
Chairman
New York Independent System Operator
3890 Carman Road
Schenectady, NY 12303

c/o William J. Museler
President and Chief Executive Officer
New York Independent System Operator
3890 Carman Road
Schenectady, NY 12303

RE: Motion in Opposition to Appeals

Dear Chairman Grossi:

Pursuant to the Procedural Rules for Appeals to the ISO Board, KeySpan-Generation LLC ("KeySpan") respectfully submits three copies of a motion in opposition to the various appeals to the NYISO Board of Directors ("Board") of the Management Committee's approval of the Demand Curve. A copy of this motion has been electronically transmitted to NYISO Staff.

In addition, KeySpan respectfully requests the opportunity to present oral arguments to the Board.

Sincerely,

James M. D'Andrea

James M. D'Andrea
Attorney for KeySpan-Generation LLC

**KEYSPAN-RAVENSWOOD, LLC MOTION IN OPPOSITION
TO VARIOUS APPEALS TO THE NYISO BOARD OF DIRECTORS
OF THE MANAGEMENT COMMITTEE'S APPROVAL OF THE
DEMAND CURVE AT ITS FEBRUARY 13, 2003 MEETING**

I. SUMMARY STATEMENT

KeySpan-Ravenswood, LLC (“KeySpan”) files this motion in opposition to the various Appeals¹ to the NYISO Board of Directors (“Board”) of the Management Committee’s approval of the Demand Curve at its February 13, 2003 meeting. KeySpan respectfully requests the Board deny the Appeals and file a section 205 petition with the Federal Energy Regulatory Commission (“FERC”) as soon as possible, but no later than March 21, 2003, requesting approval of the demand curve as of April 1, 2003, such that it could be implemented for the May 2003 spot market auction. The Board should request FERC waive its 60 day notice period and issue an order by April 23, 2003.

II. ARGUMENTS

A. THE DEMAND CURVE WILL REDUCE VOLATILITY

The Demand Curve will reduce the volatility that exists in the NYISO capacity market today. The current NYISO market design for capacity results in boom/bust cycles. When there is a small deficiency in reliability from the administratively determined level, prices spike to the administratively determined deficiency price cap. Conversely, when reliability needs are met and additional resources provide improved reliability, prices plummet. This is well documented in a New York State Department of Public Service (“DPS”) staff paper by its Chief of Regulatory Economics, Mr. Mark Reeder.² The Reeder Analysis and the boom/bust cycle was discussed at various NYISO meetings,

¹ Appeals were filed by Multiple Intervenors (“MI”); the City of New York and Consumer Power Advocates (collectively “City of New York”); New York State Electric & Gas Corp. and Rochester Gas and Electric Corp. (collectively “NYSEG”); Agway Energy Services, Inc., ECONergy Energy Company, Inc. and Mirabito Gas & Electric, Inc. (collectively “Non-Voting Members”); Strategic Energy, L.L.C. (“Strategic”); Select Energy, Inc. on behalf of Select Energy New York, Inc. (“Select Energy”); and Strategic Power Management, Inc. (“SPM”).

² See Generally, Mark Reeder, *Government Intervention Into Wholesale Electric Markets To Assure Generation Adequacy* (November 6, 2002) (hereinafter, “Reeder Analysis”).

including but not limited to ICAP Working Group meetings, as well as during a FERC Standard Market Design technical conference.

Although volatile prices are part of competitive markets, volatility is not always acceptable to market participants. Accordingly, the NYISO capacity market is subject to several administratively determined price caps. The same is true for the energy and ancillary service markets. Although these price caps do not eliminate upside volatility, they limit it to a great extent. Various bid caps also exist in the energy, capacity and ancillary service markets that limit upside volatility. However, there are no corresponding limits to potential precipitous price drops or downside volatility. Therefore, contrary to MI's claim that the capacity market is priced based on supply and demand and working as designed,³ the capacity market, as well as all other markets, are subject to administrative price caps and not providing a market based signal that additional capacity is beneficial. Similarly, NYSEG's claim that the demand curve is administrative price setting⁴ ignores the fact that the current market is subject to administratively set price caps and that the NYISO will continue to conduct various capacity auctions. The imbalance in capacity market volatility (i.e. the fact that upside volatility is limited and downside is not) is addressed by the Demand Curve. The Demand Curve strikes a balance because it further limits upside volatility and introduces downside volatility limits; it addresses the boom/bust cycle discussed in the Reeder Analysis. This is only one of the issues the demand curve remedies.

As discussed in the sections below, reduced volatility will improve reliability, create more efficient price signals, and help the development of a long term bilateral market, which is consistent with SMD and neighboring control areas goals. KeySpan thinks such a reduction in volatility and the noted improvements are important to the market and should be implemented as soon as possible.

³ MI at 3.

⁴ NYSEG at 2.

B. THE DEMAND CURVE WILL IMPROVE RELIABILITY

The Demand Curve will improve reliability because, it will encourage investments in supply that increase reliability above the administratively established minimum reliability requirement, and it does not rely on short term reliability deficiencies to ensure long term resource adequacy.

The current capacity market design requires a deficiency in reliability to occur before additional supply is considered to add value to the market. This is because construction of additional supply resources ahead of demand will result in reliability levels above the administratively determined level and market prices will plummet. Accordingly, suppliers are encouraged to develop only those resources required to meet the administratively determined minimum levels or less, and no more. The result is that periods of reliability shortages are inevitable. KeySpan does not think maintaining reliability and adequate resources in the long run should be dependent on reliability deficiencies and associated price spikes in the short run. This ensures periods of inadequate reliability will occur.

Moreover, as discussed above, if prices are capped to limit volatility on the upside but the downside risk remains volatile, suppliers of capacity discount even the potential of deficiency pricing in the current market. Suppliers contemplating development discount expected capacity revenues significantly, if not entirely, because the extreme downside risk can be caused by very small increases in supply or very small decreases in demand.

Contrary to the current market design, which values capacity above the administratively established minimum reliability requirement at zero, the Demand Curve will provide suppliers an opportunity to sell such capacity. This will eliminate the need for supply to wait for demand to exceed available resources before developing and thereby improve reliability. Nevertheless, the Demand

Curve gradually reduces the opportunities to sell additional capacity thereby protecting against the development and purchase of resources that do not provide a benefit.

The Demand Curve will encourage supply to be installed ahead of demand because improved reliability no longer results in a precipitous drop in market prices. This improves reliability as well as resource adequacy.

C. THE DEMAND CURVE WILL PROVIDE EFFICIENT PRICE SIGNALS

The Demand Curve will provide efficient price signals to the market and that in turn will encourage development of new efficient supply. The Reeder Analysis concluded that, over the long term, a sustainable market requires that overall market prices achieve equilibrium at the cost of a gas turbine. At various NYISO meetings and in his market analysis report, Dr. Patton indicated that the current price signals from the market are not adequate to support the investment in new facilities or even maintain the existing facilities in the New York Control Area. This is during a time when additional capacity is projected to be required.

In his presentation to the NYISO Management Committee (“MC”) entitled “Estimated Effects of the Proposed Capacity Demand Curves,” (“Patton Presentation”) Dr. Patton determined that over the long term, the prices in the combined NYISO markets will tend to converge to the cost required to induce new entry.⁵ The Patton Presentation therefore concludes the Demand Curve will cause a significant improvement in market price signals. Price signals are expected to change from being below the cost of new entry to converging on the cost to induce new entry. Moreover, these price signals will precede the need for additional capacity thereby providing adequate time for capacity to be

⁵ See Generally, Patton Presentation.

developed. Therefore, the Demand Curve will provide efficient price signals to resources in advance of reliability requirements, thereby ensuring long and short term reliability and resource adequacy.

D. THE DEMAND CURVE IS CONSISTENT WITH OTHER MARKET DESIGNS

Capacity provides reliability to the market. A market design that does not provide the proper price signal to capacity resources will not provide the reliability intended. In addition, capacity provides price protection against volatile energy prices. However, market participants are protected against such volatility with price caps as discussed earlier, even if capacity is not procured.

As noted above, the Demand Curve establishes a more efficient and less volatile market price signal for capacity thereby improving reliability. It is not in conflict with other market designs. At RAM Working Group meetings, the Demand Curve has been reviewed and it is considered to be a market design that can be adopted in some markets and not in others without causing a conflict. The Demand Curve is simply a substitute for the deficiency auction. Other major aspects of the NYISO capacity market design remain unchanged. Strip and Monthly auctions will continue to be conducted. Bilateral transactions will continue to be entered into. The only change is that all these auctions and transactions will now have more efficient price signals to base their behavior. This is by no means in conflict with SMD or other market designs.

III. CONCLUSION

Therefore, for the reasons stated above, KeySpan respectfully requests the Board deny the Appeals and file a section 205 petition with the Federal Energy Regulatory Commission (“FERC”) as soon as possible, but no later than March 21, 2003, requesting approval of the demand curve as of April 1, 2003, such that it could be implemented for the May 2003 spot market auction. The Board should request FERC waive its 60 day notice period and issue an order by April 23, 2003.

Dated: March 7, 2003

Respectfully submitted,

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